Comptroller's Handbook

Examination Process

Community Bank Supervision

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Office of the Comptroller of the Currency

Contents

Introduction

The Office of the Comptroller of the Currency's (OCC) *Comptroller's Handbook* booklet, "Community Bank Supervision," is prepared for use by OCC examiners in connection with their examination and supervision of community national banks and federal savings associations (collectively, banks).[1] When it is necessary to distinguish between them, national banks and federal savings associations (FSA) are referred to separately.

Examiners should use this booklet when examining banks in the OCC's community bank supervision program (i.e., a bank supervised out of one of the OCC's four district offices or the Special Supervision Division). Generally, banks with assets of $10 billion or less are characterized as community banks. The "Bank Supervision Process" booklet of the *Comptroller's Handbook* explains the factors considered when the OCC designates banks as community, midsize, or large. Each bank is different and may present specific issues. Accordingly, examiners should apply the information in this booklet consistent with each bank's individual circumstances.

The "Community Bank Supervision" booklet summarizes and expands upon the information in the "Bank Supervision Process" booklet and should be used in conjunction with that and other booklets of the *Comptroller's Handbook*, as well as the *FFIEC Information Technology Examination Handbook* and the *FFIEC Bank Secrecy Act/Anti-Money Laundering Examination Manual*.[2]

Related "Bank Supervision Process" Booklet Section(s)

Related sections of the "Bank Supervision Process" booklet of the *Comptroller's Handbook* are noted in boxes like this one throughout the booklet. Examiners should refer to these sections and use them in conjunction with the content in the "Community Bank Supervision" booklet. If *all* of the content of a section of this booklet mirrors the content in the "Bank Supervision Process" booklet, this box is not used.

The OCC's community bank supervision process is designed to

- determine the condition and risk profile of the bank.
- evaluate the overall integrity and effectiveness of the bank's risk management system by conducting periodic validation. Validation is accomplished by a combination of observation, inquiry, and testing.
- assess the bank's compliance with banking laws and regulations.
- communicate examination conclusions and deficiencies to bank management and directors in a clear and timely manner, and obtain commitments to correct deficiencies.
- verify and validate the effectiveness of corrective actions or, if actions have not been undertaken or accomplished, pursue timely resolution through supervisory or enforcement actions.

[1] This booklet is not used for the supervision of federal branches and agencies of foreign banking organizations. Refer to the "Federal Branches and Agencies Supervision" booklet of the *Comptroller's Handbook*.

[2] FFIEC is the Federal Financial Institutions Examination Council.

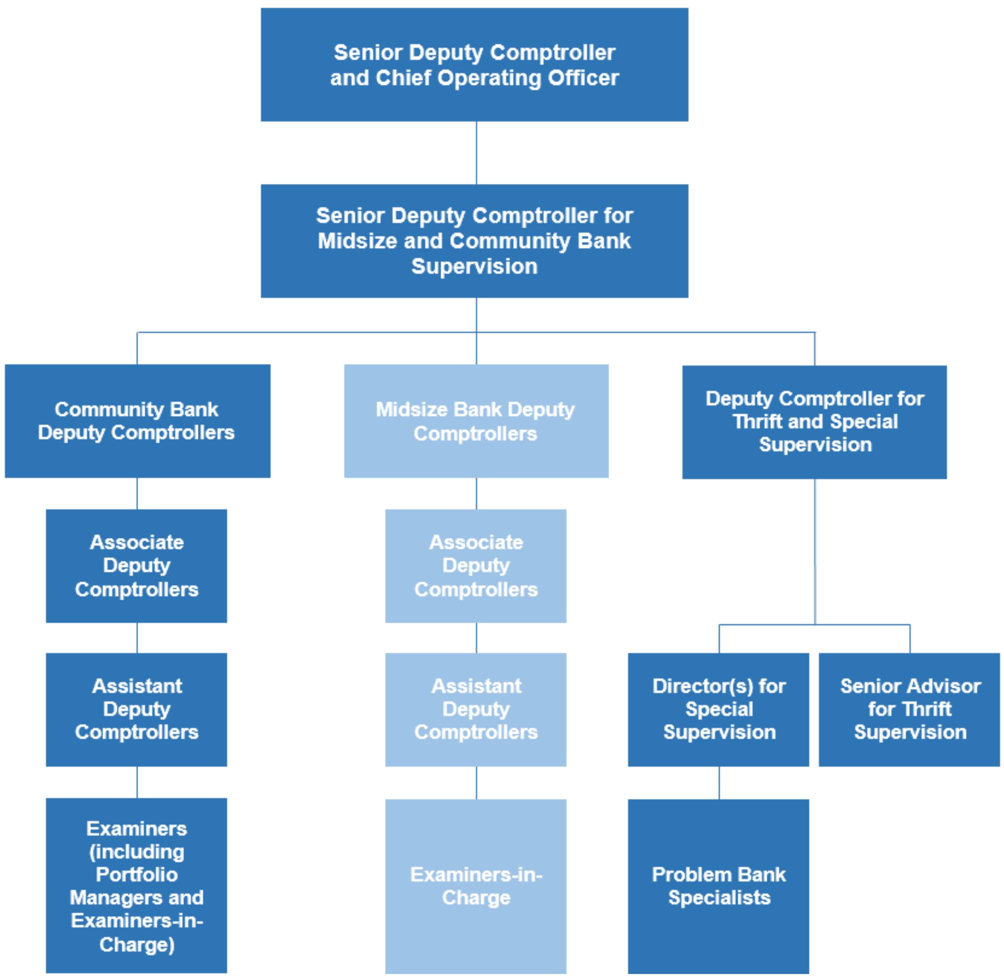
Community Bank Supervision Organizational Structure, Roles, and Responsibilities

> **Related "Bank Supervision Process" Booklet Section**
> - "Introduction" > "Bank Supervision Organizational Structure, Roles, and Responsibilities"

(Section updated in version 1.1)

This section provides an overview of the OCC's organizational structure, roles, and responsibilities pertaining to community banks (shown in figure 1).

Figure 1: The OCC's Organizational Structure for Community Bank Supervision



Note: The Midsize Bank Deputy Comptrollers management structure is lighter in tone in figure 1 because midsize banks are not in the scope of this booklet. Refer to the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for information regarding the OCC's organizational structure for midsize bank supervision.

Community banks are supervised under the Senior Deputy Comptroller for Midsize and Community Bank Supervision (MCBS), who reports to the Senior Deputy Comptroller and Chief Operating Officer (COO). The OCC's Large Bank Supervision department, Bank

Supervision Policy department, Economics department, and Office of Innovation also report to the COO.

The community bank deputy comptrollers include one for each district. There is also a Deputy Comptroller for Thrift Supervision and Special Supervision. Each district deputy comptroller is supported by one or more associate deputy comptrollers. The Deputy Comptroller for Thrift Supervision and Special Supervision is supported by one or more directors for special supervision and a Senior Advisor for Thrift Supervision. Each of the MCBS deputy comptrollers is responsible for the supervision of a portfolio of banks. The Deputy Comptroller for Thrift Supervision and Special Supervision is additionally responsible for overseeing the consistent integration and application of supervisory policies for FSAs into the OCC's mission.[3]

Assistant Deputy Comptroller

Related "Bank Supervision Process" Booklet Section

- "Introduction" > "Bank Supervision Organizational Structure, Roles, and Responsibilities" > "Assistant Deputy Comptroller (Community and Midsize Banks)"

An assistant deputy comptroller (ADC) oversees the supervision of a portfolio of community banks. ADCs also manage the team of examiners and supervision support staff that compose a field office. The director(s) for special supervision has similar supervision and oversight responsibilities as an ADC for a portfolio of problem banks but relies on an ADC to manage and assign examination staff. ADCs

- maintain an awareness of trends within the financial services industry and understanding of risks within his or her assigned portfolio of banks.
- approve appropriate supervisory strategies for individual banks.
- take actions within their authority to require banks to address deficiencies, including recommending enforcement actions when necessary.
- supervise personnel directly responsible for bank supervision.
- consider training and development needs of assigned personnel and how these will be met.
- direct planning, scheduling, and monitoring of supervisory activities for
  - effective use of resources.
  - consistency with identified priorities.
  - compliance with OCC policies.
- assign portfolio managers and examiners-in-charge (EIC) to banks or groups of banks, as applicable.
- review and concur with examination conclusions before conclusions are finalized.

[3] Pursuant to 12 USC 4b, "Deputy Comptroller for the Supervision and Examination of Federal Savings Associations," the Comptroller of the Currency shall designate a deputy comptroller, who shall be responsible for the supervision and examination of FSAs. The Deputy Comptroller for Thrift Supervision and Special Supervision fulfills the role of supervising and examining FSAs by overseeing the consistent application of supervisory policies for FSAs.

- ensure that the OCC's supervisory information systems reflect the current risk profiles and conditions of assigned banks.
- attend management exit meetings and board of directors meetings to promote consistent and effective communication. ADCs may appoint designees to attend exit meetings and board meetings, as appropriate.
- maintain communication with points of contact at other regulatory agencies and coordinate requests from other regulatory agencies (foreign and domestic) through the appropriate deputy comptroller or associate deputy comptroller. If another agency participates jointly in an examination, the ADC should ensure that (1) the supervisory strategy includes sufficient detail regarding each agency's roles and responsibilities so that unnecessary duplication can be avoided and (2) the activity is conducted in accordance with interagency agreements.
- countersign reports of examination (ROE).
- sign or countersign other correspondence, including supervisory letters.[4]

Portfolio Managers and Examiners-in-Charge

> **Related "Bank Supervision Process" Booklet Section**
>
> - "Introduction" > "Bank Supervision Organizational Structure, Roles, and Responsibilities" > "Portfolio Managers and Examiners-in-Charge"

Each community bank is assigned a portfolio manager who serves as the OCC's primary contact for bank management and the board on an ongoing basis. Portfolio managers should generally be commissioned examiners.[5] In their dialogues with bank management, portfolio managers develop a high level of understanding of banks' activities that guide the OCC's supervisory strategy for each bank. Portfolio managers understand the local economy and operating conditions and risks in banks' markets and can discuss recently implemented or proposed regulations, trends in current examination findings, and other current topics. OCC specialists provide assistance to portfolio managers as necessary.

The appropriate ADC may assign supervisory responsibility for a community bank to a noncommissioned examiner who is supervised by a commissioned examiner or the ADC. Appointing noncommissioned examiners to acting portfolio manager or acting EIC roles can help examiners develop skills and promotes efficient and effective use of OCC resources. A commissioned examiner or ADC supervising a noncommissioned acting EIC or acting portfolio manager must

- review the accuracy of the examiner's work before findings are communicated to bank management.

[4] In some cases, this may be delegated to a portfolio manager, an EIC, or another commissioned examiner.

[5] Refer to the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for more information about commissioned bank examiners.

- attend exit and board meetings with the examiner to provide for consistent and effective communication.
- sign ROEs and supervisory letters.

A community bank's portfolio manager may also be the EIC of the bank's examination(s), or the EIC may be another commissioned examiner. The EIC is responsible for coordinating and overseeing an examination. The portfolio manager or EIC

- maintains an up-to-date understanding of the core knowledge, condition, and risk profile of each assigned bank.
- identifies risks and responds in an appropriate and timely manner.
- considers the risks posed by each significant line of business within the bank or company.
- maintains responsibility for ongoing supervision of the bank and oversees the execution of examination plans. The portfolio manager or EIC must obtain approval from the supervisory office to materially change examination activities outlined in the supervisory strategy and must document the rationale for such changes in the OCC's supervisory information systems.
- reviews and concurs with examination conclusions before conclusions are finalized or submitted to the appropriate signer for review.
- updates the OCC's supervisory information systems to reflect the bank's current risk profile and condition.
- maintains ongoing and effective communication with bank management and the board.
- keeps the supervisory office informed about the status of each assigned bank.
- consistent with business unit or supervisory office procedures, establishes and maintains points of contact with domestic and foreign banking supervisors and other regulatory agencies, as appropriate. Examiners should work with these points of contact to supervise the consolidated entity by facilitating the exchange of necessary information, coordinating supervisory activities, and communicating critical issues to the appropriate regulatory agency. The supervisory office, rather than the portfolio manager or EIC, may establish and maintain points of contact with other regulatory agencies.
- implements OCC and supervisory office directives.
- takes actions within his or her authority to require banks to address deficiencies, or recommends such actions to the supervisory office.[6]
- follows up on bank management's actions to address deficiencies.
- follows up on outstanding enforcement actions by determining whether the bank is in compliance with the action and by assessing bank management and the board's effectiveness in correcting the deficiencies.[7]

[6] If the portfolio manager or EIC has concerns about activities subject to the primary supervision of another regulator, he or she should contact the appropriate ADC or deputy comptroller to coordinate the supervisory response. Refer also to appendix A of the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for information regarding functionally regulated affiliates.

[7] Refer to the "Enforcement Actions" section of this booklet for more information.

Supervisory Office

Related "Bank Supervision Process" Booklet Section

- "Introduction" > "Bank Supervision Organizational Structure, Roles, and Responsibilities" > "Supervisory Office"

The OCC supervisory office supports and oversees the portfolio manager and EIC. For community banks, the supervisory office includes the ADC (or director for special supervision) and the ADC Analyst. Examiners should follow internal OCC processes for delegations of authority.

Examination Authority and Full-Scope, On-Site Examination Requirement

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement"

(Section updated in version 1.1)

The OCC examines banks pursuant to the authority conferred by 12 USC 481 (national banks), 12 USC 1463 (FSAs), 12 USC 1464 (FSAs), and the requirements of 12 USC 1820(d).[8] The frequency of examinations of insured depository institutions is prescribed by 12 USC 1820(d). The OCC applies this statutory examination requirement to all types of banks (federal branches and agencies excepted), regardless of Federal Deposit Insurance Corporation (FDIC)-insured status, in 12 CFR 4.6, "Frequency of Examination of National Banks and Federal Savings Associations." Banks must receive a **full-scope, on-site examination** every 12 or 18 months. The examination frequency is known as the **supervisory cycle**. Banks must receive a full-scope, on-site examination at least once during each 12-month period, although the OCC may extend the supervisory cycle to 18 months under certain conditions. The OCC has discretion to extend the examination cycle only of banks meet all of the following criteria:[9]

- The bank has less than $3 billion in total assets.
- The bank is well capitalized as defined in 12 CFR 6, "Prompt Corrective Action."
- At its most recent examination, the OCC
  - assigned the bank a rating of 1 or 2 for management under the CAMELS[10] rating system, and
  - assigned the bank a composite rating of 1 or 2 under the CAMELS rating system.
- The bank is not subject to a formal enforcement proceeding or order by the OCC, Federal Reserve System, FDIC, or former Office of Thrift Supervision (OTS).
- No person acquired control of the bank during the preceding 12-month period in which a full-scope, on-site examination would have been required.

[8] Refer also to 12 USC 1467(h) (FSAs) and 12 USC 1468b (FSAs).

[9] Refer to 12 USC 1820(d)(4) and 12 CFR 4.6.

[10] A bank's composite rating under the Uniform Financial Institutions Rating System (UFIRS), or CAMELS, integrates ratings from six component areas: capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to market risk.

Types of Supervisory Activities

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Types of Supervisory Activities"

Supervisory activities are the various examination and supervision activities that are conducted throughout a bank's supervisory cycle. The OCC's approach to community bank supervision also stresses the importance of determining and validating the bank's condition during the supervisory cycle. The process is flexible, and activities can be completed through different means. Although on-site activities are essential to supervision, parts of supervisory activities, including the core assessment, may be effectively performed away from the bank.[11]

The scheduling of supervisory activities should maximize efficiency and effectiveness of the supervisory process and should be appropriate for the bank's size, complexity, risk profile, and condition. For example, if an accounting firm or other third party does internal audit work for a number of banks in an area, it may be more efficient to review the firm's work papers as part of a targeted supervisory activity than to review each bank's audit work papers during its on-site examination. Examiners may want to coordinate such reviews with other field offices whose banks employ the same third party or firm for the same purpose. Targeted reviews in other examination areas also provide scheduling flexibility when a specific area of examination expertise is needed. In addition, horizontal reviews (conducting coordinated reviews of particular functional areas across multiple institutions) are being performed more frequently, and use of this approach is expected to continue because it is an effective tool in the supervisory process

Full-Scope Examinations

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Types of Supervisory Activities" > "Full-Scope Examinations"

A **full-scope, on-site examination**[12] must consist of examination activities performed during the supervisory cycle that

[11] Refer to the "Planning" section of this booklet for more information about on-site versus off-site examination work.

[12] The full-scope, on-site examination is required by 12 CFR 4.6.

- satisfy the core assessment[13] and are sufficient in scope to assign or confirm a bank's regulatory ratings, except CRA ratings.[14]
- result in conclusions about a bank's risk profile.
- review the bank's BSA compliance program.
- assess the bank's compliance with the national flood insurance program, if the bank is an insured depository institution.[15]
- include on-site supervisory activities.[16]
- conclude with the issuance of an ROE.[17]

For many community banks, the full-scope, on-site examination requirement is fulfilled by conducting one supervisory activity during the supervisory cycle in addition to **ongoing supervision (periodic monitoring)**. For some larger or more complex community banks, the full-scope, on-site examination is fulfilled by aggregating several supervisory activities.

Ongoing Supervision (Periodic Monitoring)

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Types of Supervisory Activities" > "Ongoing Supervision"

Ongoing supervision is the OCC's process for assessing risks and reviewing core knowledge about a bank on an ongoing basis. It is a key component of the OCC's risk-based supervision approach. Ongoing supervision conclusions can result in changes to the OCC's supervisory strategy, regulatory ratings, or risk assessment system (RAS) conclusions for a bank. Ongoing supervision for community banks is generally performed off-site from the bank, but may be performed on-site as appropriate.

Ongoing supervision for community banks is primarily conducted using the periodic monitoring section of the core assessment. Periodic monitoring is designed to identify changes in the bank's condition and risk profile and to review the bank's corrective action on concerns identified during previous supervisory activities. The depth and scope of monitoring activities vary based on the bank's size, complexity, risk profile, and condition, but in all

[13] Refer to the "Core Assessment" section of this booklet and the "Core Examination Overview and Procedures for Assessing the BSA/AML Compliance Program" section of the *FFIEC BSA/AML Examination Manual.*

[14] Refer to the "Regulatory Ratings" section of this booklet for an overview of the interagency rating systems.

[15] Refer to the "National Flood Insurance Program" section of the "Bank Supervision Process" booklet of the *Comptroller's Handbook* and 12 USC 1820(i), "Flood Insurance Compliance by Insured Depository Institutions."

[16] The extent of on-site examination work is flexible. Refer to the "Planning" section of this booklet for more information.

[17] Refer to the "Report of Examination" section of the "Bank Supervision Process" booklet of the *Comptroller's Handbook* booklet for ROE requirements.

cases examiners must complete some level of supervision at least quarterly. Ongoing monitoring allows examiners to modify supervisory strategies in response to changes in a bank's risk profile and respond knowledgeably to bank management's questions. Periodic monitoring makes supervision more effective and on-site activities more focused.

The timing of periodic monitoring activities is driven by the OCC's supervisory objectives for the bank rather than predetermined calendar dates. Although the timing of these activities should be risk-based, there is a presumption that periodic monitoring will occur at least quarterly and include contact with bank management. Each bank's supervisory strategy outlines, in detail, the specific monitoring activities that will be performed and the timing of those activities.[18]

The objectives of periodic monitoring include the following:

- Identifying significant (actual or potential) changes in the bank's condition or risk profile.
- Ensuring the validity of the supervisory strategy.
- Following up on outstanding deficiencies (e.g., matters requiring attention [MRA], violations of law or regulation, or enforcement actions).
- Promoting efficiencies during on-site activities.

The specific objectives of periodic monitoring for a particular bank are determined by the portfolio manager in consultation with the supervisory office and are based on knowledge of the bank's condition and risks. In some instances, periodic monitoring may be as limited as a brief phone call to bank management or a review of bank financial information and any correspondence from the bank. In other instances, a bank's condition or risk profile may warrant more in-depth periodic monitoring and could include a comprehensive analysis of various CAMELS/ITCC[19] components or a visit to the bank. The ADC and the portfolio manager are jointly responsible for determining the depth and breadth of activities needed to achieve supervisory objectives.

The bank's assigned portfolio manager is responsible for conducting periodic monitoring. The supervisory office may assign periodic monitoring to an examiner other than the portfolio manager when necessary.

[18] Periodic monitoring generally should not be conducted during the same quarter or using the same financial "as of" date as a full-scope, on-site examination. For example, banks with a 12-month supervisory cycle will generally have three periodic monitoring activities during their supervisory cycle, whereas banks with an 18-month supervisory cycle will generally have five periodic monitoring activities during their supervisory cycle.

[19] ITCC represents the specialty areas of IT, trust, consumer compliance, and CRA. The OCC must perform a CRA evaluation to change a bank's CRA rating.

Target Examinations

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Types of Supervisory Activities" > "Target Examinations"

Target examinations may focus on one particular product (e.g., credit cards), function (e.g., audit), risk (e.g., operational risk), or CAMELS/ITCC component (e.g., asset quality), or may cover specialty areas (e.g., municipal securities dealers). Examiners may use the core assessment, expanded procedures, or verification procedures to conduct target examinations, as appropriate depending on the circumstances.

The CRA evaluation of most community banks is conducted as a target examination because a bank's CRA evaluation cycle is not the same as its supervisory cycle. Banks subject to an enforcement action generally receive a target examination for examiners to assess the bank's compliance with the action, typically around the midpoint of the bank's supervisory cycle.

A target examination alone does not fulfill all of the requirements of the full-scope, on-site examination but may fulfill a portion of the requirements. Target examinations are not as common in community banks, particularly in small, non-complex community banks, as they are in midsize or large banks. Conclusions from target examinations generally are communicated to the bank in supervisory letters. CRA conclusions are documented in performance evaluations.

Specialty Area Considerations

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Specialty Area Considerations"

Specialty areas consist of information technology (IT), asset management, BSA/AML, consumer compliance, CRA, and municipal and government securities dealers. Examination frequencies and scopes of some specialty areas are influenced by statutory mandates, interagency commitments, or OCC policy. The OCC's approach to community bank supervision includes assessing all bank activities under one supervisory strategy for each bank. With this approach, the ADC has responsibility for all supervisory activities, including safety and soundness, IT, asset management, and consumer compliance. For most community banks, the examinations for safety and soundness areas (i.e., CAMELS) and specialty areas are conducted during one supervisory activity. A benefit of this approach is that the coordination of supervisory activities minimizes duplication of effort and leverages resources in the supervisory process. For example, internal controls and audit may be reviewed once for all bank areas, rather than at different times for separate safety and soundness, IT, asset management, and compliance examinations.

Refer to the “Bank Supervision Process” booklet of the *Comptroller’s Handbook* for specialty area information. (Updated in version 1.1)

Regulatory Ratings

Related “Bank Supervision Process” Booklet Sections

- “Examination Authority and Full-Scope, On-Site Examination Requirement” > “Regulatory Ratings”
- “Uniform Financial Institutions Rating System (Commonly Known as CAMELS)”
- “Uniform Rating System for Information Technology”
- “Uniform Interagency Trust Rating System”
- “Uniform Interagency Consumer Compliance Rating System”
- “Community Reinvestment Act Rating System”

The OCC uses the uniform interagency rating systems adopted by the FFIEC to assign bank ratings. The CAMELS composite and component ratings, and all applicable specialty area ratings, are formally communicated to the bank’s board and management in the ROE or other formal written communication (e.g., a supervisory letter). The contents of the OCC’s formal written communications, including regulatory ratings, are confidential, except for the bank’s CRA performance evaluation.[20] The CAMELS rating system and RAS are used together during the supervisory process to document a bank’s condition and resilience.

A bank’s composite rating under the Uniform Financial Institutions Rating System (UFIRS), or CAMELS, integrates ratings from six component areas: capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to market risk. Evaluations of the component areas take into consideration the bank’s size and sophistication, the nature and complexity of its activities, and its risk profile. Bank management’s ability to identify, measure, monitor, and control the bank’s risks is also taken into account when assigning each component rating. Component ratings are assigned for the specialty areas of ITCC.

Composite and component ratings range from 1 to 5, except for the CRA rating, which is descriptive rather than numerical. A 1 is the highest rating and represents the least supervisory concern, indicating the strongest performance and risk management practices relative to the bank’s size, complexity, and risk profile. A 5 is the lowest rating and represents the greatest supervisory concern, indicating the most critically deficient level of performance and risk management practices relative to the bank’s size, complexity, and risk profile.

[20] Refer to 12 CFR 4, “Organization and Functions, Availability and Release of Information, Contracting Outreach Program, Post-Employment Restrictions for Senior Examiners,” and the “Disclosure of Ratings” section of the “Bank Supervision Process” booklet of the *Comptroller’s Handbook.*

Risk Assessment System

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Risk Assessment System"

(Section updated in version 1.1)

From a supervisory perspective, risk is the potential that events will have an adverse effect on a bank's current or projected financial condition[21] and resilience.[22] The RAS is a concise method of communicating and documenting conclusions regarding eight risk categories: credit, interest rate, liquidity, price, operational, compliance, strategic, and reputation. These categories are not mutually exclusive. Any product or service may expose a bank to multiple risks. Risks also may be interdependent and may be positively or negatively correlated. Examiners should be aware of and assess the effect of this interdependence. Examiners draw conclusions regarding the quantity of risk, quality of risk management, aggregate risk, and direction of risk for each of the eight categories of risk:

- **Quantity of risk** is the level or volume of risk that the bank faces and is characterized as low, moderate, or high. The quantity of risk and quality of risk management should be assessed independently. The assessment of the quantity of risk should not be affected by the quality of risk management.
- **Quality of risk management** is how well risks are identified, measured, monitored, and controlled and is characterized as strong, satisfactory, insufficient, or weak.
- **Aggregate risk** is a summary conclusion about the level of supervisory concern. It incorporates assessments about the quantity of risk and the quality of risk management. (Examiners weigh the relative importance of each.) Examiners characterize aggregate risk as low, moderate, or high.
- **Direction of risk** is a prospective assessment of the probable movement in aggregate risk over the next 12 months and is characterized as decreasing, stable, or increasing. The direction of risk often influences the supervisory strategy, including how much validation is needed. If risk is decreasing, the examiner expects, based on current information, aggregate risk to decline over the next 12 months. If risk is stable, the examiner expects aggregate risk to remain unchanged. If risk is increasing, the examiner expects aggregate risk to be higher in 12 months.

The community bank RAS is designed to prospectively identify and measure the risks in a bank and to help examiners determine the depth and type of supervisory activities that are appropriate for each community bank. To effectively use the system, examiners consider the current condition of the bank and other factors that indicate a potential change in risk. Examiners should watch for early warning signs that the level of risk may rise. The RAS also helps examiners determine when they should expand the core assessment or require

[21] Financial condition includes impacts from diminished capital and liquidity. Capital in this context includes potential impacts from losses, reduced earnings, and market value of equity.

[22] Resilience recognizes the bank's ability to withstand periods of stress.

corrective action by bank management. When making assessments, examiners use conclusions from the core assessment or expanded procedures and the RAS information in this booklet.

The presence of risk is not necessarily reason for concern. Examiners determine whether the risks a bank assumes are warranted by assessing whether the risks are effectively managed in a manner consistent with safe and sound banking practices. Generally, a risk is effectively managed when it is identified, measured, monitored, controlled, and reported. Bank management should report to the board on the bank's overall risk profile, including aggregate and emerging risks.[23] A bank should have the capacity to readily withstand the financial distress that a risk, in isolation or in combination with other risks, could cause.

If examiners determine that a risk is unwarranted (e.g., not effectively managed or supported by adequate capital), they must communicate to management and the board the need to mitigate or eliminate the unwarranted risk. Appropriate actions may include reducing exposures, increasing capital, or strengthening risk management practices.

Examiners should discuss RAS conclusions with bank management and the board during each supervisory cycle. If a change to the RAS warrants altering the bank's supervisory strategy or requires corrective action by bank management, examiners should formally communicate the rationale for the change to the bank and obtain commitments for any required corrective actions. These communications help the bank and the OCC reach a common understanding of the bank's risks, focus on the strengths and weaknesses of risk management, and achieve supervisory objectives.

Risk Management

The OCC recognizes that banking is a business of taking risks to be profitable. Banking risks historically have been concentrated in non-complex traditional banking products and services, but some community banks offer more complex or nontraditional products or services. Because of the diverse risks that community banks assume, no single risk management system works for all. Each bank should tailor its risk management system to its needs and circumstances. The sophistication of the risk management system should be proportionate to the risks present and the size and complexity of the bank. Regardless of the risk management system's design, each community bank's risk management system should do the following:

- **Identify risk:** Management and the board should recognize and understand existing risks and risks that may arise from new business initiatives. Risk identification should be a continual process and should occur at the transaction, portfolio, and bank or enterprise levels.
- **Measure risk:** Accurate and timely risk measurement is essential to effective risk management systems. A bank without a risk measurement system has limited ability to

[23] Refer to the "Corporate and Risk Governance" booklet of the *Comptroller's Handbook* for more information regarding risk management.

control or monitor risk levels. Measurement tools in community banks vary greatly depending on the type and complexity of the bank's products and services. For more complex products, risk measurement tools should be more sophisticated. Banks should periodically test their measurement tools to make sure they are accurate.[24]

- **Monitor risk:** Management's monitoring of risk levels should include timely review of risk positions and exceptions. Monitoring reports should be timely, accurate, and relevant and should be distributed to appropriate individuals (including the board) for action, when needed. Well-designed monitoring systems allow the board to hold management accountable for operating within established policies, limits, and risk appetite.
- **Control risk:** Management or the board should establish and communicate risk limits through policies, standards, and procedures that define responsibility and authority. These limits should serve as a means to control exposures to the various risks associated with the bank's activities. The limits should be tools that management can adjust when conditions or risk appetite changes. Banks should also have a process to authorize and document exceptions or changes to risk limits when warranted.

Examiners assess community banks' risk management systems to determine whether they are consistent with the bank's risk profile. For small community banks engaged in limited or traditional activities, risk management systems may be less formal in scope and structure. When examiners assess risk management systems, they consider the bank's policies, processes, personnel, and control systems.

- **Policies** are statements of actions adopted by a bank to pursue certain objectives. Policies guide decisions and often set standards (on risk limits, for example) and should be consistent with the bank's underlying mission, risk appetite, and core values. Policies should be reviewed periodically for effectiveness and approved by the board or designated board committee.
- **Processes** are the procedures, programs, and practices that impose order on a bank's pursuit of its objectives. Processes define how activities are carried out and help manage risk. Effective processes are consistent with the underlying policies and are governed by appropriate checks and balances (such as internal controls).
- **Personnel** are the bank staff and managers who execute or oversee processes. Personnel should be qualified and competent, have clearly defined responsibilities, and be held accountable for their actions. They should understand the bank's mission, risk appetite, core values, policies, and processes. Banks should design compensation programs to attract and retain personnel, align with strategy, and appropriately balance risk-taking and reward.
- **Control systems** are the functions (such as internal and external audits, loan review, and quality assurance) and information systems that bank managers use to measure performance, make decisions about risk, and assess the effectiveness of processes and personnel. Control functions should have clear reporting lines, sufficient resources, and appropriate access and authority. Management information systems (MIS) should provide timely, accurate, and relevant feedback.

[24] Refer to OCC Bulletin 2011-12, "Sound Practices for Model Risk Management: Supervisory Guidance on Model Risk Management."

For more information on risk management, refer to the “Corporate and Risk Governance” booklet of the *Comptroller’s Handbook.*

Relationship Between the RAS and the Regulatory Ratings

Related “Bank Supervision Process” Booklet Section

- “Examination Authority and Full-Scope, On-Site Examination Requirement” > “Risk Assessment System” > “Relationship Between the RAS and Regulatory Ratings”

The RAS is used in conjunction with CAMELS and other regulatory ratings during the supervisory process to evaluate a bank’s financial condition and resilience. The RAS provides both a current (aggregate risk) and a prospective (direction of risk) view of the bank’s risk profile that examiners incorporate when assigning regulatory ratings. For example, under the RAS, examiners may assess credit risk in a bank with insufficient risk management practices and increasing adverse trends as “moderate and increasing” or “high and increasing.” If the component rating for asset quality does not reflect the quality of risk management identified in the credit RAS, examiners should consider whether changing the component rating is warranted. Additionally, examiners consider their assessments of risk management practices for each of the risk categories when assigning management component ratings.

Risk-Based Supervision Approach

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach"

The OCC's supervisory process for all community banks is ongoing and focuses on the bank's ability to effectively manage risk. Risk-based supervision focuses on evaluating risk, identifying material and emerging concerns, and requiring banks to take timely corrective action before deficiencies compromise the bank's safety and soundness.

Because risk profiles of community banks are diverse, the OCC recognizes that effective and efficient supervision cannot be accomplished using a rigid set of examination procedures. Examiners evaluate risk using the OCC's RAS and tailor supervisory activities to the risks identified. Examiners must include periodic testing in supervisory activities to validate their risk assessments. The OCC's risk-based supervision approach consists of core knowledge, core assessment, expanded procedures, and verification procedures. These components are used together to assess a bank's risks and determine its regulatory ratings.

The extent of examination procedures performed depends on the bank's unique characteristics, including size, complexity, and risk profile, as well as examiner experience. When risks are high; when activities, products, and services are more complex; or when significant deficiencies are identified, examiners should expand the scope of supervisory activities to determine whether bank management has appropriately identified, measured, monitored, and controlled the bank's risks. The extent of the expansion in scope should vary depending on the impact that those risks, activities, products, services, or deficiencies may have on the overall risk profile or condition of the bank.

Core Knowledge

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Core Knowledge"

Core knowledge provides a foundation for assessing a bank's risks. It is a basic profile about the bank and its corporate structure, operations, products and services, culture, and risk appetite. It provides the OCC with the means to assess changes in a bank's activities, products, and services; identify changes in basic risk management controls; and identify broad supervisory issues. Core knowledge should be a snapshot of the most current information about the bank.

Core Assessment

> **Related "Bank Supervision Process" Booklet Section**
>
> - "Risk-Based Supervision Approach" > "Core Assessment"

Using the core assessment, OCC examiners draw conclusions about the bank's condition and risk profile, and adequacy of the bank's risk management systems. Core assessment establishes the minimum conclusions examiners must reach to assess risks and assign regulatory ratings. Examiners must reach these conclusions and assign regulatory ratings (e.g., CAMELS/ITC[25]) during the course of each supervisory cycle as part of fulfilling the full-scope, on-site examination requirement. When completing the core assessment, examiners should consider all supervisory activities conducted during the bank's supervisory cycle.

The community bank core assessment includes minimum objectives and other assessment objectives for each area for which examiners must draw conclusions. When examining low-risk areas, generally only the first (or minimum) objective under each section of the core assessment is completed. For areas that are not low-risk, examiners tailor the scope of the supervisory activity by selecting objectives and procedures from the "other assessment objectives" that are appropriate to the bank's complexity and risk profile. The other assessment objectives may be useful training information for less experienced examiners. (Updated in version 1.1)

Examiners should review the supervisory strategy to ascertain the recommended examination scope and make adjustments as appropriate in consultation with the EIC or supervisory office. For example, a low-risk community bank's supervisory strategy indicates that examiners should complete minimum objectives for all areas except asset quality because the bank has been experiencing growth in its credit card portfolio. After completing the minimum objective and selected other objectives from the core assessment for asset quality and identifying concerns, the EIC may then (with approval from the ADC) use selected expanded procedures from the "Credit Card Lending" booklet of the *Comptroller's Handbook*. By selecting from the types of procedures available, the EIC effectively focuses the scope of the examination on areas of highest risk.

Supervision requires periodic testing and validating of every bank's control systems—audit, loan review, and other control functions—to determine their effectiveness. Even when an area is consistently identified as low risk, examiners should periodically expand the scope of supervisory activities beyond the minimum objectives to determine whether supervisory concerns or issues are present and to determine whether control systems continue to be effective. Expansion in scope of supervisory activities or baseline testing does not mean that every area of the bank gets examined with expanded procedures. Expanding the scope should be used to confirm that the existing risk assessment is accurate.

[25] ITC represents the specialty areas of IT, trust, and consumer compliance.

The ADC is responsible for overseeing and approving when and to what extent periodic expansion in scope is appropriate for each low-risk area. In addition, expanded reviews and procedures may be appropriate in larger community banks; when banks engage in more complex operations; when the OCC conducts training assignments; when assignments are being completed by less-experienced examiners; and in other situations that benefit from increased testing and validation, as determined by the EIC and ADC.

Examiners must use judgment in documenting the core assessment. Examiners should include as work papers only those documents necessary to support the scope of the supervisory activity, significant conclusions, ratings changes, or changes in a risk profile. In addition, documentation should clearly indicate which procedures were performed, and to what extent the procedures were performed (e.g., fully or partially).

Refer to the "Core Assessment" section of this booklet for the community bank core assessment.

Core Assessment—Minimum Objectives

The core assessment's minimum objectives are required to be completed for all banks at least once per supervisory cycle, except for areas that are not applicable (for example, the asset management core assessment is not completed for banks that do not engage in asset management activities). The OCC has determined that these objectives are sufficient to effectively complete the required supervisory activities in low-risk areas and assign appropriate CAMELS/ITC ratings.

Minimum objectives guide examiners in determining whether significant changes have occurred in business activities, risk profile, management performance, or condition of a low-risk area from the previous supervisory cycle. If no significant changes in the bank's risk profile are identified after completion of the minimum objectives, generally no further work is required. If examiners identify supervisory concerns, however, the EIC, with approval from his or her ADC, has the flexibility to expand the scope of the supervisory activities by completing other objectives from the core assessment or expanded procedures as appropriate.

Core Assessment—Other Assessment Objectives

For areas not identified as low risk, or as otherwise outlined in the supervisory strategy, examiners should complete other selected objectives from the core assessment consistent with the bank's risks, complexity, and level of supervisory concern. The other objectives in the core assessment contain detailed procedures or clarifying steps. Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed. Experienced examiners can simply summarize their conclusions under each objective, consistent with the bank's condition and risk profile. For less-experienced examiners, the procedures provide additional details to help them fulfill the objectives. (Updated in version 1.1)

Expanded Procedures

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Expanded Procedures"

Expanded procedures contain detailed steps for examining specialized activities or products that warrant extra review beyond the core assessment. These procedures are found in other booklets of the *Comptroller's Handbook*, the *FFIEC BSA/AML Examination Manual*, or the *FFIEC IT Examination Handbook*, or may be conveyed separately in an OCC bulletin. Examiners determine which expanded procedures to use, if any, during examination planning or after drawing preliminary conclusions during the core assessment. (Updated in version 1.1)

Verification Procedures

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Verification Procedures"

Verification procedures are designed to guide verification of the existence or proper recordation of assets or liabilities, or test the reliability of financial records. Examiners may perform verification procedures, or may direct the bank to engage a third party to conduct verification, in cases where significant, unresolved safety and soundness concerns may materially affect a bank's financial condition.[26] Refer to the "Bank Supervision Process" booklet for a list of situations in which verification procedures should be used. (Updated in version 1.1)

Supervisory Process

Related "Bank Supervision Process" Booklet Section

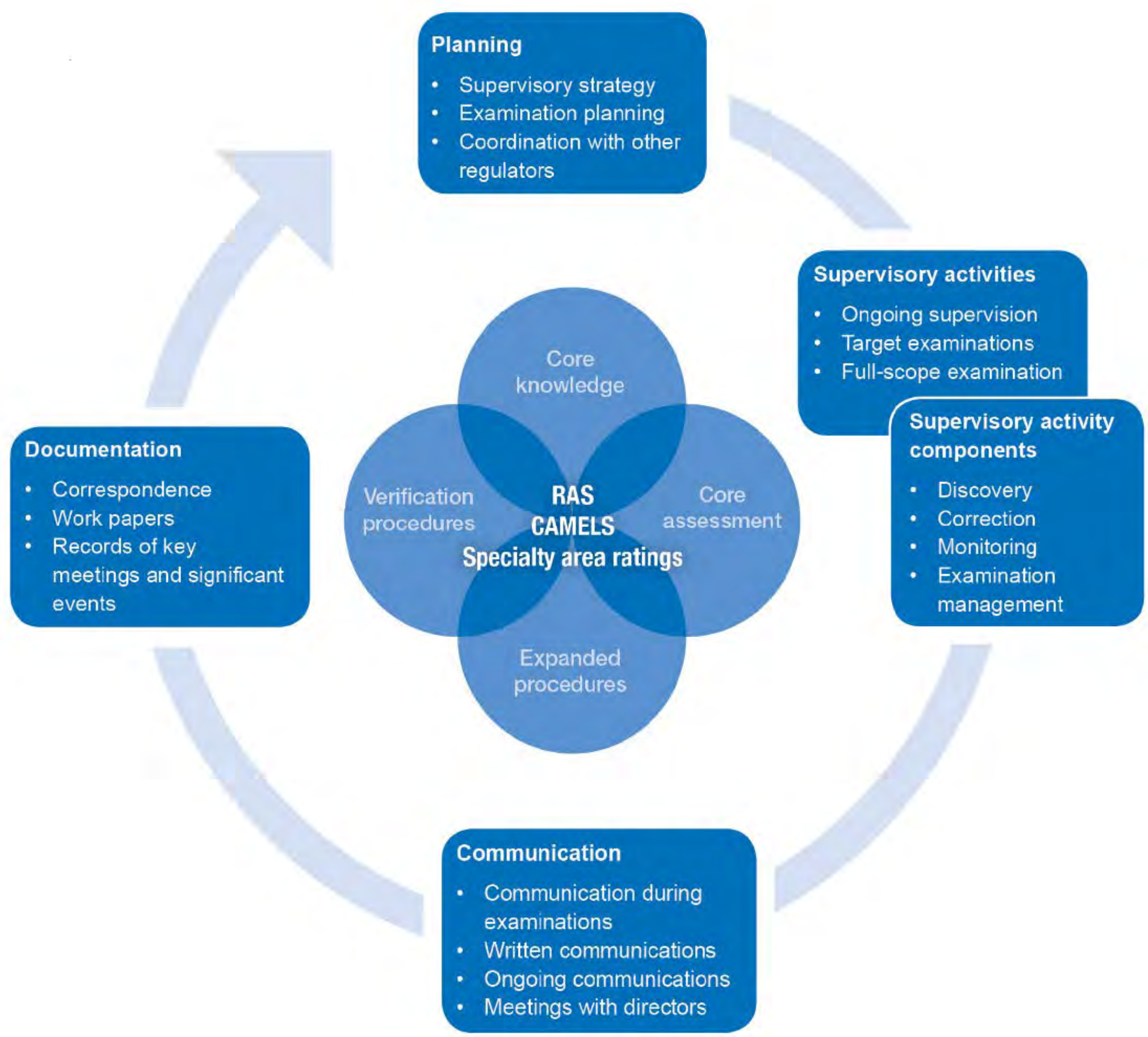
- "Risk-Based Supervision Approach" > "Supervisory Process"

Community bank supervision is an ongoing process. The supervisory process includes planning, supervisory activities, communication, and documentation as illustrated in figure 2.

[26] When the OCC directs the bank to engage a third party to conduct verification, it generally does so within the OCC's enforcement action policy. Refer to the "Enforcement Actions" section of this booklet for more information.

The elements of the OCC's risk-based supervision approach discussed earlier in this booklet are integrated throughout the supervisory process.

Figure 2: Supervisory Process



The supervisory process for community banks is designed to achieve the following objectives:

- Apply the OCC's risk-based supervision approach consistently throughout the community bank supervision process by tailoring supervisory strategies that integrate all examining areas to the risk profile of each community bank.
- Ensure that the ADC is responsible for the supervision of the bank and is accountable for the development and execution of appropriate integrated risk-based strategies.
- Define minimum conclusions that examiners must reach during the supervisory cycle, while providing the flexibility to vary the amount of supporting detail or volume of work.
- Comply with statutory requirements for full-scope examinations.

- Provide direction for less-experienced examiners through detailed procedures to be used, as needed, to reach key conclusions and objectives. (Updated in version 1.1)

Planning

Related "Bank Supervision Process" Booklet Section
• "Risk-Based Supervision Approach" > "Supervisory Process" > "Planning"

Planning is essential to effective supervision and occurs throughout a bank's supervisory cycle. Planning requires careful and thoughtful assessment of a bank's current and anticipated risks (e.g., examiners should assess the risks of both existing and new banking activities).[27] Planning consists of three primary components—supervisory strategy, examination planning, and coordination with other regulators (as applicable).

Supervisory Strategy

Related "Bank Supervision Process" Booklet Sections
• "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Specialty Area Considerations" • "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Assessment of Audit Functions" • "Risk-Based Supervision Approach" > "Supervisory Process" > "Planning" > "Supervisory Strategy"

The supervisory strategy is the OCC's detailed supervisory plan for each bank that outlines supervisory objectives, supervisory activities, and work plans. The portfolio manager or EIC develops the supervisory strategy in advance of each supervisory cycle in collaboration with other OCC personnel, including the supervisory office and subject matter experts, as appropriate, and the ADC approves the strategy.

Supervisory strategies are unique to each bank. The strategy integrates all supervisory activities planned for the supervisory cycle and quantifies the necessary examiner resources (e.g., work days and experience level) to complete the identified activities. Reviews of areas that affect more than one examination area (e.g., internal controls and audit) should be planned in a manner that will avoid duplicative examination work. Strategies are developed for three supervisory cycles and are dynamic documents that are updated as needed throughout the supervisory cycle. Supervisory strategies are based on

- core knowledge, core assessment, RAS, regulatory ratings, and the supervisory history of the bank.
- statutory examination requirements.

[27] New banking activities may be either traditional activities that are new to the bank or activities new to the financial services industry. Refer to OCC Bulletin 2017-43, "New, Modified, or Expanded Bank Products and Services: Risk Management Principles," for more information about new, expanded, or modified bank products and services.

- the OCC's annual bank supervision operating plan.[28]
- supervisory priorities of the agency.
- economic conditions.
- banking industry trends.
- other examination guidelines (e.g., expanded procedures in the *Comptroller's Handbook, FFIEC IT Examination Handbook,* or *FFIEC BSA/AML Examination Manual*).

The following are the components of a supervisory strategy:

Supervisory objectives define the goals of supervision for the specific bank, based on its risk profile, and are the foundation for supervisory activities and work plans. Well-defined objectives promote focused and efficient supervisory activities. They also help the OCC apply supervisory policies and resources consistently and appropriately. The objectives should be clear, attainable, specific, and action-oriented.

Supervisory activities are the means of achieving supervisory objectives. Each activity must be linked to at least one objective. Activities must be sufficient, in aggregate, to meet the definition of a full-scope, on-site examination.[29] The type, depth, and frequency of activities should correspond to the level of risk in each bank and statutory requirements. Examiners should employ periodic baseline transaction testing to validate key control functions and systems, even for areas that are low risk.

At a minimum, the strategy for community banks must include completing the core assessment during the supervisory cycle. For areas of low risk, the scope of the planned supervisory activities generally consists of the minimum objectives. For areas of higher risk or supervisory concern, the strategy may direct examiners to complete other objectives beyond the minimum and may expand the examination beyond the core assessment (e.g., using expanded procedures or verification procedures). When determining the appropriate scope and depth of supervisory activities for a specific examination area, the portfolio manager should take into account the level of risk of the area to be reviewed and the potential impact that area would have on the bank as a whole.

Work plans outline the scope, timing, and resources needed to meet the supervisory objectives and activities. Information pertaining to resources needed should include the level of expertise and number of work days that the OCC needs to effectively supervise the bank.

Examiners should discuss strategies with bank management as the supervisory strategy is created and modified. The portfolio manager should discuss with bank management the scope of the supervisory strategy, including specific types of supervisory activities planned for the cycle. The portfolio manager or supervisory office should discuss the planned timing of supervisory activities with bank management.

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[28] The OCC's Committee on Bank Supervision issues an annual bank supervision operating plan that sets forth the OCC's supervision priorities and objectives.

[29] Refer to the "Full-Scope Examinations" section of this booklet for requirements of a full-scope, on-site examination.

To help examiners develop risk-based supervisory strategies for each community bank, the ADC, with input from the portfolio manager, characterizes the overall risk profile of each community bank as low, moderate, or high.[30] In addition to the overall risk profile, specific areas of the bank also are characterized as low, moderate, or high risk using the RAS. For example, a bank's overall risk profile could be moderate while specific areas or activities could be low or even high risk. The OCC's portfolio manager develops a supervisory strategy using this overall risk assessment, his or her knowledge of specific risks in the areas of the bank, the effectiveness of the bank's audit program, and the strength of the bank's internal controls and compliance risk management systems.

Examination Planning

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Planning" > "Examination Planning"

Planning extends beyond developing a supervisory strategy. Before starting a supervisory activity, the EIC plans the specific supervisory activity. The planning process for a specific activity continues until that activity is initiated. A request for bank information that examiners review is sent to bank management shortly before an activity is scheduled to begin. This request is based on the planned scope of the examination and specific bank characteristics detailed in the supervisory strategy.

The portfolio manager or EIC reviews the information that the bank submitted to determine whether to adjust supervisory strategy for that activity, and may contact bank management to ask questions or discuss certain items. For example, the most recent loan review report submitted by the bank may prompt the portfolio manager or EIC to reduce or increase the scope of the asset quality review. This final step in the planning process allows the portfolio manager or EIC to effectively allocate supervisory resources based on the most current information available.

The EIC should prepare a scope memorandum and provide it to the assigned examiners before the start of the supervisory activity. The scope memorandum provides background about the bank, outlines the scope of the review (or references the supervisory strategy), provides examiner assignments, includes expectations for examiner work products and deadlines, and provides logistical information such as the work location and dress code (i.e., business casual or business attire).

For more information, refer to the "Examination Planning" section of the core assessment in this booklet.

[30] High-risk banks typically include community banks with composite ratings of 3, 4, or 5.

Coordination With Other Regulators

Related "Bank Supervision Process" Booklet Sections

- "Introduction" > "Bank Affiliates and Related Organizations"
- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Specialty Area Considerations" > "Consumer Compliance"
- "Risk-Based Supervision Approach" > "Supervisory Process" > "Planning" > "Coordination With Other Regulators"
- "Risk-Based Supervision Approach" > "Supervisory Process" > "Planning" > "Communication"
- Appendix A, "Functional Regulation"

The community bank supervision process focuses on the individual bank. Depending on the scope of a bank's operations, examiners may need to coordinate with other regulators. Risk-based supervision requires examiners to determine whether the risks at an individual bank are satisfactorily managed or increased by the activities and condition of the entire banking organization. This approach recognizes that risks present in banks may be mitigated or increased by activities in related organizations. To perform a consolidated risk analysis, examiners may need to obtain information from affiliates or related organizations, review transactions flowing between banks and affiliates, and obtain information from other regulatory agencies or service providers. A functionally regulated affiliate is a bank affiliate (including a bank operating subsidiary) whose primary regulator is the U.S. Securities and Exchange Commission (SEC), a state insurance commissioner, or the U.S. Commodity Futures Trading Commission. Refer to the "Coordination With Other Regulators" section and appendix A of the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for information.

Supervisory Activity Components

Related "Bank Supervision Process" Booklet Sections

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Types of Supervisory Activities"
- "Risk-Based Supervision Approach" > "Supervisory Process" > "Supervisory Activity Components"

Supervisory activities, regardless of type, include discovery, correction (when applicable), monitoring, and examination management. The extent of these components during a given activity depends on the type of activity, nature and extent of risks, and existence of deficiencies. The nature and extent of examination management also depends on other factors, such as the number and experience of examiners assigned.

Refer to the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for detailed discussions of discovery, correction, and monitoring.

Discovery

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Supervisory Activity Components" > "Discovery"

Discovery is ongoing and dynamic. Discovery occurs during supervisory activities when examiners complete the core assessment and applicable expanded procedures, and during ongoing supervision. If concerns remain about the adequacy of the bank's audit program or internal controls, or the integrity of the bank's risk management system after completing expanded procedures, examiners should determine whether to expand the scope of the review by completing verification procedures.[31]

Through discovery, examiners gain a fundamental understanding of the bank by

- evaluating the bank's condition.
- identifying and quantifying risks.
- evaluating management's and the board's awareness and understanding of significant risks.
- assessing the quality of risk management.
- performing sufficient testing to verify the integrity of risk management systems (including internal and external audits, loan review, compliance review, and internal controls).
- identifying unwarranted levels of risk, deficient risk management practices, and the underlying causes of any deficiencies.

Examiners' evaluations and assessments form the foundation for future supervisory activities. Bank supervision is an ongoing process that enables examiners to periodically confirm and update their assessments to reflect current or emerging risks. This revalidation is fundamental to effective supervision.

Correction

Related "Bank Supervision Process" Booklet Sections

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Supervisory Activity Components" > "Correction"
- "Supervisory Actions"

Correction occurs during supervisory activities when examiners identify deficiencies requiring the bank to take corrective action or when examiners are following up on previously identified deficiencies. Examiners identify deficiencies and monitor their correction throughout the supervisory cycle. The OCC uses various supervisory actions,

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[31] Refer to the "Internal Control Questionnaires/Verification Procedures" booklet and other booklets of the *Comptroller's Handbook* for verification procedures.

including MRAs, citations of violations of laws or regulations, or enforcement actions to address banks' deficiencies. In the correction process, examiners obtain commitments from bank management to correct each deficiency.[32]

Once examiners have identified a deficiency and its potential cause,[33] the bank should use its resources to fully determine the extent of the deficiency. Examiners should not take on actions or burdens that are the bank's responsibility. In some cases, however, examiners may perform more in-depth evaluations or investigations of a bank's deficiencies. This may occur, for example, in failing banks, banks in which fraudulent activities are suspected, or banks with severe BSA/AML deficiencies.

The bank's plans for corrective actions should be communicated through action plans. Action plans detail steps or methods that management has determined will correct the root causes of deficiencies rather than symptoms. Bank management is responsible for developing and executing action plans. A bank's directors are expected to hold management accountable for executing action plans. Not all corrective actions required by the OCC of community banks require in-depth action plans. For non-complex corrective actions, management or the board's commitment(s) to specific actions may be confirmed verbally with the examiners and documented in the commitment section of the related MRA or violation write-up.

Monitoring

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Supervisory Activity Components" > "Monitoring"

Ongoing monitoring allows the OCC to respond in a timely manner to risks facing individual banks and the industry as a whole. It allows resources to be redirected to areas of increasing or emerging risk. Monitoring also provides a better focus for on-site examination activities.

The OCC's follow-up on deficiencies focuses on verifying execution of management's commitments or action plans and validating their success. When determining whether to take further action, examiners consider management or the board's responsiveness in recognizing the deficiency and formulating an effective solution. The OCC may use an enforcement action to require the bank to correct deficiencies.[34] The OCC's follow-up on outstanding deficiencies may occur during a supervisory activity (including periodic monitoring) or stand-alone review, depending on the timing and circumstances.

[32] Refer to the "Supervisory Actions" section of the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for more information.

[33] Examiners should determine the root cause of deficiencies when possible. In some cases, examiners will need to direct management to perform a root-cause analysis.

[34] Refer to the "Enforcement Actions" section of this booklet.

Examination Management

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Supervisory Activity Components" > "Examination Management"

The EIC is responsible for effective examination management and must provide an organized environment in which supervisory goals and objectives can be achieved within appropriate time frames. During the examination, examining staff must inform the EIC of preliminary conclusions, and the EIC must evaluate examiners' progress toward completing the supervisory objectives. As OCC representatives, the conduct of examiners during an examination must be professional.

Communication

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Communication"
- "Supervisory Actions"

The OCC is committed to continual, effective communication with the community banks that it supervises and with other regulators as appropriate. Communication includes formal and informal conversations and meetings, ROEs, supervisory letters, and other written materials. Regardless of form, communications should convey a consistent conclusion regarding the bank's condition. OCC communications must be professional, objective, clear, and informative. Examiners must not have communications with banks that could be perceived as suggesting that the examination process is in any way influenced by political issues or considerations. When the OCC is considering an enforcement action, examiners should use care in communications with the bank related to the potential enforcement action. Examiners should consult with the supervisory office and assigned legal counsel before meeting with the bank regarding a potential enforcement action.

Communication should be ongoing throughout the supervisory process and tailored to a bank's structure and dynamics. The timing and form of communication depend on the situation being addressed. Examiners should communicate with the bank's management and board as often as the bank's condition and supervisory findings require.

Communication During Examinations

Related "Bank Supervision Process" Booklet Sections

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Communication" > "Written Communication"
- "Supervisory Actions"
- "Other Supervisory Considerations"

Communication during examinations includes the following:

- **Entrance meetings with bank management:** The EIC meets with bank management at the beginning of an examination to
  - explain the scope of the examination, the role of each examiner, and how the examination team will conduct the examination.
  - confirm the availability of bank personnel during the examination.
  - identify communication contacts.
  - answer any questions.
- **Ongoing communications:** Ongoing communications and discussions with bank management allow examiners to obtain the information necessary to reach sound and accurate conclusions. Periodic meetings with bank management are essential during the examination. Discussion of key issues and preliminary findings prevents misunderstanding and allows bank management to provide more information. The EIC should communicate, as necessary, with the appropriate OCC supervisory office regarding examination progress.
- **Exit meetings with bank management:** After each examination activity is completed, the EIC holds an exit meeting with bank or company management. The EIC should indicate during the exit meeting whether information is preliminary or final. During the exit meeting, the EIC
  - discusses the OCC's findings and conclusions.
  - discusses deficiencies and obtains management's commitments for corrective action.
  - discusses the areas of greatest risk to the bank.
  - provides preliminary ratings and RAS conclusions, when applicable.
  - outlines plans for future supervisory activities, when possible.

Written Communication

Related "Bank Supervision Process" Booklet Sections

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Communication" > "Written Communication"
- "Supervisory Actions"
- "Other Supervisory Considerations" > "Disclosure of Ratings"
- "Report of Examination"

Written communication of supervisory activities and findings is essential to effective supervision. Written communication should focus management's and the board's attention on the OCC's major conclusions, including any supervisory concerns. This written record, along with other related correspondence, helps establish and support the OCC's supervisory strategy.

The OCC must provide the bank's board with an ROE every supervisory cycle. The ROE communicates the overall condition and risk profile of the bank, and it summarizes the examiner's activities and related findings conducted throughout the supervisory cycle. The OCC's policy is to mail the bank's ROE within 90 days (for 1- and 2-rated banks) or 120 days (if the bank is rated 3, 4, or 5) of the start of a full-scope examination. Examiners should detail deficient risk management practices and excessive risks, along with the corrective action to which the board or management has committed, in the ROE's MRA page or in other written communications.[35] Refer to the "Report of Examination" section of the "Bank Supervision Process" booklet for more detail on requirements for the ROE.

Examiners should communicate the results of activities conducted throughout the supervisory cycle as they occur (e.g., target examination conclusions or a change in rating that occurs during periodic monitoring). Results of activities communicated during the supervisory cycle should be summarized in the ROE issued at the end of the bank's supervisory cycle. Deficiencies and excessive risks must be promptly communicated to the bank when they are identified by either sending a written communication to the board or meeting with the board or management. The EIC should consult with the supervisory office and assigned legal counsel before including information regarding a potential enforcement action in written communication. The OCC sends written communication if it is

- issuing an MRA.
- citing violations of laws or regulations.[36]
- changing any composite or component CAMELS/ITC rating.
- changing an aggregate RAS assessment.
- providing the bank with a status update regarding a previously communicated MRA or violation of law or regulation (e.g., a concern in an MRA becomes past due, or a violation's status changes to pending validation).
- responding to correspondence from the bank.

During the supervisory cycle, the supervisory office may receive correspondence and other information from banks. Examiners should acknowledge receipt of bank correspondence within five days and send the full response as soon as practicable, but typically within no more than 30 days. If a full response is not possible within 30 days, examiners or the supervisory office should provide bank management or the board frequent updates regarding the status of the response and an expected resolution date.

Meetings With Directors

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Communication" > "Meetings With Directors"

The OCC maintains communication with boards throughout the supervisory cycle to discuss OCC examination results and other matters of mutual interest, such as current industry issues and emerging industry risks. The EIC meets with the board or an authorized committee that

[35] For specific information on MRAs, refer to the "Examination Conclusions and Closing" section of this booklet. (Footnote updated in version 1.1)

[36] Some violations may be communicated to management in a list outside of a formal written communication. Refer to the "Violations of Laws and Regulations" section of this booklet for more information.

includes outside directors after the board or committee has reviewed the ROE. If necessary, the OCC uses board meetings to discuss how the board should respond to supervisory concerns and issues.

Sometimes, an exit meeting with management can be combined with the board meeting (e.g., when examiners have no significant concerns and when travel time and costs favor it). Meetings with the board should be more frequent if examiners need to discuss supervisory concerns or other items of significance. The EIC and the ADC or a representative from the supervisory office should attend the board meeting. If the ADC does not attend a board meeting when examination results are discussed, he or she may attend an examination exit meeting with directors attending or a regularly scheduled board meeting at any time during the supervisory cycle. (Updated in version 1.1)

Before a board meeting, the EIC should discuss the agenda with the supervisory office to confirm that the meeting emphasizes the proper topics. The EIC and the supervisory office should also determine who will attend the board meeting on the OCC's behalf and the role of each attendee. If the examination was conducted jointly with another regulator, the supervisory office or EIC should invite a representative from that agency to participate in the board meeting.

The EIC should also discuss with senior bank management who should attend the board meeting on the bank's behalf and determine whether any guests of the board should attend. In certain serious situations, specific directors, management officials, or guests of the board should not attend the board meeting (or certain parts of the meeting). For example, when discussing specific insider issues, the insider involved should normally be excused from that discussion.

Documentation

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Documentation"

Documentation is an ongoing process throughout the supervisory cycle. Examiners must document their decisions and conclusions. Supervisory offices must also document actions the OCC takes with respect to individual banks, including decisions regarding enforcement actions, corporate applications, and other formal communications.

Documentation includes correspondence, ROEs, work papers, and records of key meetings and significant events. In most cases, work papers need not include all of the information reviewed during a supervisory activity. Generally, only those documents necessary to support the scope and conclusions of the supervisory activity should be retained as work papers. Examiners must abide by the OCC's information security policies when handling, storing, and disposing of sensitive bank examination work papers.

OCC's Supervisory Information Systems

Related "Bank Supervision Process" Booklet Section

- "Risk-Based Supervision Approach" > "Supervisory Process" > "Documentation" > "OCC's Supervisory Information Systems"

Examiners record and communicate narrative and statistical information about OCC-supervised institutions and their affiliates[37] in the agency's electronic supervisory information systems, which is primarily Examiner View for community banks. Other systems, such as the OCC's National Credit Tool (NCT), support Examiner View. The recorded information reflects the bank's current condition; the OCC's supervisory strategy for the bank, results of supervisory activities, and supervisory actions in response to deficiencies; and bank management's progress in correcting deficiencies. Using this information and data, OCC senior management can review the condition of supervised institutions and groups of institutions. Other federal banking regulators also have access to certain information, as appropriate, through various formats.

The EIC, the portfolio manager, and the supervisory office are responsible for ensuring that the electronic files for their assigned banks are accurate and up-to-date. For community banks, examiners should enter information under the appropriate charter number.

[37] OCC-supervised banks and their affiliates include banks, holding companies and affiliates, federal branches and agencies, and supervised service providers.

Supervisory Actions

Related "Bank Supervision Process" Booklet Sections

- "Supervisory Actions"
- "Report of Examination"

This section outlines the actions the OCC can take in response to a bank's deficiencies. Collectively, deficiencies include deficient practices and violations.

A deficient practice is a practice, or lack of practices, that

- deviates from sound governance, internal control, or risk management principles and has the potential to adversely affect the bank's condition, including financial performance or risk profile, if not addressed, or
- results in substantive noncompliance with laws or regulations, enforcement actions, or conditions imposed in writing in connection with the approval of any applications or other requests by the bank.

A violation of law or regulation is an act (or failure to act) that deviates from, or fails to comply with, a statutory or regulatory requirement. Violations are often the result of deficient practices.

The term "violations" collectively describes violations of laws, regulations, final agency orders, conditions imposed in writing, or written agreements.

Recommendations can be provided informally to bank management or the board as suggestions to enhance policies or as best practices. Recommendations do not require specific action by bank management or follow-up by examiners, and are not tracked in the OCC's supervisory information systems. Recommendations must not be included in the ROE or other formal written communication to the bank (e.g., supervisory letter). Examiners must not use a graduated process by first communicating a practice meeting the MRA criteria as a recommendation and escalating it to an MRA at a later date.

Matters Requiring Attention

Related "Bank Supervision Process" Booklet Sections

- "Supervisory Actions" > "Matters Requiring Attention"
- "Report of Examination"

The OCC uses MRAs to communicate concerns about a bank's deficient practices. Examiners must communicate such concerns to management and the board when the concerns are discovered and must not defer issuing MRAs pending bank management's efforts to address the concerns.

For consistent reporting, the OCC focuses on the concerns within the MRA, tracking them through their duration. The following Five Cs format is used to communicate an MRA:

- Concern
- Cause
- Consequence (of inaction)
- Corrective action
- Commitment

If bank management is unable to provide a corrective action plan during the examination, the examiner obtains a commitment from bank management to develop a board-approved plan and provide it to the OCC within 30 days of receipt of the formal written communication containing the MRA.

A concern is either “open” or “closed.” A concern is closed if the bank implements and the OCC verifies and validates the effectiveness and sustainability of the corrective action, or if the bank’s practices are no longer a concern because of a change in the bank’s circumstances.

Within the meaning of “open,” a concern may be categorized several ways in formal written communication to the board and management and for reporting purposes:

- New
- Repeat
- Self-identified
- Pending validation
- Escalated

When discussing MRAs, examiners must be clear with bank management and the board regarding the OCC’s supervisory concerns and expectations. Examiners must impress on the board its responsibility to provide oversight of management’s corrective actions. Failure to correct MRAs on a timely basis could provide the basis for enforcement actions. Therefore, banks should have a process for following up on MRAs. Likewise, examiners must include plans to follow up on MRAs in the supervisory strategies for individual banks.

For more information, refer to the “Matters Requiring Attention” and “Report of Examination” sections of the “Bank Supervision Process” booklet of the *Comptroller’s Handbook*.

Violations of Laws and Regulations

Related "Bank Supervision Process" Booklet Sections

- "Supervisory Actions" > "Violations of Laws and Regulations"
- "Other Supervisory Considerations"
  > "Suspected Criminal Violations"
  > "Information Received From an Outside Source"
- "Report of Examination"

A violation of law or regulation is an act (or failure to act) that deviates from, or fails to comply with, a statutory or regulatory requirement. Violations are often the result of deficient practices. Frequently, correcting violations alone does not address the deficient practices that may have led to the violations. When examiners identify a violation, they must also identify any deficient practices that contributed to violations. If bank management has not corrected deficient practices that caused or contributed to the violation, examiners must communicate the OCC's concern with these practices in an MRA.

Examiners must cite all OCC-identified violations to facilitate timely and effective corrective action by bank management or the board. Substantive OCC-identified violations must be cited in an ROE or supervisory letter, whereas less substantive violations may be cited in a separate document (e.g., a list provided to management during the exit meeting). Bank-identified violations must be cited in an ROE or supervisory letter in certain circumstances (e.g., the violation requires further investigation or has not been corrected), and examiners have discretion to include substantive bank-identified violations in an ROE or supervisory letter as they determine is warranted. Examiners should use judgment to determine if less substantive bank-identified violations should be cited in writing, and if so, cite them in a separate document provided to bank management or the board.

The OCC expects management to timely and effectively correct all violations regardless of how they are communicated. If management fails to correct a violation previously communicated in a separate document by the OCC, the violation should be included in the next ROE or supervisory letter.

The first time the OCC communicates a violation to a bank, the violation must be labeled with one or more of the following attributes:

- New
- Repeat
- Self-identified

Upon completing follow-up, examiners must determine whether to label a violation as past due, pending validation, or closed, as appropriate, and communicate the status of the violation to the bank.

For more information, refer to the "Violations of Laws and Regulations" and "Report of Examination" sections of the "Bank Supervision Process" booklet of the *Comptroller's Handbook*.

Enforcement Actions

Related "Bank Supervision Process" Booklet Sections

- "Supervisory Actions" > "Enforcement Actions"
- "Other Supervisory Considerations" > "Information Received From an Outside Source"
- "Report of Examination"

The OCC uses enforcement actions to require a bank's board and management to take timely actions to correct a bank's deficient practices or violations. The OCC typically first cites a violation or issues an MRA to address a bank's deficiencies. Violations, concerns in MRAs, or unsafe or unsound practices may serve as the basis for an enforcement action.

Enforcement actions can be either formal or informal. Examiners should consider an informal enforcement action when a bank's condition is sound, but deficiencies have not been corrected in a timely manner or escalation beyond the OCC's citation of a violation or documentation of a concern in an MRA is otherwise warranted. The board's agreement or acceptance of an informal enforcement action can be indicative of its commitment to correct identified deficiencies before they adversely affect the bank's condition. When a bank's deficiencies are severe, uncorrected, repeat, or unsafe or unsound, or negatively affect the bank's condition, the OCC may use formal enforcement actions to support the agency's supervisory objectives.

Pursuant to 12 USC 1818(s), "Compliance With Monetary Transaction Recordkeeping and Report Requirements," the OCC is required to issue a cease and desist order in certain BSA cases. Refer to OCC Bulletin 2007-36, "Bank Secrecy Act/Anti-Money Laundering: BSA Enforcement Policy," and OCC Bulletin 2016-6, "Bank Secrecy Act/Anti-Money Laundering: Process for Administrative Enforcement Actions Based on Noncompliance With BSA Compliance Program Requirements or Repeat or Uncorrected BSA Compliance Problems."

Once an enforcement action is in place, examiners must periodically assess the bank's compliance with the enforcement action. Written feedback must be provided to bank management and the board, and the assessment should be documented in the OCC's supervisory information systems.

For more information on enforcement actions, refer to OCC Bulletin 2018-41, "OCC Enforcement Actions: OCC Enforcement Action Policies and Procedures Manuals," and its attachment, Policies and Procedures Manual (PPM) 5310-3, "Bank Enforcement Actions and Related Matters." (Updated in version 1.1)

Civil Money Penalties

Related “Bank Supervision Process” Booklet Sections

- “Risk-Based Supervision Approach” > “Supervisory Process” > “Communication”
- “Supervisory Actions” > “Enforcement Actions” > “Civil Money Penalties”
- “Other Supervisory Considerations” > “Information Received From an Outside Source”

Civil money penalties (CMP) are a type of enforcement action that requires monetary payments to penalize a bank, its directors, or other persons participating in the affairs of the bank for violations,[38] unsafe or unsound practices, or breaches of fiduciary duty. CMPs may be used alone or in combination with other enforcement actions. The OCC may assess CMPs against a bank or an individual.

In addition, the OCC must assess CMPs if it finds that a regulated lending institution engaged in a pattern or practice of violations of certain requirements of the national flood insurance program.[39]

Examiners should propose CMPs for serious misconduct, including misconduct that is reckless, flagrant, willful, or knowing and that, because of its frequency or recurring nature, shows a general disregard for law or regulation, fiduciary duty, or safe and sound banking. Added consideration should be given to violations, breaches of fiduciary duty, or unsafe or unsound practices that occurred or continued in direct contravention of the bank’s policy guidelines, correspondence from the regulator, or audit reports.

For more information, refer to OCC Bulletin 2018-41 and its attachment, PPM 5000-7, “Civil Money Penalties.” (Updated in version 1.1)

Reprimand or Supervisory Letter

Related “Bank Supervision Process” Booklet Section

- “Supervisory Actions” > “Enforcement Actions” > “Civil Money Penalties” > “Reprimand or Supervisory Letter”

In certain cases, the issuance of a reprimand or a supervisory letter may be more appropriate than the assessment of a CMP. A reprimand is a strongly worded document used in lieu of a CMP when, for example, the CMP would be too small to justify spending resources required or when the individual or institution has recognized the supervisory problem and taken steps to correct it. A supervisory letter is generally used to call attention to a supervisory problem that is not severe enough to warrant a CMP. Reprimands and supervisory letters are

[38] The term “violation,” for the purpose of CMPs under 12 USC 1818(i), “Jurisdiction and Enforcement; Penalty,” is defined by 12 USC 1813(v), “Violation,” to include “any action (alone or with another or others) for or toward causing, bringing about, participating in, counseling, or aiding or abetting a violation.”

[39] Refer to 42 USC 4012a(f), “Civil Money Penalties for Failure to Require Flood Insurance or to Notify,” and 42 USC 4003(a)(10), “Regulated Lending Institution.”

discussed in more detail in OCC Bulletin 2018-41, and its attachment, PPM 5000-7. (Updated in version 1.1)

Conditions Imposed in Writing

Related "Bank Supervision Process" Booklet Section

- "Supervisory Actions" > "Conditions Imposed In Writing"

The OCC may impose conditions in connection with the approval of an application, notice, or other request by a bank if it determines that one or more conditions are necessary or appropriate for the approval to be consistent with applicable laws, regulations, or OCC policies. Conditions may be imposed, for example, to protect the safety and soundness of the bank, prevent conflicts of interest, or require the bank to provide for customer protections. Conditions imposed in writing are often used by the OCC in approvals of corporate applications and interpretive letter opinions on banks' requests to engage in permissible activities. These conditions are "conditions imposed in writing" within the meaning of 12 USC 1818 if the OCC's approval explicitly makes the conditions enforceable. These conditions remain in effect until the OCC removes them.

The OCC considers some conditions imposed in writing to be enforcement actions. Generally, the OCC does not consider conditions imposed in writing in connection with the approval of a bank's licensing filing[40] to be enforcement actions, regardless of whether they are conditions imposed in writing within the meaning of 12 USC 1818. Table 1 summarizes when the OCC generally considers conditions imposed in writing to be enforcement actions.

Table 1: Conditions Imposed in Writing as Enforcement Actions

<table>
<tr><th>Were the conditions imposed in connection with the approval of a bank's licensing filing?</th><th rowspan="5">and</th><th>Are the conditions "conditions imposed in writing" within the meaning of 12 USC 1818?</th><th rowspan="5">then</th><th>The OCC generally considers the conditions to be an enforcement action</th></tr>
<tr><td rowspan="2">Yes</td><td>Yes</td><td rowspan="2">No</td></tr>
<tr><td>No</td></tr>
<tr><td rowspan="2">No</td><td>Yes</td><td>Yes[a]</td></tr>
<tr><td>No</td><td>No</td></tr>
</table>

[a] Generally, when the OCC considers a condition imposed in writing within the meaning of 12 USC 1818 to be an enforcement action, the OCC publishes the condition in its monthly enforcement action press release.

Supervisory strategies for banks with outstanding conditions imposed in writing should include periodic assessments of the bank's ongoing compliance with the conditions.

[40] A "licensing filing" means an application, notice, or other request submitted to the OCC under 12 CFR 5, "Rules, Policies, and Procedures for Corporate Activities."

For more information on conditions imposed in writing, refer to OCC Bulletin 2018-41 and its attachment, PPM 5310-3, as well as the "General Policies and Procedures" booklet of the *Comptroller's Licensing Manual*. (Updated in version 1.1)

Other Supervisory Considerations

Related "Bank Supervision Process" Booklet Section

- "Other Supervisory Considerations"

Examiners should refer to the "Other Supervisory Considerations" section of the "Bank Supervision Process" booklet for information regarding the following topics:

- Disclosure of ratings
- Suspected criminal violations
- Information received from an outside source
- Bank appeals process
- OCC's Customer Assistance Group
- Quality assurance

Core Assessment

Using the core assessment, OCC examiners draw conclusions about the bank's condition and risk profile and the adequacy of the bank's risk management systems. The core assessment establishes the minimum conclusions examiners must reach to assess risks and assign regulatory ratings. The core assessment is risk-based. Risk considerations and references to the community bank RAS are noted throughout the core assessment.

Generally, each section has a minimum objective that examiners must meet to complete the core assessment. After reviewing the supervisory strategy and considering the bank's risk profile and outstanding supervisory issues, examiners should perform additional objectives and procedures as necessary to determine whether the bank's risk is appropriately managed. For banks or specific areas identified as low risk, completing minimum objectives in the core assessment should be sufficient to assess the bank's condition and risks. Examiners have the flexibility, if necessary, to expand the scope of the supervisory activity beyond the minimum objectives.

The core assessment comprises the following sections:

- Examination Planning
- Community Bank Periodic Monitoring
- Internal Controls and Audit
- Capital Adequacy
- Asset Quality
- Credit Underwriting Assessment – Overall Credit, Commercial Credit, Retail Credit
- Management
- Earnings
- Liquidity
- Investment Portfolio and Bank-Owned Life Insurance
- Sensitivity to Market Risk
- Information Technology
- Asset Management
- Bank Secrecy Act/Anti-Money Laundering
- Consumer Compliance
- Examination Conclusions and Closing

Examiners must use judgment in deciding how much work or supporting detail is necessary to complete the objectives under the core assessment.

Examination Planning

Introduction

> **Related "Bank Supervision Process" Booklet Section**
>
> - "Risk-Based Supervision Approach" > "Supervisory Process" > "Planning"

Planning for supervisory activities is crucial to effective risk-based supervision. This section is used to plan the supervisory activities conducted throughout the cycle. The following objectives should be completed at least once during the supervisory cycle. If significant supervisory activities are conducted separately, some objectives may be completed more than once during a supervisory cycle. The underlying procedures for each objective are optional. The objectives finalizing the scope for each area are included in other sections of the core assessment.

Objectives and Procedures

Objective 1: Review the bank's characteristics and the supervisory activity's preliminary scope and objectives.

1. Obtain and review the following:

   - Applicable regulatory agency reports (e.g., holding company reviews, ROEs for IT service provider(s), or shared application software reviews).
   - OCC information and documentation, including
     - supervisory strategy.
     - prior ROEs, with particular emphasis on outstanding MRAs, violations of law or regulation, or enforcement actions.
     - examination conclusions and work papers.
     - periodic monitoring conclusions and comments.
     - RAS conclusions.
     - financial reports (e.g., the Uniform Bank Performance Report [UBPR]) and applicable OCC reports or analytical tools.
     - customer complaint data from the OCC's Customer Assistance Group. When possible, examiners should review and leverage any analyses already performed (e.g., during the most recent periodic monitoring) to avoid duplication of effort.
     - OCC correspondence.
   - Other information deemed pertinent to the bank.

2. Discuss the preliminary examination scope and bank's risks with the portfolio manager and ADC.

Objective 2: Determine whether changes to the supervisory strategy are needed.

1. Contact bank management to discuss the following:

   - Preference for obtaining request letter information in digital form.
   - Activity's timing.
   - Activity's general scope and objectives.
   - General information about examiners' schedules, staffing levels, and when examiners are expected to be on-site at the bank.
   - Availability of key bank personnel during the activity.
   - Actual or planned changes in the bank's financial condition, including significant injection of capital and the bank's plans to deploy such capital.
   - Actual or planned changes in bank products, services, or activities, including areas of growth.
   - Actual or planned changes in bank management, key personnel, or operations.
   - Results of audit and internal control reviews and compliance reviews; follow-up required by bank management; and audit staffing.
   - Material changes to internal or external audit's schedule or scope.
   - Significant trends or changes in local economy or business conditions.
   - Broad economic and systemic trends affecting the condition of the federal banking system; this includes trends identified by the OCC's national or district risk committees.
   - Purchase, acquisition, or merger considerations.
   - Issues or changes to critical third-party service providers or third-party risk management process.
   - Issues or changes in technology, including operational systems, third-party technology service providers, critical software, internet banking, or plans for new products and activities that involve new technology.
   - Issues or changes in asset management lines of business.
   - Issues or changes regarding consumer compliance, CRA, or BSA/AML/Office of Foreign Assets Control (OFAC) systems.
   - Effects of, or changes in response to, new regulatory guidance.
   - Significant customer complaints and litigation.
   - Other issues that may affect risk profile.
   - Bank management's concerns about the bank or the OCC's supervision, including any areas that bank management would like the OCC to consider in the examination scope.

2. Review the bank's risk profile. Determine whether the OCC has identified specific areas as low or high risk. Assess the appropriateness of the current supervisory strategy for the bank. With the ADC's approval, modify the strategy as appropriate. Consider the following:

   - Information from bank management.
   - Findings from periodic monitoring activities.

- Discussions with the supervisory office.
- Supervisory cycle for CRA evaluations.

Objective 3: Prepare for the supervisory activity.

1. Coordinate the activity with other regulatory agencies, as necessary.

2. Designate assignments for examining staff.

3. Prepare a scope memorandum.

4. Send the bank a request letter that provides the following:

    - Activity start date.
    - Activity's scope and objectives.
    - Advance information the bank must provide to the examination team, including due dates for submission of requested items.
    - Information the bank must have available for examiners upon their arrival at the bank.
    - Name, address, and telephone number of the OCC contact.
    - Instructions for delivering digital files.

    Appendix A of this booklet is a standard request letter for community bank examinations. Examiners should customize the letter to reflect the supervisory activity's scope, the bank's risk profile, and the bank's operations. For expanded examinations of specialized areas, refer to appropriate booklets of the *Comptroller's Handbook*, the *FFIEC IT Examination Handbook*, and the *FFIEC BSA/AML Examination Manual*.

5. Generally within one week of the start of the activity, review the requested items and finalize the scope of the supervisory activity.

Objective 4: Conduct on-site planning meetings.

1. At the beginning of the supervisory activity, conduct an entrance meeting with the chief executive officer, appropriate members of senior management, board members, and board committees, as appropriate, to

    - explain the activity's scope, each examiner's role, and how the team conducts the activity.
    - confirm availability of bank personnel.
    - identify contacts for examining staff.
    - answer questions.

2. At the beginning of the supervisory activity, meet with examining staff to confirm the following:

   - Scope and objectives.
   - Work days.
   - Assignments and due dates.
   - Administrative duties.
   - Guidelines for contact and communication among the examining staff, bank management, and the supervisory office.

Community Bank Periodic Monitoring

Conclusion: The bank's risk profile (has/has not) changed and the supervisory strategy (is/is not) valid.

Introduction

Related "Bank Supervision Process" Booklet Sections

- "Examination Authority and Full-Scope, On-Site Examination Requirement"
  > "Types of Supervisory Activities" > "Ongoing Supervision"
  > "Assessment of Audit Functions" > "12 CFR 363 Annual Report Requirement"
  > "Risk Assessment System"
- "Risk-Based Supervision Approach"
  > "Supervisory Process" > "Supervisory Activity Components"
  > "Communication"
  > "Documentation"
- "Supervisory Actions"

Examiners may perform the following procedures during periodic monitoring. These procedures are provided as a guide for examiners. The portfolio manager should review the supervisory strategy and perform whichever procedures are appropriate, consistent with the bank's condition and risk profile.

In addition to the procedures selected from the first objective in this section, examiners should use the objective for de novo banks if the bank is a de novo.

Objectives and Procedures

Objective 1: Determine whether significant trends or events have changed the bank's risk profile or require changes to the supervisory strategy.

1. Review quarterly financial information using the UBPR, bank-supplied information, call reports, or applicable OCC reports or analytical tools for significant financial trends or changes. The financial review of low-risk banks should be very brief if examiners do not identify any anomalies.

   If the bank is subject to 12 CFR 363, "Annual Independent Audits and Reporting Requirements," determine whether the bank submitted its annual report to the OCC since the last supervisory activity. If so, conduct a review of the annual report if this has not yet been conducted. Refer to the "12 CFR 363 Annual Report Review" section of the *Bank Supervision Process* booklet and the "Internal and External Audits" booklet of the *Comptroller's Handbook* for more information.

   For higher-risk banks, or banks with higher-risk areas, examiners should supplement financial information with the following, as appropriate:

- Budget and pro forma financial statements.
- Bank management and board reports.
- Loan review, audit, and compliance risk management reports.
- Board and committee minutes.

2. Discuss with bank management financial trends and changes in bank operations, controls, and management. Examiners may conduct this discussion by telephone or during an on-site meeting. Focus on areas of significant actual or planned changes, including growth. Possible discussion topics include the following:

   - Financial performance and trends.
   - Plans to raise or deploy of significant injections of capital.
   - Control systems (audit, loan review, compliance review, etc.) and their schedule or scope.
   - Significant issues identified by internal or external audit and bank management's corrective action on those issues.
   - Activities that may affect the bank's risk profile, including changes in
     - products, services, distribution channels, or market area.
     - policies, underwriting standards, or risk appetite.
     - management, key personnel, organizational structure, or operations.
     - technology—including operating systems, third-party technology service providers, critical software, and internet banking—or plans for new products and activities that involve new technology.
     - changes in third-party relationships, including new or terminated relationships.
     - legal counsel and pending litigation.
   - Purchase, acquisition, or merger considerations.
   - Broad economic or systemic trends affecting the condition of the federal banking system, as identified by the OCC's national or district risk committees.
   - Trends in the local economy or business conditions.
   - Public information disclosed since the last review, including
     - recent news media coverage.
     - market or industry information for publicly traded companies, such as 10Q and securities analyst reports.
   - Changes in asset management lines of business.
   - Issues regarding BSA/AML/OFAC compliance.
   - Issues regarding consumer compliance or the CRA.
   - Other issues that may affect the bank's risk profile.
   - Bank management's concerns about the bank or about the OCC's supervision.

3. Perform follow-up on outstanding MRAs, violations of laws or regulations, and enforcement actions, focusing on time frames for corrective action.

4. Consult with the appropriate supervisory office official to determine whether results of the monitoring activities necessitate changes to the CAMELS/ITC component ratings. (The OCC must perform a CRA evaluation to change a bank's CRA rating.)

5. Determine whether results of the monitoring activities affect the supervisory strategy with regard to the following:

   - Types of supervisory activities planned.
   - Scope of the reviews.
   - Timing or scheduling.
   - Resources (expertise, experience level, or number of examiners).

6. Update Examiner View to reflect the following:

   - Changes to supervisory strategy, ratings, RAS, or core knowledge.
   - Examination conclusion and analysis comments.

   Documentation in Examiner View and work papers should support conclusions based on the extent of findings and work performed. For example, if the bank's risk profile or CAMELS/ITC ratings have not changed, the only required Examiner View documentation is a statement that the monitoring objectives were met and that the bank's risk profile has not changed since the last review.

   If there are significant changes that require a change to CAMELS/ITC ratings or the RAS, open the appropriate CAMELS/ITC component(s) in Examiner View and document additional supervisory work performed and the effect of the changes on the RAS, CAMELS/ITC ratings, and the supervisory strategy. If concerns are identified, send written communication or conduct a meeting with the board or bank management. Any MRAs and any change in an aggregate risk assessment or CAMELS/ITC rating must be communicated in writing to the board. (The OCC must perform a CRA evaluation to change a bank's CRA rating.)

Objective 2: For de novo banks, perform the following during periodic monitoring:

- Assess the bank's performance relative to its final business plan and budget by comparing its financial results and operations with the business plan and budget.
- Evaluate any significant deviation or change from the business plan (actual or planned).
- Monitor trends in the bank's financial performance. For example, examiners should assess the quality of asset growth and the impact of that growth on the bank's condition.
- Compare the bank's financial performance to a de novo peer group using the quarterly UBPR. Comparisons with peer group data should consider any unique characteristics of the bank. Other peer groups may be needed depending on the type of charter established or if the charter has a particular banking niche.
- Discuss the results of the quarterly business plan, budget, financial performance and peer analyses with bank management, and record appropriate comments in Examiner View. Comments should highlight material variances disclosed in the analyses.

Information useful in monitoring the financial performance of de novo banks (except for trust banks) includes the following:

- Asset growth, including loan growth
- Return on assets
- Net interest margin (NIM)
- Capital ratios
- Past due and nonaccrual assets
- Non-interest expense (overhead)
- Loan mix (specific loan categories as a percentage of total loans)
- Funding mix (specific funding sources as a percentage of total liabilities)

Information useful in monitoring the financial performance of de novo trust banks includes the following:

- Fiduciary asset growth and mix by type
- Custody or safekeeping asset growth and mix
- Operating income growth by component
- Operating expense growth by component
- Operating profit margin
- Net income
- Balance-sheet composition and growth
- Liquidity level and sources

Reviewing the level and trend in non-interest expenses is critical in assessing the financial performance of de novo banks. Examiners should consider salary and compensation expenses, including employment agreements and incentive programs, occupancy costs, technology costs, fees paid for professional services, and third-party services. Examiners should understand the appropriateness of fees paid to insider-related organizations. Examiners should also understand the bank's dividend payout policy.

Examiners should use judgment and review additional information to capture the unique aspects of a particular charter (e.g., to monitor a particular banking niche). Examiners should expand the scope of periodic monitoring as appropriate based on risks present.

Internal Controls and Audit

Conclusions:
The system of internal controls is (strong, satisfactory, insufficient, or weak).
The audit program is (strong, satisfactory, insufficient, or weak).

Introduction

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Assessment of Audit Functions"

The core assessment requires examiners to assess and validate the two fundamental components of a bank's risk management system—the system of internal controls and audit. Accurate assessments of internal controls and audit are crucial to the proper supervision of a bank. Based on these assessments, examiners also determine the amount of reliance that the OCC can place on the bank's internal control system or audit work.

Complete this section's objectives to assess the bank's overall system of internal controls and audit program. In completing these assessments, the examiner should consult the EIC and other examining personnel as appropriate. Consider the following when assessing internal controls and audit:

- Board and management oversight
- Management and processes
- Reporting
- Staffing

A bank is expected to establish and maintain an effective system of internal controls and an audit system commensurate with the bank's size and complexity as well as the nature, scope, and risk of its activities.[41]

Internal Controls

A system of internal controls is made up of both internal controls and information systems. Internal controls are the systems, policies, procedures, and processes—effected by the bank board, management, and other personnel—designed to safeguard bank assets, limit or control risks, and achieve the bank's objectives.

The community bank core assessment includes objectives for assessing a bank's control environment during each supervisory cycle. The objectives are consistent with applicable

[41] Refer to 12 CFR 30, appendix A, "Interagency Guidelines Establishing Standards for Safety and Soundness."

laws and regulations[42] and industry best practices, and include an assessment of bank financial reporting and related controls. Examiners should consider each bank's risk profile, complexity, and nature of activities in their assessment. Examiners determine whether the overall system of internal controls is strong, satisfactory, insufficient, or weak.

Examiners should use expanded procedures when the assessment identifies significant control discrepancies or weaknesses or raises questions about the effectiveness of the bank's system of internal controls. Examiners should refer to appropriate booklets of the *Comptroller's Handbook*, including "Internal Control" (national banks)[43] and "Corporate and Risk Governance," or to the *FFIEC IT Examination Handbook* and the *FFIEC BSA/AML Examination Manual* for more information and expanded procedures. (Updated in version 1.1)

Audit

(Section updated in version 1.1)

The community bank core assessment includes objectives for assessing a bank's overall audit program and determining the level of OCC reliance on the bank's audit work during each supervisory cycle. The EIC reviews the supervisory strategy and, in consultation with the supervisory office, tailors the scope of the audit assessment to the bank's size and complexity as well as the nature, scope, and risk of its activities. The review of audit work papers may not be waived during any supervisory cycle. The scope of this audit work paper review may vary by bank to include internal audit, outsourced internal audit, or external audit work papers.[44] Examiners determine whether the overall audit program and the bank board's oversight thereof is strong, satisfactory, insufficient, or weak.

Examiners should use expanded procedures when the assessment identifies significant audit or control discrepancies or weaknesses or when the assessment raises questions about the audit function's effectiveness. In those situations, examiners should consider expanding the scope of the review by selecting expanded procedures in any of the following:

- "Internal and External Audits" booklet of the *Comptroller's Handbook*
- "Internal Control" booklet of the *Comptroller's Handbook* (national banks)
- *OTS Examination Handbook* section 340, "Internal Control" (FSAs)
- Other appropriate booklets of the *Comptroller's Handbook*
- *FFIEC IT Examination Handbook*
- *FFIEC BSA/AML Examination Manual*

[42] For information on the laws, regulations, and policy guidance relating to internal controls, refer to the "Internal Control" booklet of the *Comptroller's Handbook* (national banks) and *OTS Examination Handbook* section 340, "Internal Control" (FSAs).

[43] For FSAs, refer also to *OTS Examination Handbook* section 340, "Internal Control."

[44] Refer the validation section in the "Internal and External Audits" booklet of the *Comptroller's Handbook* for more information.

Examiners should determine whether to expand audit examination work in effected operational or functional business areas.

Verification is generally performed infrequently. When significant concerns remain about the adequacy of an audit or internal controls or about the integrity of a bank's financial or risk management controls, examiners should consider further expanding the audit review to include verification procedures. The supervisory office makes the determination on a case-by-case basis whether to pursue verification, along with its extent and who performs it. Examiners should refer to the "Bank Supervision Process" and "Internal and External Audits" booklets of the *Comptroller's Handbook* regarding verification procedures.

Reliance on Audit Work and Internal Controls

Upon completing the Internal Controls and Audit section of the core assessment, the examiner should determine how much reliance can be placed on the bank's audit program and internal control system. The examiner, in consultation with the EIC, should communicate this information to relevant examination staff.

Objectives and Procedures

Minimum Objective

Determine the internal control rating. Determine the audit program rating and the level of reliance the OCC can have on audit work, and consider the potential impact of these findings on the bank's risk assessment. Each supervisory cycle must include a review of audit work papers—this cannot be waived.

The examiner should review the bank's 12 CFR 363 annual reports, if the bank is covered by 12 CFR 363 or a voluntary submitter. If the 12 CFR 363 annual report was already reviewed during a prior supervisory activity, the examiner should consider the results of the review. Examiners should operate in accordance with their OCC supervisory office's guidance and instructions for analysis and documentation of the bank's 12 CFR 363 annual reporting.

Discuss with management the following:

- How the audit committee supervises audit activities.
- Any significant changes in business strategy or activities that could affect the audit function (e.g., third-party relationships, products, services, delivery channels, or market geographies).
- Any material changes in the audit program, scope, schedule, or staffing related to internal and external audit activities (e.g., external auditor, outsourcing or co-sourcing scope, and audit tools or audit systems).
- Any other internal or external factors that could affect the audit function (e.g., audit projects or initiatives).
- Observations from examiner review of internal bank reports, as well as OCC and other third-party-generated reports.

Obtain and review the following information:

- Centralized audit firm review memorandum, if applicable
- Board or audit committee minutes and related internal or external audit packages and information submitted to the board or audit committee.
- Sample of internal audit work papers. Examiners should consider high-growth areas, high-risk areas, new activities offered by the bank, and previous examination results. Refer to the “Internal and External Audits” booklet of the *Comptroller’s Handbook.* Consider the results of the work paper review when determining the adequacy of the bank’s audit program testing and assessment of internal controls.
- Most recent bank annual report package filed with the OCC (if applicable). Any report of resignation of external auditor of a public company, or of a holding company if the bank is public.

Communicate deficiencies identified by audit to the examiners assigned to review other functional areas for follow-up. Consult with the EIC and other examining personnel to determine whether the deficiencies identified by audit indicate potential weaknesses in the bank’s internal controls.

If the bank’s activities, risk profile, or risk controls have changed significantly, or if review of the above information raises substantive issues, the examiner should expand the activity’s scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude internal controls and audit review by completing objective 9.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank’s condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the internal controls and audit review.

1. Consider the information reviewed when performing the minimum objective. If not reviewed, obtain and review the following, as applicable:

    - Internal and external audit reports issued since the last examination, including management letters and such as service organization control (SOC) reports.
    - External audit engagement letter and other correspondence between the external auditor and the bank or, if applicable, the bank’s parent company.
    - Current year internal and external audit plan or schedule and status reports.
    - Management’s responses to internal and external audit reports issued since the last examination.
    - Detailed listing of job duties and responsibilities of internal audit staff, including the chief auditor. (Some small banks do not have a formal internal or external audit program. Instead, audit responsibilities may lie with an officer or employee designated as a part-time auditor or with employees who may share the audit tasks. In

other banks, the board, through its annual director's examination, performs the internal or external audit function. The person with responsibility for the audit function is considered to be the chief auditor for purposes of these examination procedures.)
- Internal audit staff résumés, including educational and work background, industry certifications, and recent developmental training.
- The bank's governance structure that outlines the bank's board and its relevant committee reporting structure.
- Audit committee meeting minutes and packages applicable to audits since the last examination.
- Listing of members of the audit committee(s), including those on the fiduciary audit committee, if applicable, and the date of each member's appointment to the committee.
- Memorandums issued as part of an OCC centralized audit firm review involving the bank's outsourced internal audit or external audit functions.
- Any report of the resignation of an external auditor of a public company, or of a holding company if the bank is public.
- Customer complaint data from the OCC's Customer Assistance Group and the bank. Coordinate with the examiner reviewing consumer compliance to avoid duplication of efforts.
- Significant litigation.

Assurance reports may be obtained by those performing services for the bank, such as an outside third party, the bank's holding company, or another affiliate of the holding company. The scope and objective of these audits are determined by the service provider, but most follow the industry-accepted standard for reporting. Refer to the "Non-Internal Audit Assurance Activities" section of the "Internal and External Audits" booklet for more information on types and considerations for internal audit.

2. Discuss with examiners responsible for completing other areas of the core assessment any significant audit findings that require follow-up.

3. Consult with the EIC and examiners responsible for completing other areas of the core assessment to identify and select an appropriate sample of internal audit work papers for review. Consider having examiners who are responsible for other bank activity and specialized areas review internal audit work papers associated with those activities.

   For more information, refer to the "Internal and External Audits" booklet of *Comptroller's Handbook.*

Objective 2: Determine the adequacy of board and audit committee oversight of the bank's audit function, including outsourced internal audit and external audit.

1. Review the board or audit committee minutes and packages to determine whether the board or audit committee, as appropriate,

- has an audit committee charter clearly that defines duties appropriate for the size, complexity, and risk profile of the bank, including oversight of the internal audit function.
- approves the internal and external audit programs, annual audit plan and schedule, and significant audit program or audit schedule changes.
- reviews and approves the decision to forego an external audit program.
- confirms that the bank has appropriate audit coverage to meet risks and demands posed by its current and planned activities.
- confirms that the bank has adequate independent and competent audit personnel, considering staffing, training, compensation, and outsourcing options.
- meets regularly with the chief auditor, outsourced internal audit firm representative(s), and external auditor.
- receives sufficient information and reports to effectively monitor audit performance and progress in meeting the audit plan and schedule (e.g., plan status, staff training, audit risk assessments, audit activity reports, verification activity status, and issue tracking reports).
- regularly review internal and external audit reports, audit findings, management's responses, and other related information.
- holds management accountable for timely and appropriate resolution of audit findings.
- reviews the external auditor's evaluations of using internal audit's work, if the external auditor is using work of the internal auditors.
- periodically evaluates the audit function, including effectiveness of any audit quality assurance activities.
- provide active oversight of outsourced audit activities, perform due diligence prior to entering into third-party audit arrangements, approve an appropriate written agreement or contract, and approve terminations of outsourced internal audit engagements.
- discusses the external auditor's independence.

For more information, refer to the "Internal and External Audits" booklet of the *Comptroller's Handbook.*

2. If the bank is subject to 12 CFR 363, determine whether the composition of the audit committee complies with 12 CFR 363.5, "Audit Committees." Consider the following:

   - If the bank's assets are $1 billion or greater, are all members of the audit committee outside directors who are independent of bank management?
   - If the bank's assets are $500 million or greater, but less than $1 billion, is a majority of the audit committee outside directors who are independent of bank management?

3. If the bank has fiduciary powers, coordinate with the examiner reviewing asset management and consider the following:

- Does the fiduciary audit committee meet requirements of 12 CFR 9.9(c) (national banks) or 12 CFR 150.470 (FSAs)? (Updated in version 1.1)
- Do board meeting minutes reflect requirements for fiduciary audits in compliance with 12 CFR 9.9(a) and (b) (national banks) or 12 CFR 150.440(a) and (b) (FSAs)?
- For banks with trust powers that offer collective investment funds (CIF), does the bank's board retain direct responsibility for the annual audit of CIFs in accordance with 12 CFR 9.18(b)(6)(i) (national banks and FSAs, as 12 CFR 9.18 is applicable to FSAs under 12 CFR 150.260(b))?

Objective 3: If the bank is covered under 12 CFR 363, determine compliance with annual filing and reporting requirements.

- Determine whether the bank's most recent fiscal year-end management report contains required information and is appropriately signed (refer to 12 CFR 363.2(b), "Management Report"). Determine whether the report includes a statement of management responsibilities and an assessment by management of the bank's compliance with designated safety and soundness laws and regulations during the fiscal year, along with other relevant statements on internal controls, management conclusion, etc.
- Review the bank's determination that it met the filing and notice requirements of 12 CFR 363.4, "Filing and Notice Requirements."
- Determine whether management's assessment of financial reporting controls and compliance with designated laws and regulations regarding insider loans and dividend restrictions (12 CFR 363, appendix A, table 1) is appropriate.

Refer to the "Internal and External Audits" booklet of the *Comptroller's Handbook* for more information and expanded procedures. (Updated in version 1.1)

Examiners may want to use appendix D, "12 CFR 363 Report Worksheet," in the "Internal and External Audits" booklet of the *Comptroller's Handbook* as an aid in completing this portion of the examination procedures.

Examiners should promptly advise the OCC supervisory office of any qualified or adverse opinion or disclaimer of opinion encountered.

Objective 4: If the bank is subject to the periodic filing and reporting requirements of 12 CFR 11, "Securities Exchange Act Disclosure Rules" (i.e., the bank has registered its securities with the OCC), determine compliance with certain SEC requirements.

1. Review correspondence or other communications issued by the OCC's Chief Counsel's Office, Securities and Corporate Practices Division, resulting from its review of the bank's proxy material and annual reports.

2. Determine whether the bank has adequately addressed issues requiring attention resulting from the review by the OCC's Chief Counsel's Office, Securities and Corporate Practices Division.

Objective 5: Determine adequacy of the bank's internal audit function.

1. Assess whether the internal audit function has been established consistent with 12 CFR 30, appendix A, II.B, "Internal Audit System." Determine whether the internal audit function

   - adequately monitors internal controls systems.
   - is independent and objective.
   - is staffed by qualified persons.
   - adequately tests and reviews information systems.
   - adequately documents tests, findings, and corrective actions.
   - verifies and reviews management actions addressing material weaknesses.
   - requires the bank board or its audit committee to review the internal audit systems' effectiveness.

   If the bank has no internal audit function, determine management's rationale and mitigating factors (e.g., strong external audit or director's examination and internal control system, limited complexity of operations, or low risk).

2. Assess the quality of internal audit activities, including outsourced internal audit activities, by considering the following:

   - Bank's size and the nature and scope of its activities.
   - Quality and effectiveness of internal control assessments, including those for financial reporting.
   - Whether audit coverage is appropriate, given the bank's risk profile.
   - Quality of audit reports and findings.
   - Quality and timeliness of management responses to audit findings and whether audit follows up on significant findings in a timely manner to assess effectiveness of management's responses.
   - Reporting lines to the board or audit committee.
   - Quality and depth of audit coverage and audit procedures, including regular testing of internal controls and MIS.
   - Whether audit provides constructive business advice or consulting on evaluating safeguards and controls in the acquisition and implementation of new products, services, and delivery channels, and what its role is in merger, acquisition, and transition activities.
   - Whether audit plans address goals, schedules, staffing, and reporting.
   - Progress made toward completing annual audit plans or schedules.
   - Whether audit scope is adjusted for significant changes in the bank's environment, structure, activities, risk exposures, systems, or new products or services.
   - Use of audit software and other computer-assisted audit techniques.

3. Determine competence and independence of internal audit staff, whether in-house or outsourced. Consider the following:

- Auditor and staff experience and training.
- Auditor and staff tenure, turnover, and vacancies.
- Incompatible duties performed by auditor or staff.
- Lines of reporting, operational duties assigned to the auditor, or other restrictions or relationships.
- Staff's ability to meet audit schedule.

4. Review internal audit outsourcing arrangement contracts or engagement letters, and determine whether they adequately address the roles and responsibilities of the bank and the third party. (Refer to OCC Bulletin 2003-12, "Interagency Policy Statement on Internal Audit and Internal Audit Outsourcing," OCC Bulletin 2013-29, OCC Bulletin 2017-21, and OCC Bulletin 2017-7.) Determine whether

   - the arrangement maintains or enhances quality of internal audit and internal controls.
   - key bank employees and third parties clearly understand lines of communication and how the bank addresses internal controls or other problems noted by the third party.
   - the outsourced internal audit firm(s) is adequately incorporated into the bank's third-party risk management program.
   - the arrangement does not compromise the role or independence of a third party who also serves as the bank's external auditor.

5. If the bank has fiduciary powers, determine quality of the fiduciary audit function and whether it complies with audit standards in 12 CFR 9.9 (national banks) or 12 CFR 150.440-480 (FSAs). Determine whether

   - suitable audit of all fiduciary activities is completed at least once every calendar year or under a continuous audit program.
   - audit results, including significant actions taken as a result of the audit, are noted in board minutes.
   - if the bank uses a continuous audit, the results of all discrete audits performed since the last audit reports, including all significant action, are noted in board minutes at least once during the calendar year.

6. Determine the quality of the bank's BSA/AML program audit function and whether it complies with 12 CFR 21.21, "Procedures for Monitoring Bank Secrecy Act Compliance." Consult with the examiner responsible for examining BSA/AML and determine whether

   - compliance testing is completed on an annual basis.
   - if testing is not completed annually, risk analysis used by management to set testing schedule, and frequency of audits is reasonable.
   - audit covered all regulatory provisions and bank's policies and procedures for complying with BSA/AML/OFAC regulations. For more information, refer to the *FFIEC BSA/AML Examination Manual.*

Objective 6: Determine whether the bank has implemented an appropriate external audit function.

1. If the bank has no external audit function, determine management's rationale and mitigating factors (e.g., strong internal audit and internal control system, limited complexity of operations or low-risk). Consider the following:
   - Bank's size.
   - Nature, scope, and complexity of bank activities.
   - Bank's risk profile.
   - Actions (taken or planned) to minimize or eliminate identified weaknesses.
   - Extent of the bank's internal auditing program.
   - Compensating internal controls in place.

2. Determine which of the following types of external audit programs the bank has:

   - Financial statement audit by an independent public accountant.
   - Reporting by an independent public accountant on the bank's internal control structure governing financial reporting.
   - Integrated audit by an independent public accountant.
   - Balance sheet audit performed by an independent public accountant.
   - Agreed-upon procedures.

   For more information, refer to the "Types of External Auditing Programs" section of the "Internal and External Audits" booklet.

3. If a financial statement audit was performed, determine what type of opinion was issued (unqualified, qualified, adverse, or disclaimer).

4. Determine whether the external audit program is performed by an independent public accountant or other independent external party and whether the program is appropriate given the bank's size, nature, and extent of its activities and operations, and risk profile.

5. Review the external audit engagement letter and assess its adequacy. Consider the following:

   - Purpose and scope of the audit
   - Period of time to be covered by the audit
   - Reports expected to be rendered
   - Limitations placed on the auditor's scope or work

   For more information, refer to the "Engagement Letters" section of the "Internal and External Audits" booklet of the *Comptroller's Handbook*.

6. Arrange with bank management to meet with the external auditor to discuss the following:

- External audit's scope, results, or significant findings, and upcoming audit plans or activities.
- Reports, management letters, and other communications (written or oral) with the board or audit committee.
- Audit planning methodologies, risk assessments, sampling techniques, and (if applicable) 12 CFR 363 control attestations.
- How much the external auditor relies on the work of internal auditors and the extent of external audit's assessment and testing of financial reporting controls.
- Assigned audit staff experience and familiarity with banking and bank auditing, particularly in specialized areas.

7. Determine whether the board or audit committee and the external auditor have discussed and resolved financial, employment, business, or nonaudit service relationships that compromise or appear to compromise the external auditor's independence.

8. Except for director's examinations, examiners are not required to review external audit work papers. External audit work papers, however, may be subject to OCC review if the review of internal audit discloses significant issues (i.e., insufficient internal audit coverage) or questions are otherwise raised about matters that are normally within the scope of an external audit program. Examiners should consider whether to review external audit work papers for areas where problems or questions exist. Examiners should consider reviewing external audit work papers when

   - unexpected or sudden change occurs with the bank's external auditor.
   - significant change occurs in the bank's external audit program.
   - issues are raised that affect the bank's safety and soundness.
   - issues are raised about the independence, objectivity, or competence of the external auditor.

   For more information, refer to the "Work Paper Review: External Audit" section of the "Internal and External Audits" booklet.

Objective 7: Use the findings from the audit review and other areas under examination to assess the bank's internal control system.

1. Assess the bank's control environment. Consider the following:

   - Organizational structure (e.g., centralized or decentralized, authorities and responsibilities, and reporting relationships).
   - Management's philosophy and operating style (e.g., formal or informal, conservative or aggressive, and success of risk strategy).
   - External influences affecting operations and practices (e.g., independent external audits).
   - Goals, objectives, attention, and direction provided by the board of directors and its committees, especially the audit or risk management committees.

2. Evaluate the bank's internal RAS. Consider the following:

   - Effectiveness of the system to identify, measure, monitor, and control risks.
   - Responsiveness of the system to changing risk conditions.
   - Competency, knowledge, and skills of personnel.
   - Adequacy of blanket bond coverage in relation to the bank's risk profile.

3. Assess the bank's control activities. Consider the following:

   - Quality of policies, procedures, and audit.
   - Quality and timeliness of management and staff training.
   - Timeliness of risk analysis and control processes.
   - Approvals and authorization for transactions and activities.
   - Supervision and oversight of payments against uncollected funds (potential for check fraud, such as kiting).
   - Segregation or rotation of duties to ensure that the same employee does not originate a transaction, process it, and then reconcile the general ledger account.
   - Vacation requirements or periodic unannounced rotation of duties for personnel in sensitive positions.
   - Safeguards for access to and use of sensitive assets and records, including wire transfer activities.
   - Internal review of employee accounts and expense reports.
   - Dual control or joint custody over access to assets (e.g., cash, cash collateral, official checks, and consigned items).
   - Independent checks or verifications on function (e.g., lending and wire transfer), performance, and reconciliation of balances.
   - Timely account reconciliation and resolution or clearing of outstanding items.
   - Accountability for actions taken by bank staff and the responsibilities and authorities given to the staff.

4. Assess the bank's accounting, information, and communication systems. Determine whether the systems

   - identify and capture relevant internal and external information in a timely manner.
   - ensure accountability for assets and liabilities.
   - ensure effective communication of positions and activities.
   - adequately address business resumption and contingency planning for information systems.

5. Evaluate the bank's self-assessment and monitoring systems. Consider the following:

   - Periodic evaluations, self-assessments, or independent audits of internal controls.
   - Whether the systems ensure timely and accurate reporting of deficiencies.
   - Processes to ensure timely modification of policies and procedures.

- Audit requirements established by the bank’s blanket bond company as specified in the insurance application and policy.

Objective 8: Determine whether expanding the scope of the supervisory activity or developing a plan for corrective action is warranted.

1. If the review of internal controls or audit, including the work paper review, discloses significant audit or control discrepancies or weaknesses that are not mitigated by a satisfactory or strong risk management program, consider whether expanded examination procedures (including internal control questionnaires) should be performed to identify the extent of deficiencies and determine their effect on bank operations. Consider expanding procedures if the following issues are identified:

    - Concerns about the competency or independence of internal or external audit.
    - Unexplained or unexpected changes in internal or external auditors or significant changes in the audit program.
    - Inadequate scope of the overall audit program or in key risk areas.
    - Audit work papers in key risk areas that are deficient or do not support audit conclusions.
    - High-growth areas without adequate audit or internal controls.
    - Inappropriate actions by insiders to influence findings or scope of audits.

2. If, after completing step 1, significant concerns remain about the adequacy of audit, adequacy of internal controls, or integrity of the bank’s financial controls, consider selecting certain verification procedures to determine root causes of the concerns and effect on bank operations. Examiners should use verification procedures if the following issues are identified:

    - Key account records are significantly out of balance.
    - Management is uncooperative or poorly manages the bank.
    - Management attempts to restrict access to bank records.
    - Significant accounting, audit, and internal control deficiencies remain uncorrected from prior examinations or from one audit to the next.
    - Bank auditors are unaware of, or are unable to sufficiently explain, significant deficiencies.
    - Management engages in activities that raise questions about its integrity.
    - Repeated violations of law affect audit, internal controls, or regulatory reports.

    Examiners may find other instances warranting further investigation. Examiners should consider the risk posed by noted weaknesses in audit or controls and use judgment in deciding whether to perform verification procedures.

Objective 9: Conclude the internal controls and audit review.

1. Assess the system of internal controls (strong, satisfactory, insufficient, or weak) and audit program (strong, satisfactory, insufficient, or weak). Refer to the "Community Bank Internal Control and Audit Assessment Factors" section of this booklet.

2. If warranted, develop action plans to address audit deficiencies before conducting the exit meeting. Consider management's ability to correct the bank's fundamental problems.

3. Use results of the foregoing procedures and other applicable examination findings to compose comments (e.g., separate comments, part of management/administration, and MRAs) for inclusion in the ROE.

4. Incorporate assessments into assigned CAMELS/ITCC ratings and risk assessment conclusions.

5. Consult with the EIC and communicate to other examiners conclusions and findings from the internal control and audit review that are relevant to other areas being reviewed. Communicate conclusions regarding the assessments of internal controls and audit to the EIC or examiner responsible for consolidating conclusions from the "Management" section.

6. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View (e.g., ratings, core knowledge, MRAs, and violations). (Updated in version 1.1)

7. In discussion with the EIC, provide preliminary strategy recommendations for the next supervisory cycle.

Capital Adequacy

Conclusion: Capital Adequacy is rated (1, 2, 3, 4, or 5).

Introduction

Complete the appropriate objectives in this section to assign the capital adequacy component rating. When assigning the rating, the examiner should consult with the EIC and other examining staff. Consider the following UFIRS factors:

- Level and quality of capital and overall financial condition of the bank.
- Ability of bank management to address emerging needs for additional capital.
- Nature, trend, and volume of problem assets, and adequacy of the allowance for loan and lease losses (ALLL) and other valuation reserves.
- Balance-sheet composition, including nature and amount of intangible assets, market risk, concentration risk, and risks associated with nontraditional activities.
- Risk exposure represented by off-balance-sheet activities.
- Quality and strength of earnings, and reasonableness of dividends.
- Prospects and plans for growth and past experience in managing growth.
- Access to capital markets and other sources of capital, including support provided by a parent holding company.

The bank is expected to maintain capital commensurate with the nature and extent of risks to the bank and the ability of bank management to identify, measure, monitor, and control these risks. Examiners should consider the bank's risk profile when determining capital adequacy and assigning the capital adequacy component rating.

Supervisory Review of Capital Planning and Adequacy

The supervisory review process assesses whether (1) the bank has a sound and effective process commensurate with its overall risk and complexity to determine that its overall capital is adequate and (2) the bank maintains a capital level that is commensurate with its risks and is consistent with the bank's internal assessment and identified capital needs on an ongoing basis and as underlying conditions change (for example, changes in the bank's overall risks or economic conditions). Examiners review the capital planning process at least once during each supervisory cycle. Conclusions about the capital planning process are considered and incorporated in the assessment of the capital and management component ratings.

Examiners should consider the quality of the bank's overall corporate governance of the bank's risk taking activities, including senior management and board oversight, when assessing capital adequacy. As part of this evaluation, examiners should consider the quality of risk management, internal control, model validation, and audit processes as well as bank management's expertise and ability to identify and control financial and operating risks.

When serious deficiencies exist in any of these areas, examiners may determine that the bank should hold capital above the level suggested in the bank's assessments of specific risks.

The bank's failure to have an effective capital planning process may be an unsafe and unsound banking practice. If the bank does not have an effective capital planning process that is commensurate with its overall risks, the OCC may require immediate corrective action. An ineffective or weak capital planning process may invalidate the bank's internal capital assessment and necessitate that examiners determine an appropriate capital level. The OCC may impose higher capital requirements if the bank's level of capital is insufficient in relation to its risks; determining the appropriate capital level is necessarily based in part on judgment grounded in agency expertise. Potential OCC actions to ensure adequate capital may include, as deemed necessary, an individual minimum capital ratio, memorandum of understanding, formal written agreement, consent order, cease-and-desist order, or a prompt corrective action directive.

Examiners should discuss with the board and bank management any material risks that the capital planning process did not capture and any other material issues regarding capital adequacy or contingency plans. The board should direct bank management to address any gaps in the bank's capital planning process to ensure that the quality and quantity of capital is sufficient to support the risks in the bank.

For more information, refer to the "Capital Planning" section of the "Capital and Dividends" booklet of the *Comptroller's Handbook.* (Updated in version 1.1)

Objectives and Procedures

Minimum Objective

Determine capital adequacy component rating and potential impact on the bank's risk assessment.

At the beginning of the supervisory activity, discuss with bank management the following:

- The bank's present condition and future plans (e.g., dividends, growth, new products, and strategic initiatives, including plans to raise and deploy significant new injections of capital).
- Actual or planned changes in controlling ownership.

Follow up on significant capital-related audit or IT issues that examiners identified while reviewing the bank's audit and IT programs, as applicable.

Obtain and review the following information:

- The OCC's supervisory strategy for the bank.
- The bank's capital computations. (Refer to 12 CFR 3, "Capital Adequacy Standards.") (Updated in version 1.1)

- Results from supervisory activities.
- Results from other areas of this and other supervisory activities that may affect capital adequacy (e.g., earnings or asset quality).
- Financial reports (e.g., UBPR) and applicable OCC reports or analytical tools.

If the bank's activities, risk profile, or risk controls have changed significantly, or if review of this information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the capital review by completing objective 8.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the capital adequacy review.

1. Review supervisory information to identify previously identified deficiencies that require follow-up in this area.

2. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is required.

3. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about the integrity, confidentiality, or availability of data and require follow-up.

4. If not previously reviewed, obtain and review the following:

    - The bank's total capital and risk-based capital computations.
    - Findings from the OCC's periodic monitoring activities.
    - List of shareholders who own 5 percent or more and their percentage of ownership.

5. Calculate and distribute capital limits and shareholder information to other examiners.

Objective 2: Determine adequacy of capital.

1. Review applicable information to identify trends. Consider the following:

    - Reports used by bank management to monitor and project capital requirements.
    - UBPR and other OCC analytical tools calculations. Compare the bank's ratios with those of peer banks.
    - The bank's present condition, risk profile, and future plans. (Updated in version 1.1)

2. Obtain capital-related information from the examiner assigned to review board minutes.

3. Consider impact of the following on current or future capital adequacy: (Updated in version 1.1)

   - Earnings.
   - Dividends.
   - Asset quality and adequacy of the ALLL.
   - On- and off-balance-sheet activities.
   - Historical and planned growth.
   - New products, services, or distribution channels.
   - Strategic initiatives, including plans to raise and deploy significant new injections of capital.
   - Financial plans and budgets, including replacement costs for fixed assets and technology.
   - Related organizations.

4. Evaluate sources of capital. Consider the following:

   - Earnings retention.
   - Ownership capacity—condition of principal shareholders, parent, or subsidiaries.
   - History of public or private offerings.

Objective 3: Determine risk to capital posed by the aggregate level or direction of applicable risks.

Consult with the EIC and other examining staff to decide whether the aggregate level or direction of risk has an adverse impact on current or future capital adequacy. Refer to the "Risk Assessment System" section of this booklet.

Objective 4: Determine quality of risk management systems through discussions with key risk managers and analysis of applicable information.

1. Assess the bank's system of internal controls over the capital accounts. Consider relevant controls listed in objective 7 of the "Internal Controls and Audit" section of the core assessment. Also consider other controls pertinent to capital.

2. Assess integrity, confidentiality, and availability of data used to record, analyze, and report information related to capital. Consider input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to the data and procedures in place to monitor system activities. Determine if these controls have been independently validated. Coordinate this review with examiners responsible for all functional areas of the examination, including internal controls, to avoid duplication of effort. Share findings with the examiner reviewing IT.

Objective 5: Assess the adequacy of the bank's capital plan and stress testing. Consult with the loan portfolio manager or other examiners responsible for asset quality to avoid duplication of efforts pertaining to the review of the bank's stress testing.

1. Determine whether the bank's capital planning process includes the following:

   - Identifying and evaluating risks.
   - Setting and assessing capital adequacy goals that relate to risk.
   - Controls for integrity in the internal capital planning process and capital adequacy assessments.

   For more information, refer to the "Capital Planning" section of the "Capital and Dividends" booklet of the *Comptroller's Handbook.* (Updated in version 1.1)

2. Evaluate the bank's stress testing process. Consult with the loan portfolio manager or other relevant examiners responsible for asset quality as appropriate. Determine whether the stress test includes the following:

   - Asks plausible "what if" questions about key vulnerabilities.
   - Makes a reasonable determination of how much impact the stress event or factor might have on earnings and capital.
   - Incorporates the resulting analysis into the bank's overall risk management process, asset/liability strategies, and strategic and capital planning processes.

   For more information, refer to OCC Bulletin 2012-33, "Community Bank Stress Testing: Supervisory Guidance."

Objective 6: Determine whether to expand the procedures or develop a plan for corrective action.

Consider whether

- bank management can adequately manage the bank's risks.
- bank management can correct fundamental problems.
- to propose a strategy to address identified weaknesses and to discuss strategy with the supervisory office.

For more information, refer to the "Capital and Dividends" booklet of the *Comptroller's Handbook*. (Updated in version 1.1)

Objective 7: After completing expanded procedures, determine whether risks and concerns indicate the need to perform verification procedures.

The extent to which examiners perform verification procedures is decided on a case-by-case basis after consulting with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 8: Conclude the capital adequacy review.

1. Adjust the bank's reported capital ratios to reflect the results of the examination and distribute them to examining staff. Consider the following:

   - Asset charge-offs
   - Examiner-directed provisions to the ALLL (Updated in version 1.1)
   - Errors in financial reporting
   - Other capital adjustments

2. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the capital review that are relevant to other areas being reviewed.

3. Use results of the foregoing procedures and other applicable examination findings to compose comments (e.g., capital adequacy, MRAs, violation write-ups) for the ROE. (Updated in version 1.1)

4. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

5. In consultation with the EIC, provide preliminary strategy recommendations for the next supervisory cycle.

Asset Quality

Conclusion: Asset quality is rated (1, 2, 3, 4, or 5).

Introduction

Complete the appropriate objectives in this section to assign the asset quality component rating. When assigning the rating, the examiner should consult with the EIC and other examining staff. Consider the following UFIRS factors:

- Adequacy of underwriting standards, soundness of credit administration practices, and appropriateness of risk identification practices.
- Level, distribution, severity, and trend of problem, classified, nonaccrual, restructured, delinquent, and nonperforming assets for both on- and off-balance-sheet transactions.
- Adequacy of ALLL and other asset valuation reserves.
- Credit risk arising from or reduced by off-balance-sheet transactions, such as unfunded commitments, credit derivatives, commercial and standby letters of credit, and lines of credit.
- Diversification and quality of loan and investment portfolios.
- Extent of securities underwriting activities and exposure to counterparties in trading activities.
- Existence of asset concentrations.
- Adequacy of loan and investment policies, procedures, and practices.
- Ability of bank management to properly administer its assets, including the timely identification and collection of problem assets.
- Adequacy of internal controls and MIS.
- Volume and nature of credit documentation exceptions.

Examiners should consider the ability of bank management to identify, measure, monitor, and control the current and planned level of credit risk when assigning the component rating.

Objectives and Procedures

Minimum Objective

Assign the asset quality component rating, complete the applicable credit underwriting assessment(s), determine the adequacy of the ALLL, and conclude on the credit RAS. (Updated in version 1.1)

At the beginning of the supervisory activity, discuss with bank management the actual or planned changes in the following:

- Lending policies or procedures, including underwriting criteria and practices.
- Lending strategies, including actual and planned growth in the loan portfolio.

- Lending department management or staff.
- Loan origination, servicing, default management, or other key systems.
- Loan products, marketing, or loan acquisition channels.
- Volume, type, and trend of loan policy, credit, and collateral exceptions.
- Loan review process and credit risk rating processes.
- Other external or internal factors that could affect loan quality.
- ALLL balance or methodology.
- Third-party service providers or outsourced functions.

Follow up on significant asset quality-related audit or IT issues identified by examiners reviewing the bank's audit and IT programs.

Obtain and review the following information:

- Supervisory strategy.
- Results from supervisory activities.
- Financial reports (e.g., UBPR), applicable OCC reports or analytical tools, and past-due and nonaccrual reports.
- Risk-rating distribution reports.
- Problem and "watch" loan lists.
- Other performance reports for retail loans (e.g., reports with trends by characteristics such as term, LTV, credit score, or DTI.)
- List of loans to executive officers, directors, and principal shareholders.
- Concentration of credit reports.
- ALLL analysis, including all supporting work papers.
- List of loan participations (in whole or part) purchased and sold since the last examination.
- All loan review reports and bank management responses since the last examination.
- Lending-related audit reports, findings, and bank management responses since the last examination.
- Description of the qualifications and expertise of key lending or credit administration personnel added since the prior examination. (Updated in version 1.1)
- List of credit-related training completed by or scheduled for lending and credit administration personnel.
- Details from other real estate owned (OREO) and "other asset" accounts that are material to financial statements.

Review a sample of loans. The sample should generally include the following:

- At least five recently originated extensions of credit, including loan commitments.
- Loans to executive officers, directors, and principal shareholders.
- Past-due and nonaccrual loans.
- Previously classified and special mention loans and loans from the bank's problem and "watch" loan lists.

The sample size and composition should be based on the supervisory strategy and the trends and overall risk posed by each segment of the loan portfolio. The review's purpose is to determine whether the loans indicate any changes in risk appetite or tolerance level, underwriting practices, credit administration, risk-rating criteria, or other aspects of credit risk management, including compliance with credit-related laws and regulations. This may be accomplished by reviewing credit files, credit approval documents, and loan committee minutes. Documentation of credit file reviews and work paper attachments should support the loan classification. Examiners should hold loan discussions and meetings with bank management to review findings.

If the bank's activities, risk profile, or risk controls have changed significantly, or if review of this information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the asset quality review by completing objective 8.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the asset quality review.

These procedures apply to both commercial and retail credit portfolios, unless specifically stated otherwise. Refer to the "Loan Portfolio Management" booklet of the *Comptroller's Handbook* (national banks) or *OTS Examination Handbook* section 201, "Overview: Lending Operations and Portfolio Risk Management" (FSAs) for more information. (Updated in version 1.1)

1. Review supervisory information to identify previous deficiencies or emerging risks that require follow-up.

2. Discuss with the examiner responsible for completing the "Internal Controls and Audit" section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is necessary. (Updated in version 1.1)

3. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about integrity, confidentiality, or availability of data and require follow-up. If any discrepancies were noted in the loan accounting system, notify other examiners of any potential or actual concerns.

4. If not previously reviewed, obtain and review reports bank management uses to supervise the loan portfolio, including but not limited to, the following:

    - Loan trial balances.

- "Watch" loans list, problem loan list, problem loan workout reports, and past-due and nonaccrual reports.
- Exception and tickler reports. (Updated in version 1.1)
- Concentration of credit reports, including the results of portfolio stress testing.
- List of loans to executive officers, directors, and principal shareholders.
- List of participations (in whole or in part) purchased and sold since the last examination.
- Overdraft list.
- Most recent ALLL analysis.
- Most recent loan review report and work papers, including responses from loan officers, bank management, or the board.

5. Review financial reports (e.g., UBPR) and applicable OCC reports or analytical tools, and request information to assess the size, composition, and trends in the loan portfolio and off-balance-sheet exposures. Consider the following:

   - Current and planned loan growth in relation to bank capital, risk limits, and adequacy of capital and strategic planning.
   - Segments of high growth and reasons for this growth.
   - Concentrations of credit and the results of portfolio stress testing.
   - Internal portfolio management reports (e.g., loan policy exceptions, credit exceptions, collateral exceptions, and concentrations of credit).
   - Unfunded loan commitments.
   - Deteriorating trends in asset quality indicators.
   - Other information related to risk characteristics of the loan portfolio, including
     – local and national economic indicators.
     – trends at other local financial institutions.
     – new products planned or already initiated.

6. In discussions with bank management, determine the following:

   - How the bank manages the loan portfolio and monitors loan quality.
   - Degree of changes in loan products; lending practices (e.g., underwriting and risk selection standards, and out-of-area lending); service distribution channels; or third-party service providers engaged in origination, servicing, or asset disposal activities since the last examination. Examiners should determine the reasons for significant changes.
   - Potential impact of external or internal factors on asset quality (e.g., local industry reduction or expansion, competition, management and lending staff changes, changes in credit concentrations, or changes in product lines).

7. Obtain asset quality-related information from the examiner assigned to review board minutes. Review minutes of loan committee meetings to understand the bank's lending practices.

8. Obtain and review the bank's loan policies for adequacy and changes since the last examination. Develop a preliminary assessment of the quality of board-approved credit underwriting policy standards in the appropriate credit underwriting assessment module in Examiner View. Refer to the "Credit Underwriting Assessment" module. Provide supporting comments and documentation to support this assessment.

   Consider whether policies effectively address the following:

   - Portfolio objectives, composition, and limits.
   - Underwriting standards for all types of lending in which the bank is engaged.
   - Responsibilities and authorities for those involved in the lending process.
   - Required documentation and supporting analysis for credit approvals and credit administration.
   - Appraisal policies or procedures that establish an effective real estate appraisal and evaluation program.
   - Oversight of third parties engaged in origination, servicing, or asset disposal activities.

   Share an overview of underwriting criteria with loan file workers to use as a reference point to assess whether practices are aligned with bank policy, identify potential policy exceptions, and validate internal exception tracking reports.

9. Based on the foregoing discussions and review, make an initial assessment of which expanded procedures or additional credit underwriting assessments should be completed, if applicable. After consulting with the EIC and supervisory office, add, as appropriate, expanded procedures or credit underwriting assessment modules: (Updated in version 1.1)

***Comptroller's Handbook* booklets (expanded procedures**	**Credit Underwriting Assessment Modules**
• Accounts Receivable and Inventory Financing" (national banks) or OTS Examination Handbook section 214, "Other Commercial Lending" (FSAs) • "Agricultural Lending" • "Asset-Based Lending" • "Commercial Loans" (national banks) or OTS Examination Handbook section 214, "Other Commercial Lending" (FSAs) • "Commercial Real Estate Lending" • "Concentrations of Credit" • "Credit Card Lending" • "Deposit-Related Credit" • "Floor Plan Lending" • "Installment Lending" • "Lease Financing" • "Leveraged Lending" (national banks) or OTS Examination Handbook section 214, "Other Commercial Lending" (FSAs) • "Loan Portfolio Management" (national banks) or OTS Examination Handbook section 201,	• Commercial Lending—General Commercial and Industrial • Large Corporate Lending • Middle Market Lending • Commercial Real Estate Lending—General • Commercial Real Estate Lending—Permanent • Commercial Real Estate Lending—Construction • Commercial Leasing • Leverage Lending • Oil and Gas Lending • Automobile Lending • Credit Card Lending • Home Equity Lending • Other Consumer Lending • Residential Mortgage Lending—Portfolio • Residential Mortgage Lending—Distributed

“Overview: Lending Operations and Portfolio Risk Management” (FSAs) • “Mortgage Banking” • “Oil and Gas Exploration and Production Lending” • “Other Real Estate Owned” • “Residential Real Estate Lending” • “Retail Lending” • “Student Lending” • “Trade Finance and Services”	

10. Obtain the loan trial balance, and select a sample of loans from the bank’s loan portfolio. When selecting the sample, consult with the EIC, and consider the supervisory strategy and information obtained from discussions with bank management. Consider the following:

    - Large-dollar commercial loans.
    - Loan participations (in whole or part) purchased and sold.
    - Loans sourced or originated through brokers and other third parties (including loans acquired through pool purchases).
    - Significant loan concentrations.
    - Recently originated loans in new loan products and in seasoned products or portfolios experiencing rapid growth.
    - Loans securitized and sold that the bank services for investors.
    - Insider loans and loans to affiliates.
    - Loans originated by different branches, loan officers, and underwriters.
    - Lower-rated “pass” and “watch” loans.
    - Loans with exceptions to lending policies, risk selection, and underwriting standards.
    - Loans marked for re-review at the previous examination.
    - Higher-risk lending products, such as leveraged finance, high loan-to-value real estate loans, and subprime loans.
    - Loans or lending concentrations to businesses or industries exhibiting signs of weakness or higher risk.
    - Loans on the problem loan list and loans previously classified, significant past-dues, nonaccruals, troubled debt, and restructured loans.
    - Loans reviewed by credit risk review (i.e., loan review), director’s examinations, or audit.
    - Loans continuously renewed without principal reduction or significant curtailment given the nature of the transaction.
    - Out-of-market or out-of-territory loans.
    - Loans made under the supplemental lending limits program (12 CFR 32.7, “Residential Real Estate Loans, Small Business Loans, and Small Farm Loans (‘Supplemental Lending Limits Program’)”).

    Loans not reviewed in detail should be discussed without preparing line sheets. Discuss-only line sheets may be used to facilitate low-documentation review of credit files.

Because credit risk typically poses the largest single risk to the bank's earnings and capital, and loans are typically the largest asset concentration in most banks, the OCC usually samples a meaningful percentage of loan portfolios.

The loan sample's size and composition should be commensurate with the quantity of credit risk, adequacy of risk management, bank's condition, and objectives of the asset quality review. Examiners should use judgment when determining the focus and extent of loan sampling.

Types of loans in the sample are as important as how much of the portfolio is reviewed. The sample should generally be skewed toward loans that pose more risk in the portfolio, or other pertinent risks as outlined in the supervisory strategy. Examiners should also consider emerging risks when selecting the sample.

FSAs have statutory limits on the types and amounts of loans the banks may originate or in which they may invest. If the bank is a mutual FSA, consider that mutual loan portfolios may be predominately concentrated in residential mortgage loans. While some mutual FSAs originate a moderate and growing level of loans secured by commercial real estate, mutual FSAs tend to be less concentrated in commercial, industrial, and consumer loans than stock FSAs. The different levels of one- to four-family first-lien residential loans is a common distinction between mutual and stock FSAs. For more information, refer to OCC Bulletin 2014-35, "Mutual Federal Savings Associations: Characteristics and Supervisory Considerations."

In a stable, well-managed bank exhibiting few signs of change, examiners should still sample new and pass-rated credits to determine the continued adequacy of loan quality, underwriting practices, and credit risk management.

If the number of exceptions to sound underwriting practices or risk selection practices is significant, or if the bank's risk identification or credit administration is insufficient or weak, the examiner should expand the sample to determine the severity and root cause of these issues and their effect on credit quality. Additional samples may also be required, for example, when banks have significant growth, or when there are changes to the loan or product mix, credit or economic conditions, strategic direction, or key personnel, or when loan portfolio management needs improvement.

11. Use reports or information obtained directly from external sources to verify balances of assets serviced by third parties. Examiners should reconcile balances indicated on the bank's financial records to information provided by the third party. Material differences should be investigated thoroughly.

Objective 2: Determine quantity of credit risk inherent in the loan portfolio.

1. Analyze individual credits, document line sheets sufficiently, and assign a risk rating to each loan reviewed. Refer to risk rating information in the "Rating Credit Risk" booklet

of the *Comptroller's Handbook* or other booklets relevant to the type of loan reviewed. Analysis should include a review of related debt. (Updated in version 1.1)

- Document and support the reasons for each loan rating.
- Use the most recent version of the NCT to conduct the review. (Note: Line sheets are not required for all credit reviews. For example, spreadsheets are often used to document transaction testing of homogenous portfolios such as small business loans or retail loans, and can be an efficient method to document a review targeted to a specific issue (e.g., accrual status, compliance with 12 CFR 34, adequacy of problem loan workout plans). Community bank examinations should generally employ NCT line sheets for commercial loan reviews, but NCT line sheets need not be used for the entire review.)
- Conclusions from the individual transaction reviews for new originations should be used to support the assessment of the quality and direction of underwriting practices in the appropriate credit underwriting assessment module.

2. Evaluate changes in the retail portfolio's size, composition, and growth rate since the last examination. Consider the following:

   - Changes in products, marketing or origination channels, underwriting standards, operations, and technology.
   - Levels and trends in delinquencies, nonaccruals, and losses by product.
   - Level, trend, and performance of loans made with exceptions to loan policies.
   - Level, trend, and performance of accounts that have been re-aged, extended, deferred, renewed, or rewritten.
   - Dependence on third-party relationships for originations, account management, or collection activities.

3. Assess the adequacy of the bank's retail classification and account management policies, processes, and controls. For more information, refer to OCC Bulletin 2000-20, "Uniform Retail Credit Classification and Account Management Policy: Policy Implementation."

   - Use the checklist in the "Retail Lending" booklet of the *Comptroller's Handbook* to determine whether policies and procedures are consistent with OCC Bulletin 2000-20. Examiners should investigate any "no" answers and determine the appropriateness of practices that are different from those in OCC Bulletin 2000-20.
   - Select a sample of retail loans to evaluate the adequacy of the bank's loan classification, account management, and charge-off practices for consistency with sound governance, internal control, risk management principles, and accounting guidance. Choose retail loan samples that include the following:
     – Accounts booked within the last 90 days.
     – Severely delinquent retail loans that have not been charged off (i.e., installment loans past due greater than 120 days and not charged off, and open-end loans past due greater than 180 days and not charged off).
     – Loans that have been re-aged, extended, deferred, renewed, or rewritten.

- Loans that have been placed in temporary or permanent workout or forbearance programs.

While conducting reviews of lending activities, examiners should be alert to, and discuss with the EIC, policies, practices, or product terms that could indicate discriminatory, unfair, deceptive, abusive, or predatory lending issues.

4. Review completed line sheets and summarize loan sample results. The loan portfolio manager should do the following:

   - Determine whether the risk rating, accrual status, and underwriting assessment, if applicable, are accurate and supported for each credit.
   - Reconcile and prepare a summary list of exceptions.
   - Migrate work papers from the National Credit Tool to Examiner View. Update and verify the accuracy of the asset quality statistics under the “Supervisory Activity Data” node.

5. Develop preliminary assessments of the quality and direction of underwriting practices in the appropriate credit underwriting assessment module. Refer to the “Credit Underwriting Assessment” module. Provide supporting comments and documentation to support this assessment. (Updated in version 1.1)

6. Determine credit risk inherent in the loan portfolio as a whole, considering the risk-rating profile, underwriting and risk selection practices, existence of concentrations of credit, loan policy exceptions, credit and collateral exceptions, pricing, collateral coverage, adequacy of analysis and credit administration practices, economic indicators, etc.

Objective 3: Determine quantity of risk from other assets. For more information, refer to the following: (Updated in version 1.1)

- Booklets of the *Comptroller’s Handbook*
  - “Other Real Estate Owned”
  - “Other Assets and Other Liabilities” (national banks)
  - “Cash Accounts” (national banks)
  - “Due From Banks”
- *OTS Examination Handbook* (FSAs)
  - Section 250, “Other Assets/Liabilities”

1. Obtain and review a list of the following items:

   - OREO
   - Repossessed assets
   - Cash items
   - Other asset accounts with material balances

2. Based on the preliminary assessment of risk and using examiner judgment, review a sample of OREO and conclude on the overall quantity of associated risks.

3. Obtain list of classified investments and other findings regarding quality and composition of investments from the examiner evaluating the investment portfolio.

4. In discussion with bank management and based on the review of other assets, determine whether any items should be classified or charged off. (Updated in version 1.1)

Objective 4: Determine adequacy of the ALLL.

1. Determine the appropriateness of the ALLL methodology.

   - Review the ALLL policy to assess conformance with generally accepted accounting principles. Verify that the board reviews the policy at least annually.
   - Review the methodology for accuracy, and conclude on the adequacy of supporting documentation.
   - Evaluate the bank's portfolio segmentation under Accounting Standards Codification (ASC) 450-20, "Loss Contingencies," for reasonableness.
   - If the bank has significant holdings of junior liens, determine whether the ALLL methodology includes sufficient information to adequately assess the probable loss incurred within junior lien portfolio(s). For more information, refer to OCC Bulletin 2012-6, "Interagency Guidance on ALLL Estimation Practices for Junior Liens: Guidance on Junior Liens."
   - Evaluate the reasonableness of the historical loss period under ASC 450-20.
   - If applicable, review loss estimation models to determine conformance with generally accepted accounting principles based on the determination of reasonable model assumptions and adequate documentation supporting the model and its output.
   - Determine the appropriateness of qualitative factors and accompanying adjustments used for the homogenous pools.
   - Assess impaired loan identification and measurement for conformance to ASC 310-10, "Receivables."
   - Determine the adequacy of management information systems (MIS) used to compose the ALLL methodology.

2. Conclude on the adequacy of the ALLL balance. Consider the following:

   - Determine whether ALLL-related ratios (including peer comparison) previously reviewed indicate potential concern regarding the reasonableness of previously reported ALLL balances.
   - Evaluate whether the ALLL balance is directionally consistent with credit trends in the loan portfolio, including loan growth, level, and trend of concentrations, and trends in nonperforming loans.
   - Based on transaction testing of impaired loans analyzed under ASC 310-10 or other relevant transactions, determine whether bank management is recording charge-offs

in a timely manner. If not, determine whether this results in bank management's most recent or prior period ALLL balances being materially deficient.
- If deficiencies are identified in the bank's risk identification and classification process, determine if the most recent or prior-period ALLL balances are materially deficient.
- If the balance is deficient, calculate necessary provision to restore ALLL to an adequate level. Direct bank management to make necessary adjustments to the call report, and share findings with the examiners reviewing earnings and capital. Refer to 12 USC 161, "Reports to Comptroller of the Currency" (national banks), and 12 USC 1464(v), "Reports of Condition" (FSAs).

Examiners should also consider reviewing the separate account, call report Schedule RC-G, "Other Liabilities," for reasonableness of the amount reported for estimated incurred losses on unfunded off-balance-sheet credit exposures.

Objective 5: Determine quality of credit risk management through discussions with key risk managers and analyses of applicable information, including credit review reports. Complete the following procedures related to policies, processes, personnel, and controls, as appropriate.

1. Conclude on the adequacy and effectiveness of board-approved lending and credit policies.

    - Review the bank's lending policies. This may include assessing the following:
        - Lending objectives and risk appetite, including acceptable types of loans, portfolio distribution (concentrations of credit), lending market or territory, risk limits measured as a percentage of capital, approval authorities, and correlation risk among industries in the bank's loan portfolio.
        - Reasonableness of underwriting criteria and documentation standards.
        - Policy requirements for the use of covenants and credit enhancements.
        - Policy requirements for ongoing monitoring activities, including the use of tickler systems, periodic credit reviews and financial statement analysis, and enhanced monitoring for problem loans.
        - Policies related to the appraisal and evaluation program and environmental risk management.
        - Policy requirements for problem loan management.

2. Conclude on the effectiveness of the bank's credit administration practices.

    - Conclude on the overall accuracy and timeliness of the bank's loan rating system. Consider any risk rating differences from the loan sample, problem loan discussions, retail loan review, and conclusions regarding the effectiveness of the credit review function.
    - Determine whether the number and nature of credit, collateral, and policy exceptions; risk rating changes; or other loan review findings raise concerns about the quality of the credit administration function.

- Determine whether the number and nature of underwriting exceptions raise concerns about the quality of policy standards. Provide preliminary conclusions on the adequacy of board-approved credit underwriting policy standards in the "Credit Underwriting Assessment" module. Comment as necessary. (Updated in version 1.1)
- Determine the effectiveness of exception identification and reporting. Consider the following:
  - Frequency of exception reporting
  - Adequacy of exception reporting
  - Reasonableness of limits as a percentage of the loan portfolio
- Consider the bank's appraisal policies, procedures, and practices. Evaluate the bank's appraisal and evaluation program and the bank's compliance with 12 CFR 34, subpart C, "Appraisals." For more information, refer to OCC Bulletin 2010-42, "Sound Practices for Appraisals and Evaluations: Interagency Appraisal and Evaluation Guidelines." (Updated in version 1.1)
- Evaluate the bank's ongoing credit monitoring practices. Consider the following:
  - Adequacy of periodic review requirements, considering frequency and coverage.
  - Problem loan management and monitoring.
  - Timeliness of obtaining and analyzing financial statements.
  - Use of tickler systems for tracking financial statement exceptions and other tracking reports used to monitor the status of pending reviews.
- Conclude on the quality of concentration risk management. Consider whether
  - processes and controls to identify all material concentrations are adequate.
  - risk selection aligns with the board's risk appetite, strategic plan, and capital plan.
  - portfolio stress testing and sensitivity analysis allow the bank to appropriately identify and measure risks posed by concentrations. Refer to OCC Bulletin 2012-33.
  - an examiner-prepared basic portfolio level stress test is needed to measure the risks posed by concentrations.
  - concentration reporting is timely, accurate, and appropriate.
  - risk limits are appropriate in relation to capital, credit risk management, and staffing.

Examiners document conclusions on the quantity of concentration risk and quality of concentration risk management by completing the "Concentrations and Correlations" node in Examiner View and building a concentrations ROE page as appropriate. The concentrations ROE page must be completed when concentration levels that pose a challenge to bank management are identified, or present unusual or significant risk to the bank. Concentration data must always be entered in Examiner View.

3. Conclude on the adequacy of credit personnel.

- Determine whether loan management and personnel are adequate to effectively oversee quantity of credit risk inherent in the loan portfolio. Consider whether
  - staff experience and expertise align with the sophistication and complexity of the products and services offered.

- staff size is sufficient to manage the scope of operations and volume of transactions expected.
- compensation systems promote prudent, long-term growth and performance objectives and comply with applicable regulatory requirements.
- credit department management has demonstrated effective oversight and management of the credit function.

4. Conclude on the quality of control systems over the credit function.

- Determine if the bank has established a system of independent, ongoing credit review. Consider the following:
  - Independence of the credit review function.
  - Qualifications of credit risk review personnel based on level of education, experience, and extent of formal credit training.
  - Adequacy of the scope and depth of reviews.
  - Risk-based work plan with minimum coverage standards.
  - Frequency of credit review (e.g., annually or more frequently based on risk).
  - Accurate and timely problem loan identification.
  - Conclusion on the effectiveness of the risk rating framework.
  - Conclusions on the overall effectiveness of the credit administration function and adherence to the bank's policies and procedures.
  - Formal documentation of findings, including monitoring of adverse findings.
  - Timeliness of correction of deficiencies noted by loan review.
  - Communication to bank management and the board.
- Conclude on the appropriateness of any other credit-related audits that may include loan operational audits, directors' examinations, or the financial statement audit.
- Assess integrity, confidentiality, and availability of data used to record, analyze, and report information related to asset quality. Consider input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to data and procedures in place to monitor system activities. Determine if controls have been independently validated. Coordinate review with examiners responsible for all functional areas of the examination, including internal controls, to avoid duplication of effort. Share findings with the examiner reviewing IT.
- Assess the bank's system of internal controls over the credit function, including pre- and post-funding controls. Consider the relevant controls listed in objective 7 of the Internal Controls and Audit section of the core assessment. Also consider other controls pertinent to the credit function.

Objective 6: Develop preliminary assessments of quantity of credit risk, quality of credit risk management, aggregate credit risk, and direction of credit risk. Refer to the "Risk Assessment System" section of this booklet. Provide relevant information (e.g., related to OREO) to the examiner assigned to assess price risk. Consult with the EIC and other examining staff to identify significant risks that should be considered in other risk assessment conclusions. (Updated in version 1.1)

1. Determine whether to expand the procedures or develop a plan for corrective action. Consider whether

   - bank management can adequately manage the bank's risk.
   - bank management can correct fundamental problems.
   - a strategy should be proposed to address identified weaknesses and discussed with the supervisory office.

Objective 7: After completing expanded procedures, perform verification procedures as appropriate. The extent to which examiners perform verification procedures is decided on a case-by-case basis after consulting with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 8: Conclude the asset quality review.

1. Provide and discuss with bank management the following items: (Updated in version 1.1)

   - Risk rating changes
   - Policy exceptions
   - Loans with underwriting and credit administration exceptions and weaknesses
   - Classified assets
   - Special mention assets
   - Special mention and classified loan write-ups
   - Results of the credit underwriting assessment

2. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the asset quality review relevant to other areas being reviewed.

3. Develop a plan for corrective action. Consider whether

   - examiners identified any deficient practices or violations of laws or regulations.
   - bank management can adequately manage the bank's risks.
   - bank management can correct fundamental problems.

4. Use results of the foregoing procedures and other applicable examination findings to compose comments (e.g., asset quality, concentrations, and MRAs) for the ROE.

5. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

6. In discussions with the EIC, provide preliminary conclusions about the following:

   - Asset quality component rating.
   - Quantity of credit risk.
   - Quality of credit risk management.
   - Aggregate level and direction of credit risk and other applicable risks. Complete summary conclusions in the “Community Bank Risk Assessment” section of this booklet.
   - Credit underwriting assessment modules, including “Credit Underwriting Assessment,” “Overall Credit-Underwriting Assessment, “Commercial Credit–Underwriting Assessment,” “Retail Credit–Underwriting Assessment” and, if applicable, any product-level credit underwriting assessment modules. (Updated in version 1.1)

Credit Underwriting Assessment

(Section updated in version 1.1)

Examiners document underwriting conclusions for overall credit, commercial credit, and retail credit, and as applicable, certain credit products.

Overall Credit	**Commercial Credit**	**Retail Credit**
Board Approved Credit Underwriting Policy Standards ☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak **Credit Underwriting Practices** ☐ Conservative ☐ Conservative/Moderate ☐ Moderate ☐ Moderate/Liberal ☐ Liberal **Direction of Credit Underwriting Practices** ☐ Tightened ☐ Unchanged ☐ Eased	**Board Approved Credit Underwriting Policy Standards** ☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak **Credit Underwriting Practices** ☐ Conservative ☐ Conservative/Moderate ☐ Moderate ☐ Moderate/Liberal ☐ Liberal **Direction of Credit Underwriting Practices** ☐ Tightened ☐ Unchanged ☐ Eased	**Board Approved Credit Underwriting Policy Standards** ☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak **Credit Underwriting Practices** ☐ Conservative ☐ Conservative/Moderate ☐ Moderate ☐ Moderate/Liberal ☐ Liberal **Direction of Credit Underwriting Practices** ☐ Tightened ☐ Unchanged ☐ Eased
Provide support for assessment conclusions:	**Provide support for assessment conclusions:**	**Provide support for assessment conclusions:**

Management

Conclusion: Management is rated (1, 2, 3, 4, or 5).

Introduction

Complete this section's objectives to assign the management component rating. When assigning the rating, the examiner should consult the EIC and other examining staff. Consider the following UFIRS factors:

- Level and quality of board and bank management oversight and support of all the bank's activities.
- Ability of the board and bank management, in their respective roles, to plan for and respond to risks that may arise from changing business conditions or new activities or products.
- Adequacy of, and conformance with, internal policies and controls addressing the operations and risks of significant activities.
- Accuracy, timeliness, and effectiveness of management information and risk-monitoring systems appropriate to the bank's size, complexity, and risk profile.
- Adequacy of audit and internal controls to promote effective operations and reliable financial and regulatory reporting, safeguard assets, and govern compliance with laws, regulations, and internal policies.
- Compliance with laws and regulations.
- Responsiveness to recommendations from auditors and supervisory authorities.
- Bank management's depth and succession.
- Extent to which the board and bank management are affected by, or susceptible to, a dominant influence or concentration of authority.
- Reasonableness of compensation policies and avoidance of self-dealing.
- Demonstrated willingness to serve the legitimate banking needs of the community.
- Overall performance of the bank and its risk profile.

Also consider the following:

- Conclusions from all areas.
- Adequacy of the bank's BSA/AML program. Serious BSA/AML deficiencies create a presumption that the bank's management rating will be adversely affected. Refer to OCC Bulletin 2012-30, "BSA/AML Compliance Examinations: Consideration of Findings in Uniform Rating and Risk Assessment Systems."
- Nature, extent, and severity of deficiencies in the bank's third-party risk management program.

To determine the component rating for management, examiners assess the capability of the board and bank management to identify, measure, monitor, and control the risks of the bank's existing and planned activities.

Objectives and Procedures

Minimum Objective

Determine the management component rating and the aggregate level of reputation, strategic, and operational risk, and consider potential impact of these findings on the bank's risk assessment.

At the beginning of the supervisory activity, discuss with bank management actual or planned changes in the following:

- Senior management or the board
- Strategic plan or strategic planning processes (Updated in version 1.1)

Follow up on significant management-related issues identified by the examiners reviewing the bank's audit and IT programs, including any concerns regarding third-party risk management.

Obtain and review the following information:

- Supervisory strategy
- Results from supervisory activities
- Board minutes and reports since the last examination

If the bank's activities, risk profile, or risk controls have changed significantly, or if review of this information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. Serious deficiencies in the bank's BSA/AML compliance create a presumption that the bank's management component rating will be adversely affected because risk management practices are less than satisfactory. If this review does not disclose significant changes or issues, conclude the management review by completing objective 4.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine scope of the management review.

1. Review supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether review of audit work papers is required.

3. Discuss with the examiner responsible for completing the IT section of the core assessment

    - whether significant deficiencies raise questions about integrity, confidentiality, or availability of data require follow-up.
    - whether there are any deficiencies in the bank's risk management of third-party IT service providers.

4. Obtain and review the following:

    - Board and significant committee minutes since the last examination.
    - Recent representative packet of board meeting materials.
    - Current organizational chart.
    - Findings from OCC monitoring activities.
    - List of directors and their backgrounds.
    - List of significant pending litigation, including description of the circumstances.
    - Details about the bank's blanket bond insurance.
    - List of related organizations (e.g., parent holding company, affiliates, operating subsidiaries, and chain and parallel-owned banking organizations).
    - List of third-party relationships, including changes in those involved in critical activities (e.g., new, terminated, or significantly changed third-party relationships).
    - Summary of payments to bank affiliates.

5. Update list of directors and executive officers in the core knowledge section of Examiner View. (Updated in version 1.1)

Objective 2: Determine the adequacy of bank management and board oversight.

1. At the beginning of the supervisory activity, discuss the following with senior management and other members of bank management:

    - Major risks (current or planned) and bank management's strategies to control them.
    - Board involvement in ensuring adequate risk management system is in effect.
    - Changes, or planned changes, in senior management or the board since the last examination.
    - Board or board committee structure.
    - Plans for growth or acquisition. Consider
        - board-approved strategic plan.
        - financial and operational plans.
        - changes in products, services, delivery channels, third-party service providers, etc.
        - resources and staffing necessary to accomplish strategic goals.
    - Potential impact of management succession plans.

2. Review minutes of board and significant committee meetings held since the last examination. Identify the following:

    - Areas of significant risk in the bank that are not being reported appropriately to the board.
    - Potential or actual violations of laws or regulations. Report violations of insider laws, regulations, and related internal bank policies to the EIC. (Updated in version 1.1)
    - Actual or planned changes in bank operations or strategy and whether these were approved as part of the bank's strategic planning process.
    - Individuals or factions exercising control over the bank.
    - Directors involved in the management of the bank and the degree of their involvement.
    - Designated BSA officer.
    - Changes in bylaws or articles of association.
    - Directors who do not regularly attend board or committee meetings. Determine
        - why they do not attend regularly.
        - whether these directors are fulfilling their fiduciary responsibilities.

3. After reviewing board minutes, provide examiners of other functional areas with significant information acquired about those areas. Consider having the examiner responsible for a functional area review minutes of committees that oversee those areas.

4. Review how the board and bank management select and retain competent staff. Consider the following:

    - Requirements for annual performance reviews of senior management
    - Length of vacancies in key positions
    - Reasonableness of employment contracts
    - Compensation programs
    - Recruitment methods

    Mutual FSAs do not have the same ability to offer stock-or equity-based compensation arrangements that many stock banks are able to offer. Mutual FSAs may use a combination of higher salaries, bonuses, and benefits to overcome this difference. Both mutual and stock banks occasionally use phantom stock plans to provide incentive compensation. The total value of compensation plans should be considered when comparing mutual FSAs' and stock banks' compensation programs. The overarching consideration is that compensation programs should be reasonable in amount and commensurate with the duties and responsibilities of the covered individuals. Mutual FSAs should customize their compensation programs to fit the bank's individual needs, taking into consideration an appropriate balance of risk with reward that is accompanied by effective controls and corporate governance. For more information on mutual FSAs, refer to OCC Bulletin 2014-35.

5. Assess the bank's vulnerability to self-dealing and level of compliance with established laws, regulations, and bank policies regarding insider transactions and activities. Refer to

the “Insider Activities” booklet of the *Comptroller’s Handbook* for more information. (Updated in version 1.1)

6. Review pending or threatened litigation with bank management to determine whether litigation has a potentially significant impact on the financial condition of the bank. Refer to the “Litigation and Other Legal Matters” booklet of the *Comptroller’s Handbook* for more information. (Updated in version 1.1)

7. Review insurance policies (blanket bond, liability, fixed assets and equipment, operating activities, etc.) to determine whether they are current and provide adequate coverage. Consider the following:

   - Blanket bond coverage in relation to the bank’s risk profile and control systems.
   - Compliance with requirements established by the blanket bond company.
   - Board involvement in the insurance process.

   Refer to the “Corporate and Risk Governance” booklet of the *Comptroller’s Handbook* for more information. (Updated in version 1.1)

8. Review the relationship—financial or operational—between the bank and the bank’s related organizations. Determine whether the transactions between the bank and its related organizations comply with applicable laws and regulations and conform to proper accounting standards. Consider the impact on the following:

   - Earnings.
   - Capital.
   - Funds management practices.
   - Management.

   Refer to the following: (Updated in version 1.1)

   - 12 USC 371c, “Banking Affiliates”
   - 12 USC 371c-1, “Restrictions On Transactions With Affiliates”
   - 12 USC 1468, “Transactions With Affiliates (FSAs)
   - 12 CFR 223, “Transactions Between Member Banks and Their Affiliates (Regulation W)”
   - “Related Organizations” booklet of the *Comptroller’s Handbook* (national banks)
   - *OTS Examination Handbook* Section 380, “Transactions With Affiliates and Insiders” (FSAs)
   - *OTS Examination Handbook* Section 730, “Related Organizations” (FSAs)

9. Review how management plans for new, modified, or expanded products or services. Consider the following:

   - Due diligence or feasibility process.

- Financial projections.
- Risk analysis.
- Legal opinions.
- Compliance implications.

For more information, refer to OCC Bulletin 2017-43.

10. Assess the adequacy of the bank's third-party risk management program, particularly for third parties involved in critical activities. Obtain relevant conclusions regarding the bank's risk management of third-party IT service providers from the examiner responsible for the IT review, and incorporate these conclusions into the overall assessment of the bank's third-party risk management program. Consider the following:

    - Whether the bank has an effective process to manage risks related to third-party relationships in a manner consistent with the bank's strategic goals, organizational objectives, and risk appetite.
    - The adequacy of the bank's due diligence and approval processes for third parties.
    - Whether the board approves contracts with third parties that involve critical activities.
    - The adequacy of bank management's ongoing monitoring of third parties.
    - The adequacy of processes bank management or the board use to take appropriate action to remedy significant deterioration in a third party's performance.

    For more information regarding third-party risk management, refer to OCC Bulletins 2013-29 and 2017-21.

    If deficiencies have been identified upon completing this procedure, determine whether to expand the scope of the review. Select from the examination procedures in OCC Bulletin 2017-7 as appropriate.

Objective 3: Determine the quality of risk management systems.

1. After completing the previous objectives, consult with other examining staff to make preliminary conclusions on adequacy of risk management systems. Consider whether

    - bank management recognizes weaknesses and understands existing or emerging risks.
    - bank management measures risk in an accurate and timely manner.
    - the board establishes, communicates, and controls risk limits.
    - bank management accurately and appropriately monitors established risk levels.

2. Consult with other examining staff to determine whether findings from other areas (e.g., quantity of risk, quality of risk management practices, direction of risk, or aggregate risk) affect the management conclusion. Refer to the "Risk Assessment System" section of this booklet. Comment as necessary.

Objective 4: Conclude the management review.

1. Consult with the EIC and supervisory office to develop action plans for addressing supervisory concerns before conducting the exit meeting. Consider bank management's ability to correct the bank's fundamental problems.

2. Consult with the EIC and other examining staff to identify and communicate to examiners conclusions and findings from the management review that are relevant to other areas being reviewed.

3. Use results of the foregoing procedures, conclusions on quality of audit and system of internal controls, BSA/AML examination findings, and other applicable examination findings to compose comments (e.g., management/administration and MRAs) for the ROE.

4. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

5. In discussion with all examining staff, draw preliminary conclusions about the following:

   - Quantity of operational, reputation, compliance, and strategic risks.
   - Quality of operational, reputation, compliance, and strategic risk management.
   - Aggregate level and direction of operational, reputation, compliance, and strategic risk. Complete the summary conclusions in the "Community Bank Risk Assessment" section of this booklet.
   - Supervisory strategy recommendations.

Earnings

Conclusion: Earnings are rated (1, 2, 3, 4, or 5).

Introduction

Complete this section's objectives to assign the earnings component rating. When assigning the rating, the examiner should consult the EIC and other examining staff. Consider the following UFIRS factors:

- Level of earnings, including trends and stability.
- Ability to provide for adequate capital through retained earnings.
- Quality and sources of earnings.
- Level of expenses in relation to operations.
- Adequacy of the budgeting systems, forecasting processes, and MIS in general.
- Adequacy of provisions to maintain the ALLL and other valuation allowance accounts.
- Earnings exposure to market risks such as interest rate and price risks.

In rating earnings, the examiner should also assess the sustainability of earnings and the potential impact the quantity of risk and quality of risk management could have on earnings.

Objectives and Procedures

Minimum Objective

Determine the earnings component rating and the potential impact on the bank's risk assessment.

At the beginning of the supervisory activity, discuss with bank management the following:

- Actual or planned changes in the bank's budget or budgeting process.
- The bank's present condition and future plans.
- Earnings trends or variances.
- Changes in the bank's call report preparation processes and whether re-filings have occurred.

As requested, follow up on significant earnings-related audit or IT issues identified by the examiners reviewing the bank's audit and IT programs.

Obtain and review the following information:

- Supervisory strategy.
- Results from supervisory activities.

- Financial reports (e.g., UBPR), applicable OCC reports or analytical tools, and budget and variance reports.

Considerations for mutual FSAs: Earnings are essential to any bank's viability but are especially important for mutuals, which build capital primarily through the accumulation of earnings. Examiners evaluate mutuals' earnings for stability, trends, quality, and level. The mutual's operations are also evaluated, and additional factors, such as capital level, credit risk, and interest rate risk (IRR), are considered. Mutuals generally have lower earnings, net interest income, noninterest income, NIM, and return on equity relative to stock FSAs. On the other hand, mutuals have more stable levels of profitability. Mutuals, like stock banks, need to generate sufficient earnings to meet expenses, pay interest on deposits, and satisfy regulatory capital requirements. Whenever possible, examiners should compare mutuals with other mutuals to provide a more meaningful review of the various financial ratios to identify problem trends and outliers. For more information, refer to OCC Bulletin 2014-35.

If the bank's activities, risk profile, or risk controls have changed significantly, or if the minimum objective review raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the earnings review by completing objective 9.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine scope of the earnings review.

1. Review supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is necessary. (Updated in version 1.1)

3. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about integrity, confidentiality, or availability of data and require follow-up.

4. If not previously reviewed, obtain and review the following:

    - Most current balance sheet and income statement
    - Most recent budget, variance reports, and related items
    - Most recent annual and quarterly reports
    - Findings from OCC monitoring activities

Objective 2: Determine the quality and composition of earnings.

1. Review applicable information to identify trends. Consider the following:

   - Results from OCC monitoring activities.
   - Bank management reports used to monitor and project earnings.
   - Financial reports (e.g., UBPR), applicable OCC reports or analytical tools, and the bank's present condition and future plans.

2. Obtain earnings-related information from the examiner assigned to review board minutes.

3. Discuss earnings trends and variances with bank management. Coordinate discussions with those examining other functional areas.

4. Analyze earnings composition. Focus on the following:

   - Core earnings
   - NIM
   - Noninterest income and expenses
   - Loan loss provisions
   - Off-balance-sheet items
   - Changes in balance-sheet composition
   - Impact of fair value adjustments (ASC 320, "Investments – Debt and Equity Securities")
   - Loan and deposit pricing
   - Earnings from affiliate transactions
   - Earnings from high-risk lines of business

5. If the bank has fiduciary powers, obtain fiduciary-related earnings information and evaluate the quantity and quality of fiduciary earnings. Coordinate with the examiner responsible for the asset management review. Refer to factors listed in the Uniform Interagency Trust Rating System (UITRS), including the following:

   - Level and consistency of profitability in relation to business volume and characteristics.
   - Methods used to allocate direct and indirect expenses.
   - Effects of fiduciary settlements, surcharges, and other losses.

6. Determine the root causes of significant trends and the impact of nonrecurring items. Consider the following:

   - Whether earning trends are improving, stable, or declining.
   - Bank earnings compared with budget and peer group. (Updated in version 1.1)

- Adequacy of bank earnings in relation to
  - debt service requirements of the bank's owner.
  - dividend-paying capacity. (If appropriate—and in conjunction with the examiner reviewing capital—review and discuss with bank management the bank's dividend plans.)

7. Adjust the bank's reported earnings to reflect results of the examination and project current year's net income. Consult with the EIC and distribute adjustments to examining staff.

Objective 3: Determine the adequacy of the bank's budgeting process.

Review and determine reasonableness of the bank's budget. Consider the following:

- Economic, market, and other assumptions
- Historical performance of the budgeting process
- Examination results
- Changes in bank management or strategies
- Variance reports and other supplemental budgeting reports

Objective 4: Determine adequacy of management processes to prepare call reports and validity of call report data.

1. If not previously reviewed, obtain and review the following:
   - The most recent call report
   - The bank's work papers for that call report

2. Review and determine the adequacy of the bank's process for preparing call reports. Determine whether the process is periodically and independently verified.

3. Verify call report data. Consider the following:
   - Asking other examiners whether their findings agree with call report information.
   - Determining whether follow-up is needed.
   - Testing call report accuracy by randomly checking selected call report line items against the bank's work papers and source documents. Consider having examiners assigned to review other functional areas verify the appropriate schedule in the call report.
   - Results of any call report audits.

Objective 5: Determine the risk to bank earnings posed by the aggregate level or direction of applicable risks.

Consult with the EIC and other examining staff to decide whether the aggregate level or direction of risk has an adverse impact on the bank's current or future earnings. Refer to the "Risk Assessment System" section of this booklet.

Objective 6: Determine the quality of risk management systems through discussions with key risk managers and analysis of applicable internal or external audit reports.

1. Assess the bank's system of internal controls over income and expense accounts. Consider relevant controls listed in objective 7 of the "Audit Functions and Internal Control" section of the core assessment in this booklet. Also consider other controls pertinent to earnings.

2. Assess integrity, confidentiality, and availability of data used to record, analyze, and report information related to earnings. Consider input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to data and procedures in place to monitor system activities. Determine if controls have been independently validated. Coordinate this review with examiners responsible for all functional areas of the examination, including internal controls, to avoid duplication of effort. Share findings with the examiner reviewing IT.

Objective 7: Determine whether to expand procedures or develop a plan for corrective action. Consider whether

- bank management can adequately manage the bank's risks.
- bank management can correct fundamental problems.
- to propose a strategy to address identified weaknesses and discuss strategy with the supervisory office.

Refer to appropriate booklets of the *Comptroller's Handbook* for expanded procedures.

Objective 8: After completing expanded procedures, determine whether verification procedures should be performed.

The extent to which examiners perform verification procedures is decided on a case-by-case basis after consulting with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 9: Conclude the earnings review.

1. Use results of the foregoing procedures and other applicable examination findings to compose comments (e.g., earnings, MRAs, or violation write-ups) for the ROE. (Updated in version 1.1)

2. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the earnings review relevant to other areas being reviewed.

3. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

4. In discussion with the EIC, provide preliminary strategy recommendations for the next supervisory cycle.

Liquidity

Conclusion: Liquidity is rated (1, 2, 3, 4, or 5).

Introduction

Complete this section's objectives to assign the liquidity component rating. When assigning the rating, the examiner should consult the EIC and other examining staff. Consider the following UFIRS factors:

- Adequacy of liquidity sources to meet present and future needs and ability of the bank to meet liquidity needs without adversely affecting operations or condition.
- Availability of assets readily convertible to cash without undue loss.
- Access to money markets and other sources of funding.
- Level of diversification of funding sources, both on- and off-balance-sheet.
- How much the bank relies on short-term, volatile sources of funds, including borrowings and brokered deposits, to fund longer-term assets.
- Trend and stability of deposits.
- Ability to securitize and sell certain pools of assets.
- Capability of bank management to properly identify, measure, monitor, and control the bank's liquidity position, including effectiveness of funds management strategies, liquidity policies, MIS, and contingency funding plans (CFP).

Objectives and Procedures

Minimum Objective

Determine the liquidity component rating, quantity of liquidity risk, and quality of liquidity risk management.

At the beginning of the supervisory activity, discuss with bank management actual or planned changes in the following:

- Liquidity risk management
- Liquidity planning or funding sources and needs
- Investment strategy
- Liquidity policy or CFP

As requested, follow up on significant liquidity-related audit or IT issues identified by the examiners reviewing the bank's audit and IT programs.

Obtain and review the following information:

- Supervisory strategy.
- Results from supervisory activities.
- Financial reports (e.g., UBPR), applicable OCC reports or analytical tools, and liquidity reports.
- Investment trial balance.
- Asset-liability committee (ALCO) minutes and reports since the last supervisory activity.

Refer to OCC Bulletin 2010-13, "Final Policy Statement: Interagency Policy Statement on Funding and Liquidity Risk Management" for more information. (Updated in version 1.1)

If the bank's activities, risk profile, or risk controls have changed significantly, or if review of this information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the liquidity review by completing objective 15.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the liquidity review.

1. Review supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is necessary. (Updated in version 1.1)

3. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about integrity, confidentiality, or availability of data and require follow-up.

4. Obtain and review the following items:

    - Most recent liquidity reports.
    - CFP.
    - Investment trial balance.
    - List of investments purchased and sold (within a reasonable time frame).
    - List of securities acquired using the bank's lending authority.
    - Findings from monitoring activities.
    - Other information or reports management uses (ALCO packages and minutes, etc.).

- Financial reports (e.g., UBPR) and applicable OCC reports or analytical tools. (Updated in version 1.1)

5. Discuss current investment, liquidity, and funds management strategies with bank management.

Objective 2: Determine whether available liquidity sources are adequate to meet current and potential needs.

1. Evaluate volume and trends of sources of liquidity available to meet liquidity needs.

From assets:

- Compare level of money market assets and other liquid assets (easily convertible into cash) with current and potential short-term liquidity needs.
- Determine amount of free (unencumbered) marketable investment securities available for cash conversion or collateral for available borrowing lines.
- Determine level and impact of asset depreciation.
- Determine the distribution of securities designated “held-to-maturity” and “available-for-sale.”
- Determine adequacy of cash flows (e.g., payments, prepayments, or maturities) from such assets as loans, investments, and off-balance-sheet contracts.
- Review other potential sources of asset liquidity (e.g., securitization or loan sales), and determine trends in pricing and spreads (e.g., market acceptance).

From liabilities:

- Compare estimated cash flows to short-term liquidity needs.
- Consider the bank’s capacity to increase deposits through pricing and direct-marketing campaigns to meet medium- and long-term liquidity needs.
- Consider the bank’s capacity to borrow under the Federal Home Loan Bank collateralized loan program or other similar collateralized borrowing facilities. Assess the availability of required collateral.
- Consider the capacity to issue longer-term liabilities and capital to meet medium- and long-term liquidity needs. Options may include
  - deposit-note programs.
  - medium-term note programs.
  - subordinated debt.
  - trust preferred securities.
- Consider the capacity and collateral available to borrow from the Federal Reserve discount window and whether the bank qualifies for the primary or secondary borrowing program.

2. Identify volume and trends of liquidity needs by reviewing the following:

   - Historical and prospective behavioral cash flow reports, sources and uses analyses, and behavioral gap reports used by bank management to identify expected liquidity requirements over short-, medium-, and long-term horizons. This review should include an assessment of
     – bank management's support for significant assumptions and projections in prospective cash flow and behavioral gap reports.
     – reasonableness and consistency of assumptions and projections with historical performance and bank management's budgets and operating forecasts.
   - Static and prospective policy limits, including compliance with those limits.
   - Projected liability reductions, including
     – managed balance-sheet restructuring and
     – potential erosion due to credit-sensitive funds providers.
   - Potential unanticipated asset growth due to impairment in the bank's ability to sell or securitize assets.
   - Potential off-balance-sheet requirements.

Objective 3: Determine impact of the cost of liquidity on the bank's ability to generate reasonable profits.

1. Review the level and trend in funding costs and the impact on the bank's NIM and overall earnings. Determine the following:

   - The bank's NIM performance and causes for changes since the last examination.
   - Level and trend in the spread between liability costs and assets they fund.
   - Comparison of retail and wholesale deposit rates against local and national competitors.
   - Changes in deposit funding costs in comparison with peer banks, market interest rates, and asset yields.
   - Reasons for change in the rate or spread of other wholesale deposit sources.
   - Whether anxiety for income has hampered prudent liquidity actions.

Objective 4: Determine stability, credit and rate sensitivity, and character of the bank's deposit structure.

1. Analyze reports generated from the bank's internal MIS, UBPR data, and applicable OCC reports or analytical tools on insured deposits to determine the following:

   - Changes and trends in deposit volume and product mix.
   - Material shifts between deposit types and reasons for these shifts.
   - Offering rates and costs for all major deposit types, including those gathered through the internet and deposit-splitting arrangements, compared with peer banks and market interest rates.
   - Ability and likelihood of renewal or retention of these funds at maturity.

- Bank management's deposit pricing policies and the success of recent pricing decisions.
- Success of recent branch expansion and marketing efforts to attract and retain deposit relationships.

2. Review list of deposits greater than $250,000 (i.e., uninsured deposits). To determine stability of these accounts, discuss with bank management the following:

   - Aggregate number and volume of these accounts and degree of the bank's reliance on this funding source.
   - Nature of account holders' relationship with the bank (insider, multiple product or service relationships, location of account holder, and proximity to the bank's branch network).
   - Rate paid on these accounts relative to local and national market competitors.
   - Whether the aggregate dollar amount of these accounts originated through an intermediary (brokered deposits).
   - Concentrations.
   - Ability to retain and replace these funds.
   - Recent success of marketing efforts related to these accounts.
   - Pledging requirements and bank management's controls over collateral availability.
   - Policies of large wholesale funds depositors and whether the policies require them to reduce or remove funds on deposit because of a decline in the bank's credit rating or deterioration in the bank's financial condition.
   - Competitive pressures, economic conditions, or other factors that may affect retention of these deposits.

Objective 5: Evaluate level of risk in wholesale and other nondeposit funding activities.

1. Determine the bank's level of reliance on wholesale funding and other borrowings.

2. Through discussion with bank management and analysis of relevant bank data, determine the following:

   - Purpose of the bank's wholesale funding activities and strategy for the current or future use of these funds. (Are they temporary or permanent?)
   - Assets or activities being funded. If funds are part of an effort to leverage capital, consult with the examiner reviewing sensitivity to market risk and determine if bank management properly understands risks associated with this strategy and whether bank management measures, monitors, and controls these risks.
   - Profitability or spread between these sources and their uses. Determine reasonableness of these profits and compare with bank management's objectives and risks assumed. This step should be coordinated with the examiner(s) evaluating bank earnings and sensitivity to market risk.
   - Types of maturity mismatches that exist between wholesale sources and the assets they fund.

- Structural characteristics of wholesale funding sources (call or put options, complex interest rate rules or calculations, and complex prepayment schedules, etc.), liquidity risks they present, and bank management's understanding and ability to control those risks.
- Whether there has been deterioration in the bank's ability to raise or renew wholesale funds by reviewing such items as
  - interest rates paid by the bank for these funds that exceed prevailing market rates.
  - impact of costs associated with these funds on bank profitability.
  - the bank's credit rating.
  - frequent or recent changes in wholesale lenders.
  - changes in sensitivity to credit risk of the bank's wholesale funding providers.
  - changes in amount and availability of collateral.
  - requests for, increases in, or changes to collateral requirements of wholesale funding providers.
  - significant concentrations in these funding sources.
  - changes in the bank's Federal Reserve discount window status (primary or secondary lending program).

Objective 6: Determine whether adequate contingent funds are available to meet the needs required in liquidity stress or crisis scenarios. Refer to objective 11 for procedures regarding the bank's CFP. (Updated in version 1.1)

1. Determine impact of current or potential deterioration in the bank's credit or reputation on liquidity and ability of identified contingent sources to support related outflows of funds.

2. Assess impact of aggressive short- or longer-term growth patterns or strategies.

3. Determine impact of a disruption to the bank's asset sales or securitization activities. Consider the following:

   - Level of reliance on these funding sources.
   - Availability of contingent funding sources and capital if the bank has to refund or repurchase a portion or all of these assets.

4. Consider potential effects of destabilization in the market or trade area caused by the following:

   - Competitor or peer bank failure.
   - General market trends (e.g., net emigration from the bank's market area).
   - Disintermediation (i.e., loss of deposits).
   - Changes in investor preference (e.g., to mutual funds).
   - Stock or real estate market declines resulting in reduced customer wealth.
   - Systemic technology failure.

Objective 7: Assess appropriateness and integrity of corporate governance over liquidity risk management. (Updated in version 1.1)

1. Review senior management structures to determine adequacy in overseeing and managing the bank's liquidity. Consider the following:

   - Designation of a representative ALCO or other management decision-making body.
   - Whether ALCO composition includes managerial and departmental leadership necessary to communicate issues integral to assessing liquidity and to carry out tactical and strategic initiatives relevant to liquidity management.
   - Frequency and documentation of ALCO meetings and adequacy, accuracy, and timeliness of the reports presented.
   - Decisions made by ALCO and validation of follow-up, including policy compliance assessments and ongoing review of open issues.
   - Technical and managerial expertise and responsibilities of management and personnel involved in liquidity management.
   - Clear delineation of centralized and decentralized liquidity management responsibilities.

Objective 8: Determine that liquidity policies, procedures, and limits are appropriate for the bank's size, complexity, and sophistication.

1. Review and discuss with bank management liquidity policies, procedures, and risk limits, and determine their appropriateness and comprehensiveness with respect to the following:

   - Identification of objectives and strategies of the bank's liquidity management and its expected and preferred reliance on various sources of funds to meet liquidity needs under alternative scenarios.
   - Clear delineation of responsibility and accountability over liquidity risk management and management decision making.
   - Specification of and rationale for quantitative limits and guidelines that define acceptable level of risk for the bank. Examples include use of maximum and targeted amounts of projected cash flow mismatches, liquidity reserves, volatile liabilities, collateral usage, maximum usage of borrowing capacity, and funding concentrations.
   - Specification of methods used to measure and monitor liquidity risk and their frequency.
   - Definition of specific procedures and approvals necessary for exceptions to policies, limits, and authorizations.

Objective 9: Assess adequacy of the bank's liquidity risk measurement systems.

1. Review liquidity risk measurement policies, processes, methodologies, models, and assumptions. Discuss the following with bank management: (Updated in version 1.1)

- Adequacy and comprehensiveness of cash flow analyses and sources and uses of funds projections used to manage liquidity.
- Appropriateness and comprehensiveness of the scenarios analyzed and reported for cash flow and sources and uses projections. Consider impact of the following on the bank's projections:
  - Volatility or unpredictability of the bank's cash flows
  - Changes to business strategies
  - Current interest rate environment
  - Local and national economic conditions
- Appropriateness of summary measures and ratios to reflect adequately the bank's liquidity risk profile.
- Appropriateness of the identification of stable and volatile sources of funding.
- Validity of assumptions used to construct liquidity risk measures and frequency of management's review.
- Comprehensiveness and breadth of alternative contingent liquidity scenarios incorporated in the ongoing estimation of liquidity needs.
- Frequency, independence, and scope of procedures to validate models used to quantify liquidity risk.

2. Assess integrity, confidentiality, and availability of data used to record, analyze, and report information about liquidity. Consider input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to data and procedures in place to monitor system activities. Determine if these controls have been independently validated. Coordinate this review with examiners responsible for all functional areas of the examination, including internal controls, to avoid duplication of effort. Communicate findings to the examiner reviewing IT. Consider whether reports are sufficient for management or the board, as applicable, to monitor the following: (Updated in version 1.1)

   - Compliance with risk limits
   - Sources and uses of funds
   - Funding concentrations
   - Funding costs
   - Availability under wholesale funding lines
   - Projected funding needs

Objective 10: Determine whether policies and processes regarding wholesale funding are adequate.

1. Review wholesale funding policies and determine whether they

   - designate lines of authority and responsibility for decisions.
   - outline objectives of bank wholesale funding activities.
   - describe the bank's wholesale funding philosophy relative to risk considerations (e.g., leverage/growth or liquidity/income).

- control concentration exposure by diversifying sources and staggering maturities. Determine whether funding decisions are based largely on cost.
- limit wholesale funds by amount outstanding, specific type, individual source, market source, or total interest expense.
- provide a system of reporting requirements to monitor wholesale funding activity.
- provide controls over wholesale funding cash flow uncertainty by limiting amount and type of embedded options.
- require material strategies and transactions be reviewed and approved by the board, a committee (e.g., ALCO), or senior management. (Updated in version 1.1)
- review and revise established policy at least annually.

Objective 11: Assess adequacy of the bank's CFP. (Objective and underlying procedures updated in version 1.1)

1. Review the bank's CFP. Determine whether bank management is properly planning for contingent liquidity in unexpected or emergency situations. Review the following:

   - Liquidity events identified in the CFP and adequacy of cash flows and other sources to meet liquidity needs during those events. (This review should consider assessment of the reasonableness of all material assumptions used in the planning process.)
   - Identified market disruptions (nationally and within the bank's trade area) and adequacy of contingent liquidity to meet short- and long-term funding needs.

   For more information on CFPs, refer to OCC Bulletin 2010-13, "Final Policy Statement: Interagency Policy Statement on Funding and Liquidity Risk Management" and OCC Bulletin 2003-36, "Liquidity Risk Management: Interagency Advisory on the Use of the Federal Reserve's Primary Credit Program in Effective Liquidity Management."

2. Review the CFP and minutes from ALCO meetings and board meetings. Discuss with bank management adequacy of the bank's liquidity contingency planning processes.

   Consider the following:

   - Customization of CFP to fit the bank's liquidity risk profile.
   - Identification of potential sources of liquidity under stress events.
   - Breadth of potential stress triggers and events and analyses of various levels of stress to liquidity that can occur under defined scenarios.
   - Quantitative assessment of short- and intermediate-term funding needs in stress events.
   - Reasonableness of assumptions used in forecasting potential contingent liquidity needs and frequency of bank management's review of these assumptions to determine whether they remain valid.
   - Comprehensiveness in forecasting cash flows under stress conditions, including incorporation of off-balance-sheet cash flows.

- Use of contingent liquidity risk triggers to monitor, on an ongoing basis, the potential for contingent liquidity events.
- Consideration of the limitations of payment systems and their operational implications to the bank's ability to access contingent funding.
- Operating policies and procedures to be implemented in stress events, including assignment of responsibilities for communicating with various stakeholders.
- Prioritization of actions for responding to stress situations.

Objective 12: Develop preliminary assessments of quantity of liquidity risk, quality of liquidity risk management, aggregate liquidity risk, and direction of liquidity risk. Refer to the "Risk Assessment System" section of this booklet. Consult with the EIC and other examining staff to (1) identify significant risks that should be considered in risk assessment conclusions, and (2) decide whether aggregate level or direction of risk identified during the liquidity review has had, or is expected to have, an adverse impact on the bank's capital or earnings.

Objective 13: Determine whether to expand the procedures or develop a plan for corrective action.

Consider whether

- bank management can adequately manage the bank's risk.
- bank management can correct fundamental problems.
- a strategy should be proposed to address identified weaknesses and discussed with the supervisory office.

Refer to the "Liquidity" booklet of the *Comptroller's Handbook* for expanded procedures. (Updated in version 1.1)

Objective 14: After completing expanded procedures, determine whether verification procedures should be performed.

The extent to which examiners perform verification procedures is decided on a case-by-case basis after consulting with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 15: Conclude the liquidity review.

1. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the liquidity review that are relevant to other areas being reviewed.

2. Use results of the foregoing procedures and other applicable examination findings to compose comments (e.g., liquidity adequacy, liquidity management processes, or MRAs) for the ROE.

3. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

4. In discussion with the EIC, provide preliminary conclusions about the following:

    - Quantity of liquidity risk.
    - Quality of liquidity risk management.
    - Aggregate level and direction of liquidity risk or other applicable risk. Complete summary conclusions in the “Community Bank Risk Assessment” section of this booklet.
    - Supervisory strategy recommendations.

Investment Portfolio and Bank-Owned Life Insurance

Conclusion: The assessment of the investment portfolio and bank-owned life insurance should be included in the asset quality rating.

Introduction

Complete this section's objectives to assess relevant risks in the bank's investment portfolio and bank-owned life insurance (BOLI) and quality of management and board oversight of investment portfolio activities. The examiner should consult the EIC and other personnel when completing these assessments. Consider the following factors when assessing the investment portfolio:

- Nature, level, and complexity of relevant investment portfolio risks.
- Investment portfolio strategies and future plans.
- Ability of bank management to adequately understand and monitor relevant risks.
- Board and bank management oversight policies, practices, and procedures.

Objectives and Procedures

Minimum Objective

Determine quality of oversight of the investment portfolio, including BOLI. Evaluate how and to what degree investments contribute to relevant risk areas.

At the beginning of the supervisory activity, discuss with bank management actual or planned changes in the following:

- Investment portfolio strategies
- Investment risk appetite or types of securities purchased
- Policies or procedures governing investments

As requested, follow up on significant investment and BOLI-related audit or IT issues identified by the examiners reviewing the bank's audit and IT programs.

Obtain and review the following information:

- Supervisory strategy
- Results from supervisory activities
- Financial reports (e.g., UBPR) and applicable OCC reports and analytical tools
- Investment portfolio trial balance
- Investment portfolio analytics

If the bank's activities, risk profile, or risk controls have changed significantly, or if the review of this information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the review by completing objective 10.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the investments and BOLI review. (Updated in version 1.1)

1. Review supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is required.

3. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about integrity, confidentiality, or availability of data and require follow-up.

4. Obtain and review the following items:

   - Internal audit reports and management responses.
   - Portfolio price sensitivity.
   - Portfolio yields.
   - Portfolio appreciation/depreciation.
   - Whether a large portion of the portfolio was acquired during a short time period or whether it has a concentration in assets with embedded options or maturity dates.
   - Potentially higher risk holdings, such as
     - zero coupon bonds.
     - securities denominated in a foreign currency.
     - securities with low credit ratings.
     - nonrated securities.
     - long maturities.
     - variable principal redemption bonds.
     - floating rate assets with low interest rate caps or long periods between rate resets.
     - structured products. (Updated in version 1.1)

   Refer to OCC Bulletin 2009-15, "Investment Securities: Risk Management and Lessons Learned" (national banks), Thrift Bulletin 73a, "Investing in Complex Securities" (FSAs), and *OTS Examination Manual* section 540, "Investment Securities." (Updated in version 1.1)

5. Contact and discuss the following with the bank's investment portfolio officer and money market personnel:

    - Significant risk issues and management strategies.
    - Significant changes in policies, strategies, procedures, controls or personnel.
    - Whether the bank emphasizes liquidity, yield, or total return in its investment activities. (Updated in version 1.1)
    - How bank management supervises risks (e.g., types of reports reviewed or frequency of committee meetings).
    - Degree of price sensitivity of the investment account, and how the bank measures it.
    - Volume of securities with options.
    - Whether the bank owns variable principal redemption bonds (i.e., securities for which the maturity amount may be less than par because of a formula that determines the redemption amount).
    - Practices for documenting pre-purchase analyses.
    - Whether and extent to which the bank uses its lending authority to acquire securities.
    - Whether the bank owns securities denominated in a foreign currency.
    - Issues identified by internal or external auditors.
    - The bank's philosophy for taking credit risk in the portfolio.
    - Distribution of credit ratings and existence of defaulted securities.
    - Whether the bank uses outside consultants to manage the portfolio or execute purchase and sale transactions.
    - Level of unrealized appreciation or depreciation.
    - The bank's tax position and plans to acquire tax-advantaged assets (including BOLI).
    - Credit or accounting concerns related to the portfolio, including ASC 825-10 implications.

6. Develop a preliminary risk assessment and discuss it with the EIC for perspective and examination planning coordination. Consider the following:

    - Purchases and sales between examinations.
    - Policy or strategy changes.
    - The bank's reliance on the investment portfolio for income.
    - Price sensitivity or credit concerns raised from preliminary discussions with bank management.

Objective 2: Determine appropriateness and effectiveness of the risk management practices of the investment portfolio.

1. Evaluate board and senior management oversight. Consider the following:

    - Procedures for approving major policies.
    - Annual review of investment strategies and policies.
    - Establishment of risk limits and procedures to promote compliance.

- How well directors and bank management not involved directly or daily in investment activities understand those activities.

2. Review pre-purchase analyses of recent investments, and determine whether analyses provide adequate information to understand the price sensitivity of the security. For more information, refer to OCC Bulletin 1998-20, "Investment Securities: Policy Statement." Refer also to OCC Bulletin 2012-18, "Alternatives to the Use of External Credit Ratings in the Regulations of the OCC: Final Rules and Guidance."

3. Determine whether limits (pre-purchase and portfolio sensitivity) established by bank management are reasonable and serve as an appropriate subset of bank-wide IRR limits, given the bank's capital, earnings and management's expertise.

4. Evaluate credit risk management of the portfolio. Assess whether the process establishes an appropriate framework for pre-acquisition credit due diligence that analyzes the repayment capacity of the issuer. Confirm whether the bank management process regularly monitors holdings so risk ratings are reviewed and updated when significant new information is received.

5. Determine how well bank management monitors the investment portfolio. Consider the following:

   - Whether significant risks in the bank's investment activities are understood and properly reported.
   - Completion and documentation of stress testing on the types of securities as required in the bank's investment policy or procedures.
   - Periodic evaluations of aggregate risk exposure and the overall performance of the investment portfolio.

Objective 3: Evaluate the quality of the investment portfolio as a potential source of liquidity.

1. Consider the following:

   - Percentage and quality of investment portfolio that is unpledged.
   - Level and impact of portfolio depreciation.
   - Maturity distribution and average life sensitivity of the investment portfolio.
   - Distribution of securities designated as held-to-maturity (HTM) and available-for-sale (AFS).
   - Marketability of AFS securities.
   - Trends in monthly cash flow from the investment portfolio.
   - Potential impact of embedded options on cash-flow patterns.
   - Volume and quality of securities not priced or securities that show a constant price of par.

Objective 4: Assess the level of credit risk in the investment portfolio.

1. Review the UBPR and the bank's investment reports to evaluate the following: (Updated in version 1.1)

   - Investment yields and market values.
   - Investment portfolio ratings distribution.
   - Holdings of structured products.
   - Significant holdings of nonrated securities, BOLI, below-investment-grade securities, zero or low coupons, and long maturities.

2. Evaluate credit analysis performed on investment securities and determine whether the level of due diligence is appropriate.

3. Review credit analysis on nonrated securities and assess whether securities are the credit equivalent of investment grade.

4. Evaluate holdings of structured products to determine whether risks in these securities are understood and consistent with bank policy. Determine whether bank management analyzed cash-flow modeling assumptions, including default and recovery rates, collateral risk, structural risk, and call risk.

5. Determine whether securities acquired using the bank's lending authority conforms to the bank's lending policies for credit analysis, underwriting, and approval.

6. Assess trend in credit quality of the investment portfolio between examinations. Determine whether there has been a significant change in the credit risk profile and whether that change has been appropriately managed.

7. Determine whether there are issues in the portfolio that are ineligible, in default, or below investment grade. Classify defaulted or below-investment-grade securities, and distribute findings to examiners reviewing asset quality, earnings, and capital adequacy. Refer to OCC Bulletin 2013-28, "Classification of Securities: Interagency Guidance," and OCC Bulletin 2012-18.

8. If a security is rated below investment grade, assess the security structure and determine if that security is providing credit enhancement to other tranches. If so, refer to 12 CFR 3 to determine whether the bank is appropriately applying capital requirements for that security. Distribute those findings to the examiner assessing capital adequacy.

9. Review credit information for securities purchased under the "reliable estimates" authority (12 CFR 1.3(i), "Securities Held Based on Estimates of Obligor's Performance" (national banks)), nonrated securities, and below-investment-grade securities.

10. Review the bank's process for setting and monitoring settlement limits with securities dealers.

Objective 5: Determine the level of IRR in the investment portfolio.

1. Consider the following:

    - Price sensitivity of the investment portfolio.
    - Level and nature of optionality in the investment portfolio.
    - Impact of changing interest rates on average life, effective duration, and cash-flow projections.
    - Impact of depreciation or amortization on earnings performance and capital adequacy.

Objective 6: Determine compliance risk, operational risk, and strategic risk posed by the investment portfolio.

1. Consider the following:

    - Levels of type I, type II, type III, type IV, and type V securities (national banks) and whether the levels of investment securities exceed regulatory limits. Refer to 12 CFR 1, "Investment Securities" (national banks), and 12 CFR 160, "Lending and Investment" (FSAs).
    - Documentation maintained for ongoing monitoring of portfolio and individual security quality, purchase documentation, and reconciliation.
    - Purchase and sales records, with particular attention to the timing and products being purchased and sold.
    - Significance of changes to portfolio strategy, including board awareness and resulting impact on operations and performance.

Objective 7: Develop an overview of BOLI activities via a review of bank policies and procedures that address BOLI and pertinent BOLI information. Refer to OCC Bulletin 2004-56, "Bank Owned Life Insurance: Interagency Statement on the Purchase and Risk Management of Life Insurance."

1. Compile a brief description of the bank's BOLI program(s), including the following elements:

    - Dates policies were purchased.
    - Purpose(s) for the bank's BOLI program(s) (e.g., key man, employee benefit cost recovery, funding deferred compensation plans, and insurance on borrowers).
    - How policies were acquired (e.g., purchased, acquired via merger, or debts previously contracted)
    - List of employees covered and amount of insurance.
    - Temporary (term) or permanent insurance.
    - Original premium paid along with ongoing premium requirements.
    - History of credit rates on policies.

- Whether the cash surrender value (CSV) of the policy is invested in a general account of the carrier or in a separate account. If a separate account,
  - obtain recent list of investments and provide a holdings summary.
  - determine whether the bank purchased stable value protection (SVP). If so, obtain SVP and the parameters on which the SVP provider can limit its liability.
  - obtain list of authorized investments and most current investment manager reports.
  - determine if policies are leveraged.
- Obtain a list of changes in investments made in the prior year.
- Determine if policies are a modified endowment contract.

Objective 8: Using findings from the previous objectives and discussions with bank management and the EIC, determine whether to expand the procedures or develop a plan for corrective action. Consider whether

- bank management can adequately manage the bank's risk.
- bank management can correct fundamental problems.
- to propose a strategy to address identified weaknesses and discuss strategy with the supervisory office.

Objective 9: After completing expanded procedures, determine whether verification procedures should be performed.

The extent to which examiners perform verification procedures is decided on a case-by-case basis after consulting with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 10: Conclude the review of the bank's investment activities.

1. Provide the examiner responsible for asset quality with a list of classified investments.

2. Use the results of the foregoing procedures and other applicable examination findings to compose comments for the ROE.

3. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the investment review.

4. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

5. In discussion with the EIC, provide preliminary strategy recommendations for the next supervisory cycle.

Sensitivity to Market Risk

Conclusion: Sensitivity to market risk is rated (1, 2, 3, 4, or 5).

Introduction

Market risk includes IRR and price risk. Complete this section's objectives to assign the sensitivity to market risk component rating. When assigning the rating, examiners should consult with the EIC and other examining staff as appropriate. Consider the following UFIRS factors:

- Sensitivity of the bank's earnings or the economic value of its equity to adverse changes in interest rates, foreign exchange rates, commodity prices, or equity prices.
- Ability of bank management to identify, measure, monitor, and control exposure to market risk given the bank's size, complexity, and risk profile.
- Nature and complexity of IRR exposure arising from nontrading positions.
- Nature and complexity of market risk exposure arising from trading and foreign operations.

If the bank's only price risk exposure is from OREO, coordinate with examining staff assigned to review OREO to coordinate completion of the RAS for price risk.

Objectives and Procedures

Minimum Objective

Determine the sensitivity to market risk component rating, quantity of risk, and quality of risk management for IRR and price risk.

At the beginning of the supervisory activity, discuss with bank management actual or planned:

- Changes to IRR policy (e.g., limit structures or risk measurement).
- Changes in IRR management process.
- Material changes in the bank's asset or liability structure.
- Changes in the investment portfolio's impact on IRR.
- Changes in mortgage banking activities.
- Changes in the total volume of assets and liabilities accounted for at fair value through earnings, such as mortgage servicing rights and OREO.
- Changes in the size of held-for-sale loan portfolios.
- Changes in key personnel with responsibilities relating to market risk.

As requested, follow up on significant market risk-related audit or IT issues that examiners identified while reviewing the bank's audit and IT programs.

Obtain and review the following information:

- Supervisory strategy.
- Results from supervisory activities.
- Financial reports (e.g., UBPR), applicable OCC reports or analytical tools, and IRR reports.

If the bank's activities, risk profile, or risk controls have changed significantly, or if review of this information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the sensitivity to market risk review by completing objective 11.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the sensitivity to market risk review.

1. Review supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up, or whether a review of audit work papers is required.

3. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about the integrity, confidentiality, or availability of data and require follow-up.

4. Obtain and review financial reports (e.g., UBPR), applicable OCC reports or analytical tools, and the most recent bank-prepared reports used to measure and monitor IRR.

Objective 2: Evaluate the types, levels, and trends in market risk.

Refer to the "Interest Rate Risk" booklet of the *Comptroller's Handbook* on the following considerations.

1. Review and analyze the bank's balance-sheet structure, off-balance-sheet activities, and trends in its balance-sheet composition to identify major sources of IRR exposures. Consider the following:

   - Composition, risk characteristics, and repricing structures of the bank's loans, investments, liabilities, and off-balance-sheet items.
   - Whether the bank has substantial holdings of products with explicit or embedded options—prepayment options, caps, or floors—or products with rates that

considerably lag market interest rates. Refer to OCC Bulletin 2004-29, "Embedded Options and Long-Term Interest Rate Risk: Interest Rate Risk." (Updated in version 1.1)

- Reliance on non-stable, less stable, or rate-sensitive sources of funding.
- Various indexes the bank uses to price its variable rate products (e.g., prime or Treasury) and the level or mix of products tied to these indexes.
- Interest rate sensitive non-interest income sources, such as mortgage servicing portfolios.
- Use and nature of derivative products.
- Other off-balance-sheet items (e.g., letters of credit and loan commitments).

2. Assess and discuss with bank management the bank's vulnerability to various movements in market interest rates, including the following:

   - Timing of interest rate changes and cash flows because of maturity or repricing mismatches.
   - Changes in key spread or basis relationships.
   - Changes in yield curve relationships.
   - Nature and level of embedded options exposures.

3. Evaluate quantity of IRR posed by the loan portfolio. Consult with the loan portfolio manager as appropriate when completing this procedure. Consider the following:

   - If the bank has substantial volumes of loans with unspecified maturities, such as credit card loans, ascertain the effective maturities or repricing dates for those loans and assess the potential exposure for the bank.
   - If the bank has substantial volumes of medium- or longer-term fixed rate loans, assess how appreciation or depreciation of these loans could affect the bank's capital.
   - If the bank has substantial volumes of adjustable-rate mortgage products and other loans with explicit caps, evaluate the potential effect of those caps on the bank's future earnings and at what level of interest rates those caps would come into effect.
   - Assess how a substantial increase in interest rates would affect credit performance of the bank's loan portfolio.
   - If the bank incorporates and enforces prepayment penalties on medium- or longer-term fixed-rate loans, assess the effect of penalties on optionality of these loans.

4. In discussions with the examiner performing the investment review, determine IRR exposure posed by the investment portfolio.

5. Review the results produced by the bank's IRR measurement system(s), including results from gap reports, earnings simulation models, and economic value models, as applicable. Consider the following:

   - Whether the bank is asset or liability sensitive.
   - The level and trend of earnings-at-risk.

  - Is the bank's exposure low, moderate, or high?
  - Is the trend decreasing, stable, or increasing?
  - Identify root causes of negative trends.
- The level and trend of exposure to the bank's economic value of equity.
  - Is the bank's exposure low, moderate, or high?
  - Is the trend decreasing, stable, or increasing?
  - Identify root causes of negative trends.

Calculating economic value of equity in base-case and rising and falling interest rate environments is the most effective risk measurement method for banks with significant longer term or options-related risk positions.

Consider the adequacy of the bank's IRR measurement system when determining how much reliance to place on the measurement system's results when deriving conclusions about the quantity of IRR.

6. If the bank has other sources of IRR or price risk, such as mortgage servicing, credit card servicing, or other loan servicing assets, or OREO. Determine the sensitivity of these other sources to changes in interest rates and the potential impact on earnings and capital.

Objective 3: Evaluate derivatives and hedging activities.

1. Review the use of derivative products. If the bank's exposure to derivative products is new or is of significant volume, expand the review and refer to the "Risk Management of Financial Derivatives" booklet of the *Comptroller's Handbook* (national banks and FSAs), *OTS Examination Handbook* section 660, "Derivative Instruments and Hedging" (FSAs), and OCC Bulletin 2014-8, "End-User Derivatives and Trading Activities: Comptroller's Handbook Supplemental Examination Procedures" (national banks and FSAs). Refer also to the following: (Updated in version 1.1)

   - Banking Circular 277, "Risk Management of Financial Derivatives" (national banks)
   - OCC Bulletin 1994-31, "Risk Management of Financial Derivatives Q & A's" (national banks)
   - OCC Bulletin 1996-43, "Credit Derivatives: Guidelines for National Banks" (national banks)
   - OCC Bulletin 1999-2, "Risk Management of Financial Derivatives and Bank Trading Activities – Supplemental Guidance" (national banks and FSAs)
   - OCC Bulletin 2017-43 (national banks and FSAs).

2. Determine whether bank management uses off-balance-sheet derivative interest rate contracts to manage IRR exposure. Distinguish between the following activities:

   - Risk reduction activities that use derivatives to reduce volatility of earnings or to stabilize the economic value in a particular asset, liability, or business.
   - Positioning activities that use derivatives as investment substitutes or specifically to alter the bank's overall IRR profile.

3. Evaluate ongoing performance and effectiveness of hedging strategies.

Objective 4: Determine the adequacy of IRR measurement system(s) relative to the bank's exposure. Refer to the "Interest Rate Risk" booklet of the *Comptroller's Handbook;* OCC Bulletin 2010-1, "Interagency Advisory on Interest Rate Risk Management"; OCC Bulletin 2012-5, "FAQs on 2010 Interagency Advisory on Interest Rate Risk Management" and OCC Bulletin 2004-29. (Updated in version 1.1)

1. Determine the type(s) of IRR measurement system(s) used by the bank (e.g., gap report, earnings simulation, and economic valuation). If the bank uses a gap report as its only IRR measurement system, determine whether this is appropriate based on the bank's size, balance-sheet composition, or other relevant factors.

2. Determine whether the risk management systems used to measure earnings-at-risk and economic value-at-risk are appropriate for the level and complexity of the bank's exposure.

   Identify the interest rate scenarios the bank uses to measure its potential IRR exposures. Assess adequacy of such rate scenarios. Do they

   - cover a reasonable range of potential interest rate movements in light of historical rate movements?
   - allow the bank to consider the impact of at least a 200 basis point interest rate change over a 12-month horizon?
   - reasonably anticipate holding periods or the time it may take to implement risk-mitigating actions given the bank's strategies, activities, market access, and management abilities?
   - sufficiently capture potential risks arising from option-related positions? Risk to earnings and economic value of equity (EVE) should be measured under a minimum change in interest rates of plus or minus 200 basis points within a 12-month horizon. Banks should also regularly assess IRR exposures beyond typical industry conventions, including changes in rates of greater magnitude (e.g., plus or minus 300 or 400 basis points) across different tenors to reflect changing slopes and twists of the yield curve. Scenarios should be severe but plausible in light of the existing level of rates and the interest rate cycle.

3. Determine whether the bank's method of aggregating data is sufficient for analysis purposes given the nature and scope of the bank's IRR exposure(s). Consider the following:

   - If the bank has significant holdings of fixed-rate residential mortgage-related products, determine if coupon data are captured in sufficient detail to allow the bank to reasonably assess its prepayment and extension risks.
   - If the bank has significant holdings of adjustable-rate residential mortgage-related products, determine whether

- data on periodic and lifetime caps is captured in sufficient detail to permit adequate analysis.
- effect of teaser rates as well as the type of rate indexes used (current versus lagging) has been factored into the bank's risk measurement system.
- data permit the bank to monitor the prepayment, default, and extension risks of the products.

4. Discuss with bank management the key assumptions underlying the bank's risk measurement models. Determine whether

   - assumptions are periodically reviewed for reasonableness.
   - major assumptions are documented and their sensitivity tested, and results are communicated to senior management and the board at least annually.
   - assumptions are reasonable in light of the bank's product mix, business strategy, historical experience, and competitive market.
   - cash flow assumptions for products with option features are reasonable and consistent with the interest rate scenario being evaluated.

5. Determine whether major assumptions used to measure earnings at risk (EAR) and EVE are reasonable and supported. Consider whether assumptions are documented with sufficient detail to allow verification of their reasonableness and accuracy.

6. Determine whether the bank's MIS provide sufficient historical, trend, and customer information to help bank personnel formulate and evaluate assumptions regarding customer behavior. Consider, where material, if information is available to analyze the following:

   - Loan or mortgage-backed security prepayments.
   - Early deposit withdrawals.
   - Spreads between administered rate products, such as prime-based loans and nonmaturity deposit accounts, and market rates of interest.

7. Determine whether the bank's MIS provide adequate and timely information for assessing IRR exposure in the bank's current on- and off-balance-sheet positions. Determine whether information is available for the bank's material portfolios, lines of business, and operating units. Consider the following:

   - Current outstanding balances, rates/coupons, and repricing indexes
   - Contractual maturities or repricing dates
   - Contractual caps or floors on interest rates
   - Scheduled amortizations and repayments
   - Introductory "teaser" rates

8. Assess integrity, confidentiality, and availability of data used to record, analyze, and report information related to IRR. Consider the input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to the data and procedures in

place to monitor system activities. Determine if these controls have been independently validated. Coordinate this review with examiners responsible for all functional areas of the examination, including internal controls, to avoid duplication of effort. Share findings with the examiner reviewing IT.

Objective 5: Determine the characteristics, nature, and methods of management oversight of deposit accounts.

1. Analyze trends in deposit accounts. Consider the following:

   - Stability of offering rates
   - Increasing or declining balances
   - Large depositor concentrations
   - Seasonal and cyclical variations in deposit balances

2. Assess how the bank's deposits might react in different rate environments. Consider management's assumptions for the following:

   - Implicit or explicit floors or ceilings on deposit rates.
   - Rate sensitivity of the bank's depositor base and deposit products.
   - Reasonableness of the bank's assumptions about the effective maturity of the bank's deposits and extent to which the bank's deposit base could offset IRR.

3. Determine whether bank management performs a sensitivity analysis on deposit assumptions. In particular, determine whether bank management analyzes how its IRR exposure may change if those assumptions change or prove to be incorrect and what action, if any, would be taken.

Objective 6: Determine the nature and adequacy of policies, processes, procedures, and controls over market risk.

1. Obtain IRR-related information from the examiner assigned to review board minutes. Review minutes of committees responsible for overseeing IRR.

2. Determine whether the board has approved policies that

   - establish a risk management process for identifying, measuring, monitoring, and controlling risk.
   - establish risk appetite, risk limits, and responsibility for managing risk.
   - are appropriate for the nature and complexity of the bank's IRR exposure.
   - are periodically reassessed in light of changes in market conditions and bank activities.

3. Assess effectiveness of management and the board in overseeing IRR. Consider the following:

   - Existence and reasonableness of board-approved limits for earnings or economic value-at-risk.
   - Compliance with established risk limits.
   - Adequacy of controls over the IRR management process.
   - Bank management's understanding of IRR and ability to anticipate and respond appropriately to changes in interest rates or economic conditions.

4. Evaluate bank management's ability and effectiveness in managing IRR. Consider the following:

   - Level of understanding of IRR dynamics.
   - Ability to respond to competitive pressures in financial and local markets.
   - Whether a balanced presentation of risk and return are appropriately considered in asset and liability strategies.
   - Ability to anticipate and respond to adverse or changing economic conditions and interest rates.
   - Whether skills of bank personnel are appropriate for the level of complexity and risk.

5. Determine whether a competent, independent review process periodically evaluates the effectiveness of the IRR management system. In reviewing measurement tools, evaluators should determine whether the assumptions used are reasonable and whether the range of interest rate scenarios considered are appropriate. Refer to the "Interest Rate Risk" booklet of the *Comptrollers Handbook* and OCC Bulletin 2011-12, "Sound Practices for Model Risk Management: Supervisory Guidance on Model Risk Management."

6. Determine whether the internal controls are appropriate for the bank's type and level of IRR. Consider the following:

   - Do risk limits address a range of possible interest rate changes?
   - Do risk limits address the potential impact of interest changes on both earnings and economic value of equity?
   - Does the bank operate within established limits and risk appetite?
   - How are limit exceptions monitored, reported to bank management, and approved?
   - Are separation of duties and lines of responsibility enforced?

   Consider the relevant controls listed in objective 7 of the Internal Controls and Audit section of the core assessment. Also consider other controls pertinent to IRR.

7. Assess integrity, confidentiality, and availability of data used to record, analyze, and report information related to IRR. Consider input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to the data and procedures in place to monitor system activities. Determine if these controls have been independently

validated. Coordinate this review with the examiners responsible for all functional areas of the examination, including internal control, to avoid duplication of effort. Share findings with the examiner reviewing IT.

8. Using the findings under this objective, determine whether the risk management system to identify, measure, monitor, and control IRR is effective.

Objective 7: Determine the level of price risk. (Updated underlying procedures in version 1.1)

1. If the bank uses derivatives, engages in trading activities, owns mortgage servicing assets, has investments denominated in foreign currencies, or engages in other banking activities whose value changes are reflected in the income statement, consider the following:

    - Quantity of risks in relation to bank capital and earnings.
    - Quality of risk management systems, including
        - bank management's ability or expertise.
        - adequacy of risk management systems.

2. Determine whether appropriate accounting treatment is used (i.e., fair value through earnings).

For more information, refer to the "Large Bank Supervision" booklet of the *Comptroller's Handbook* and OCC guidance on trading activities, investments, OREO, and mortgage banking, including the following:

- *Comptroller's Handbook* booklets
    - "Bank Dealer Activities" (national banks)
    - "Country Risk Management"
    - "Emerging Market Country Products and Trading Activities" (national banks)
    - "Foreign Exchange" (national banks)
    - "Futures Commission Merchant Activities" (national banks)
    - "Mortgage Banking"
    - "Other Real Estate Owned"
    - "Private Placements" (national banks)
    - "Risk Management of Financial Derivatives"
- *OTS Examination Handbook* (FSAs)
    - Section 660, "Derivative Instruments and Hedging"
- Banking Circular 216, "Securities Denominated in Foreign Currencies" (national banks)
- Banking Circular 277, "Risk Management of Financial Derivatives" (national banks)
- OCC Bulletin 1994-31, "Risk Management of Financial Derivatives Q & A's" (national banks)
- OCC Bulletin 1996-43, "Credit Derivatives: Guidelines for National Banks" (national banks)

- OCC Bulletin 1999-2, "Risk Management of Financial Derivatives and Bank Trading Activities – Supplemental Guidance"
- OCC Bulletin 2003-9, "Mortgage Banking: Interagency Advisory on Mortgage Banking"
- OCC Bulletin 2014-8, "End-User Derivatives and Trading Activities: Comptroller's Handbook Supplemental Examination Procedures"

Objective 8: Using the findings from meeting the foregoing objectives, develop preliminary RAS conclusions for IRR and price risk. Consult with the EIC and other examining staff to decide whether the aggregate level or direction of risk noted during the review of sensitivity to market risk has had, or is expected to have, an adverse impact on the bank's capital or earnings. Refer to the "Risk Assessment System" section of the booklet. Comment as necessary.

Objective 9: Determine whether to expand the procedures or develop a plan for corrective action. Consider whether

- bank management can adequately manage the bank's risks.
- bank management can correct fundamental problems.
- to propose a strategy to address identified weaknesses and discuss strategy with the supervisory office.

Refer to booklets of the *Comptroller's Handbook* for expanded procedures.

Objective 10: After completing expanded procedures, determine whether verification procedures should be performed.

The extent to which examiners perform verification procedures is decided on a case-by-case basis after consulting with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 11: Conclude the review of the bank's sensitivity to market risk.

1. Use results of the foregoing procedures and other applicable examination findings to compose comments (e.g., sensitivity to market risk and MRAs) for the ROE.

2. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the sensitivity to market risk review that are relevant to other areas being reviewed.

3. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

4. In discussion with the EIC, provide preliminary conclusions about the following:

- Sensitivity to market risk component rating.
- Quantity of IRR and price risk.
- Quality of IRR and price risk management.
- Aggregate level and direction of interest rate, price, or other applicable risks.
- Complete the summary conclusions for IRR and price risk in the "Community Bank Risk Assessment System" section of this booklet.
- Supervisory strategy recommendations.

Information Technology

Conclusion: URSIT composite rating is (1, 2, 3, 4, or 5).

Introduction

IT is an integral part of banking. Without technology, banks would be unable to provide the volume, variety, and complexity of products and services offered. Because IT can have a considerable effect on all banking activities, the OCC has integrated the review of technology into the core assessment in three ways:

- Examiners assess the management of key IT functions, such as information security, business continuity planning, audit, IT third-party risk management, and conformance with 12 CFR 30, appendix B, "Interagency Guidelines Establishing Information Security Standards."
- Examiners consider the effect of technology on each area they review, focusing on the integrity, confidentiality, and availability of data used in that area.
- Examiners assess the potential impact of technology on each of the eight OCC-defined risks.

Technological risk is not a separate RAS category. But because technology affects all areas of the bank, a single weakness can increase risk in several RAS categories. For example, a weakness in internet banking controls could lead to increased fraud (operational risk). If this fraud becomes public knowledge, reputation risk may also increase. The bank's tarnished reputation can increase the cost of funding or reduce funding availability (interest rate and liquidity risks). Examiners should consider the domino effect in their assessment of the bank's total risk profile.

In conducting IT examinations, examiners focus on the four major issues that are common to all IT activities:

- **Management of technology:** Planning for and oversight of technological resources and services and ensuring that they support the bank's strategic goals and objectives.
- **Integrity of data:** Accuracy, reliability, and timeliness of automated information and associated MIS.
- **Confidentiality of information:** Protection of bank and customer information from inadvertent disclosure.
- **Availability of information:** Effectiveness of business resumption and contingency planning and adherence to data retention requirements.

The community bank core assessment includes minimum standards for IT supervision in the form of examination conclusions and objectives. The core assessment objectives for IT directly correspond to the four major IT issues. Examiners are required to reach conclusions on each issue and communicate their conclusions in the ROE.

The OCC has adopted the FFIEC's Uniform Rating System for Information Technology (URSIT). Examiners assign an IT composite rating to all banks. Examiners discuss this rating with bank management and disclose it in the ROE.

Complete this section's objectives to assign the IT composite rating, using as a guide the "Uniform Interagency Information Technology Rating System," in the "Bank Supervision Process" booklet of the *Comptroller's Handbook.* The composite URSIT rating should reflect the following:

- Adequacy of the bank's risk management practices.
- Management of IT resources.
- Integrity, confidentiality, and availability of automated information.
- Degree of supervisory concern posed by the bank.

To assign the rating, the examiner should consult the EIC, examiners assigned to review management and audit, and other examining staff to avoid duplication of effort. Although the OCC does not assign URSIT component ratings to the banks it supervises, risks arising from the areas covered by the component ratings are considered when assigning the URSIT composite rating.

Objectives and Procedures

Minimum Objective

Determine the IT composite rating and the quantity of operational risk and quality of operational risk management related to IT.

At the beginning of the supervisory activity, discuss with bank management the following:

- Actual security events or service interruptions during the supervisory cycle.
- Changes in the financial condition of, or quality of service provided by, third-party IT service providers.
- Actual or planned changes in third-party IT service providers, systems, applications, distribution channels, or personnel.
- Changes in the audit plan or risk assessment relating to IT areas.
- Changes in the information security or contingency planning processes.
- Changes in the processes or reports that bank management uses to monitor IT activity.
- Impact of these changes on the bank's written information security program.

Follow up on significant IT-related audit issues identified by the examiner reviewing the bank's audit program.

Obtain and review the following information:

- Supervisory strategy.
- Results from supervisory activities.
- Results of tests of the bank's information security program and bank management's response.
- Results of tests of the bank's contingency plan and bank management's response.
- IT audit risk assessment.
- Annual report to the board consistent with 12 CFR 30, appendix B.
- IT-related MIS reports, including recent fraud and processing losses.
- Documentation for major IT initiatives.

If the bank's activities, risk profile, or risk controls have changed significantly, or if review of this information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the IT review by completing objective 11.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the IT review.

1. Review supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant IT audit findings require follow-up or whether a review of audit work papers is required. Determine whether the scope of the IT audit includes testing of the bank's information security program and contingency plan, as well as the annual report to the board required by 12 CFR 30, appendix B. If a more detailed review of the IT audit is necessary, refer to the "Audit" booklet of the *FFIEC IT Examination Handbook.*

3. Discuss with examiners assigned to other areas their assessments of integrity, confidentiality, and availability of data used to record, analyze, and report information.

4. If not previously provided, obtain and review lists describing the complexity of the bank's processing environment and reports that bank management uses to supervise the IT area, including but not limited to the following:

    - List of third-party IT service providers, description of products or services provided, and the bank's analysis of the third parties' financial condition.

- A report or diagram that illustrates computer systems and networks, application and software deployment, vendor and external connectivity, and data flows, including primary data repositories.
- Reports used to monitor computer activity, network performance, system capacity, security violations, and network intrusion attempts.

5. Determine the following in discussions with bank management:

- How bank management administers and controls IT activities throughout the organization.
- Significant changes or planned changes in systems, applications, distribution channels, or personnel since the last examination.
- How bank management monitors quality and reliability of outsourced services and support functions.

6. Review and consider other factors:

- New regulatory guidance.
- Actual or planned organizational changes.
- Significance of the system or application in supporting bank products and services.
- Volume or average dollar size of transactions processed.
- Overall complexity of the bank's IT environment.
- Bank management's reliance on the application or its output.
- Recent audit coverage provided internally or externally.
- Scope of the most recent supervisory activity and changes since that review.

7. Determine which IT processes represent the most significant risks to the bank. Table 2 lists some areas that examiners should consider:

Table 2: Examiner Considerations

IT processes	Systems	Applications
• Board and bank management oversight • Third-party risk management • System controls and data integrity • Information security and conformance with 12 CFR 30, appendix B • Business continuity • Providing services to other financial institutions • Project management • System development with in-house programming	• Mainframe or midrange system • In-house networks • Departmental local area networks • Wireless networks • Imaging systems • Item processing systems	• Core applications (e.g., general ledger, loans, and deposits) • Electronic banking • Wire transfer • Trust processing • Mortgage processing • Credit cards

8. If an area of higher risk is identified (e.g., in-house programming, account aggregator, certificate authority, cross-border internet banking, online account origination, internet service provider, or providing automated services to other financial institutions), expand the review to assess additional risks inherent in such activities using procedures from the *FFIEC IT Examination Handbook*.

Objective 2: Assess the adequacy of IT management, including oversight of technological resources and strategic planning.

1. Obtain technology-related information from the examiner assigned to review board minutes. Review minutes of committees responsible for overseeing and coordinating IT resources and activities to determine user involvement and organizational priorities.

2. Review organizational charts, job descriptions, compensation, turnover, and training programs to determine whether the bank has a sufficient number of technology personnel with the expertise the bank requires (consider the bank's outsourcing arrangements). (Updated in version 1.1)

3. Review the bank's strategic planning as it relates to IT, and determine if the goals and objectives are consistent with the bank's overall business strategy. Consider whether (Updated in version 1.1)

   - the IT strategic plans align with the bank's overall strategic plan.
   - IT priorities and the distribution of resources align with the priorities in the bank's overall strategic plan.
   - the IT strategic plan priorities align with the results of the IT audit risk assessment and the Business Continuity Planning Impact Analysis.

4. Review documentation supporting major projects or initiatives to determine effectiveness of technology planning, implementation, and follow-up activities. Consider the following:

   - Decision process, including options considered and basis for final selection.
   - Reasonableness of implementation plans, including periodic milestones.
   - Effectiveness of monitoring of implementation activities.
   - Whether validation testing of new programs or systems is conducted before putting the programs into production.

5. Discuss pending litigation and insurance coverage pertaining to IT activities with the examiner responsible for evaluating bank management. Assess the adequacy of insurance coverage for employee fidelity, IT equipment and facilities, e-banking activities, loss resulting from business interruptions, and items in transit.

6. Review MIS reports for significant IT systems and activities to assess whether risk identification, measurement, control, and monitoring are commensurate with the complexity of the bank's technology and operating environment. Consider the following:

- Systems capacity, including peak processing volumes.
- Up-time performance and processing interruptions.
- Network monitoring, including penetration attempts and intruder detection.
- Activity logs and security reports for operations, program and parameter changes, and terminals use, etc.
- Volume and trends of losses from errors, fraud, or unreconciled items.

7. Assess timeliness, completeness, accuracy, and relevance of MIS for IT systems and operational risk. Consider source of reports, controls over report preparation, and independent validation of report accuracy.

Objective 3: Assess the effectiveness of the bank's management and monitoring of third-party IT service providers. Consider the information in the "Outsourcing Technology Services" booklet of the *FFIEC IT Examination Handbook*, OCC Bulletin 2013-29, OCC Bulletin 2017-7, and OCC Bulletin 2017-21. Communicate conclusions to the examiner(s) reviewing the bank's third-party risk management program and management component rating. (Updated in version 1.1)

1. Obtain the bank's third-party risk management policy and procedures. Determine how the bank assesses risks associated with third-party technology service provider relationships, and assess the adequacy of the policy and procedures. Determine if the policy has board or IT committee approval.

2. Evaluate the selection process for third-party IT service providers, particularly if a change in third-party IT service providers or new products or services have been implemented since the last examination or anticipated during this supervisory cycle. Consider whether management

   - checked references.
   - evaluated the third party's financial condition.
   - evaluated insurance and disaster recovery plans.
   - determined that the third party's information security practices are sufficient

3. Review contract guidelines, including customer privacy protections. Consider whether

   - contract contains adequate measurable service-level agreements.
   - pricing methods in the contract could adversely affect the bank's safety and soundness.
   - required contract clauses address financial reporting, right to audit, ownership of data and programs, and data confidentiality.
   - application source code and documentation for software developed or maintained by the third-party IT service provider are available (generally applies to turnkey software).

4. Assess whether the bank monitors the third-party IT service provider's performance under the contract. Consider whether

   - service provider's financial information is available and analyzed.
   - bank management reviews service provider's operations and security audits.
   - bank management is meeting key service level agreements.
   - service provider's disaster recovery program and testing are effective.
   - information security practices are sound.
   - the bank participates in user groups and other mechanisms to communicate and influence the service provider.

Objective 4: Assess the adequacy of controls for integrity of data. (Updated in version 1.1)

1. Determine that system and network administrator access is appropriately monitored and adequately controlled. Determine whether segregation of duties exists between the responsibility for networks and the responsibility for computer operations. Evaluate overall separation of duties and responsibilities in the bank operations and data processing areas.

2. Review controls and audit trails over file change requests (e.g., address changes, due dates, loan payment extensions or renewals, loan or deposit interest rates, and service charge indicator). Consider the following:

   - Individuals authorized to make changes and potential conflicting job responsibilities.
   - Documentation and audit trail of authorized changes.
   - Procedures used to verify accuracy of file changes.

3. Assess adequacy of controls over changes to systems, programs, data files, and personal computer-based applications. Consider the following:

   - Procedures for implementing program updates, releases, and changes.
   - Controls to restrict and monitor use of data-altering utilities.
   - Process that bank management uses to select system and program security settings (i.e., whether settings were made based on sound technical advice or were default settings).
   - Controls to prevent unauthorized changes to system and programs security settings.
   - Process and authorizations to change application parameters.

4. Determine whether employees' levels of online access (blocked, read-only, update, and override, etc.) match current job responsibilities.

5. Evaluate effectiveness of password administration for employee and customer passwords considering the complexity of the processing environment and type of information accessed. Consider the following:

- Whether passwords are confidential (known only to the employee or customer).
- Whether procedures to reset passwords promote confidentiality.
- Frequency of required changes in passwords.
- Password design (number and type of characters).
- Security of passwords while stored in computer files, during transmission, and on printed activity logs and reports.

6. Determine whether the bank has removed or reset default profiles and passwords from new systems and equipment, and determine whether access to the system administrator level is adequately controlled.

Objective 5: Evaluate the effectiveness of controls to protect data confidentiality (i.e., to prevent inadvertent disclosure of confidential information). Determine conformance with 12 CFR 30, appendix B.

1. Obtain the bank's annual information security risk assessment. Review risk assessment to determine whether the bank has

   - identified and ranked information assets (customer information that the bank houses, maintains, and uses to conduct transactions).
   - identified all reasonable threats to the bank.
   - analyzed technical and organizational vulnerabilities.
   - considered potential effect of a security breach on customers and the bank.
   - updated risk assessment to reflect changes in new products or services or changes in external conditions.

2. Determine if risk assessment provides adequate support for security strategy, controls, and testing plan implemented by the bank.

3. Review information security policy to determine whether it sufficiently addresses the following:

   - Authentication and authorization.
   - Network access controls.
   - Physical controls over access to hardware, software, media storage, data disposal, and paper records.
   - System configuration.
   - Operating system access.
   - Intrusion detection and response.
   - Service provider oversight.
   - Encryption controls.
   - Employee training.

4. Evaluate systems used to monitor access and detect unauthorized internal or external attempts to access the bank's systems (e.g., intrusion detection and review of activity

logs). Determine whether the bank has an appropriate intrusion response and customer notification program. Evaluate the need for or adequacy of testing (e.g., vulnerability assessments or penetration testing) for the more complex aspects of the bank's security program. If the bank has had a breach in security, determine why and what was done to correct the issue and improve security.

Refer to OCC Bulletin 2005-13, "Response Programs for Unauthorized Access to Customer Information and Customer Notice: Final Guidance: Interagency Guidance."

5. Evaluate control and security for data transmitted to or from remote locations. Consider the following:

   - Type of data transmitted.
   - Use of encryption or other security techniques (e.g., firewalls).
   - Access to network components (e.g., servers, routers, and telephone lines) that support data transmission.

6. Evaluate controls over remote access, and determine whether they are sufficient to restrict use and access to authorized users only.

7. Assess the adequacy of the bank's e-banking services (e.g., transaction internet banking, online cash management, e-bill payment, or telephone banking) authentication. Refer to OCC Bulletin 2005-35, "Authentication in an Internet Banking Environment: Interagency Guidance"; OCC Bulletin 2006-35, "Authentication in an Internet Banking Environment: Frequently Asked Questions"; and OCC Bulletin 2011-26, "Authentication in an Internet Banking Environment: Supplement."

8. Determine whether the bank's information security program conforms with 12 CFR 30, appendix B. The program should

   - be approved and overseen by the board.
   - be adjusted for changes in the bank's (or service provider's) processing environment or systems.
   - be tested and validated.
   - provide employee training.
   - include an annual report to the board or committee describing overall status of the program and the bank's conformance with 12 CFR 30, appendix B.

9. Determine whether the bank's risk assessment process for customer information and its test of key controls, systems, and procedures in the bank's information security program are commensurate with sensitivity of the information and complexity and scope of the bank's activities.

Objective 6: Assess the adequacy of the bank's policies and procedures for the availability of automated information and ongoing support for technology-based products and services.

1. Review business impact analysis. Determine whether mission-critical activities are identified and prioritized and maximum allowable downtimes are considered.

2. Determine the adequacy of the bank's business resumption contingency plan. Consider whether the

   - plan has a corporate-wide focus and is appropriate for the organization's size and complexity.
   - plan takes into account personnel, facilities, technology, telecommunications, third-party relationships, utilities, geographical diversity, and data records.
   - plan considers reasonable scenarios, significant threats, and vulnerabilities.
   - board or committee annually reviews the plan.

3. Review annual validation of the contingency plan, including backup and alternate site test findings. Determine whether the board and senior management were apprised of the scope and results of the backup test, whether they have confidence that the plan operates as expected, and whether the plan meets requirements of the bank's business impact analysis. Consider whether the

   - test has realistic conditions.
   - test uses actual backup systems and data files, and establishes network connectivity.
   - post-test analysis is conducted with recommendations and plans for corrective action.
   - test is adequate for the bank's size and complexity.
   - test validates recovery time frames.

4. If third-party service providers provide mission-critical activities or systems, determine whether the bank's recovery plan is compatible with business recovery plans of the service providers. Determine whether the bank has reviewed primary third-party testing results.

5. Evaluate planning for event management activities. Consider the following:

   - Emergency procedures and evacuation plans
   - Response to network attack or penetration
   - Reporting to appropriate regulatory or law enforcement agencies

6. Assess processes and procedures to prevent destruction of electronic files and other storage media. Consider the following:

   - Frequency of file backup
   - Access to backup files and storage media (e.g., disks and tapes)
   - Location of off-site file storage

- Virus protection for networks and personal computers

7. Determine whether only authorized personnel have access to the computer area, electronic media, and supplies of negotiable items. Determine whether equipment and networks supporting mission-critical services are appropriately secured. Consider physical security and environmental controls.

8. Determine how bank management implements record retention practices that are in compliance with legal, regulatory, and operational requirements. Consider records at the bank, at service provider locations, and in off-site or long-term storage.

Objective 7: Assess the bank's processes for managing information security risk and operational risk by using the findings from meeting the foregoing objectives, by discussing the processes with key managers, and by analyzing applicable internal or external audit reports.

1. Determine whether the volume and nature of fraud and processing losses, network and processing interruptions, customer-reported processing errors, or audit criticisms lower quality of automated activities and services.

2. Determine whether the bank's risk assessment process for customer information and its test of key controls, systems, and procedures in the bank's information security program are commensurate with the sensitivity of the information and complexity and scope of the bank's activities.

3. Assess timeliness, completeness, accuracy, and relevance of management and board reports regarding operational risk (focus on the aspects of such reports that relate to IT). Consider the source of reports, controls over report preparation, and independent validation of report accuracy. Risk management reports should cover major sources of operational risk. (Updated in version 1.1)

4. Using the findings from meeting the previous objectives, combined with the information from the EIC and other examining staff, make preliminary assessments on the quality of operational risk management as it relates to IT. Consider whether

   - bank management recognizes and understands existing and emerging risks.
   - bank management measures risk in an accurate and timely manner.
   - the board establishes, communicates, and controls risk limits.
   - bank management accurately and appropriately monitors established risk limits.

Objective 8: Using the findings from meeting the foregoing objectives, identify significant risk exposures from the IT review.

Develop preliminary assessments of quantity of operational risk, quality of operational risk management, aggregate operational risk, and direction of operational risk related to IT. Refer to the "Risk Assessment System" section of this booklet. Consult with the EIC and other examining staff to identify findings from the IT review that have significance for other risk rating categories.

Objective 9: Determine whether to expand the procedures or develop a plan for corrective action. Consider whether

- bank management can adequately manage the bank's risks.
- bank management can correct fundamental problems.
- to propose a strategy to address identified weaknesses and discuss strategy with the supervisory office.

Refer to booklets of the *Comptroller's Handbook* or *FFIEC IT Examination Handbook* for expanded procedures.

Objective 10: After completing expanded procedures, determine whether verification procedures should be performed.

The extent to which examiners perform verification procedures is decided on a case-by-case basis after consulting with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 11: Conclude the review of the bank's IT activities.

1. Provide bank management with a list of deficiencies for consideration.

2. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the IT review that are relevant to other areas being reviewed.

3. Use results of the foregoing procedures and other applicable examination findings to compose comments (e.g., IT and MRAs) for the ROE.

4. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge. (Updated in version 1.1)

5. In discussion with the EIC, provide preliminary conclusions about the following:

   - Quantity of operational risk as it relates to IT.
   - Quality of risk management as it relates to IT.
   - Aggregate level and direction of operational risk, or other applicable risks, as they relate to IT.
   - Complete the summary conclusions in the "Community Bank Risk Assessment" section of this booklet.
   - Supervisory strategy recommendations.

Asset Management

Conclusions:
Aggregate asset management risk is (low, moderate, or high)
UITRS ratings: Composite (1, 2, 3, 4, or 5)
Management (1, 2, 3, 4, or 5)
Operations, internal controls, and auditing (1, 2, 3, 4, or 5)
Earnings (1, 2, 3, 4, or 5)
Compliance (1, 2, 3, 4, or 5)
Asset management (1, 2, 3, 4, or 5)

Introduction

Many community banks provide asset management-related services. Asset management is the business of providing financial products and services to a third party for a fee or commission. Asset management services include trust and fiduciary services, investment management, retirement planning, corporate trust administration, custody, safekeeping, securities lending services, security-holder and transfer agent services, and retail sales of nondeposit investment products. The trust rating is only assigned to banks exercising trust powers (i.e., banks only offering retail nondeposit investment products (RNDIP) and no other asset management services do not receive a trust rating).

The *Asset Management* series of booklets of the *Comptroller's Handbook* provides a complete overview of asset management services provided by banks. The booklets in this series are

- "Asset Management"
- "Asset Management Operations and Controls"
- "Collective Investment Funds"
- "Conflicts of Interest"
- "Custody Services"
- "Investment Management Services"
- "Personal Fiduciary Activities"
- "Retirement Plan Products and Services"
- "Unique and Hard-to-Value Assets"

The asset management section of the core assessment is structured to conduct supervisory activities along the asset management product lines typically found in community banks, including limited-purpose trust banks. The results of these reviews are then used to assign the composite and component ratings under UITRS. Under UITRS, fiduciary activities of banks are assigned a composite rating based on an evaluation and rating of five essential components of an institution's fiduciary activities: management, operations, internal controls and auditing, earnings, compliance, and asset management. The composite rating is discussed with bank management and disclosed in the ROE. The component ratings can, but are not required to, be discussed with bank management and disclosed in the ROE, at the EIC's discretion and with the ADC's approval. Refer to the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for more information on the UITRS. (Updated in version 1.1)

When assigning the aggregate risk and the UITRS ratings, the examiner consults the EIC; examiners assigned to review management, internal controls and audit, IT, and earnings; and other examining staff.

The examiner completes appropriate objectives from this section to assess asset management risk. While asset management is not a defined RAS category, examiners assess the overall risk arising from the type and volume of activities conducted and the quality of risk management using the risk indicators in the "Other Risks" section of this booklet as a guide. The portfolio manager uses this assessment of asset management risk, along with the potential impact that risk has to the bank as a whole, to develop the scope of future asset management supervisory activities and determine any effect on the bank's operational, compliance, reputation, and strategic risks.

Objectives and Procedures

Minimum Objective

Determine the quantity of risk and the quality of risk management for asset management and assign UITRS composite and component ratings.

At the beginning of the supervisory activity, discuss the following with bank management:

- Actual or planned changes in
  - management, key and operational staff, including portfolio managers and advisors.
  - board and fiduciary committee structure and oversight.
  - facilities and operating systems, processes, and controls.
  - audit plan or risk assessment relating to asset management areas.
  - policies, procedures, and controls.
- New, modified, or expanded products and services. (Updated in version 1.1)
- New or expanded third-party relationships, including investment advisors.
- Strategic plans for asset management activities.
- Asset management business plan, budget, or budgeting process.
- Asset management earnings performance.
- Significant transactions with related parties, including businesses of directors, officers, or employees of the bank and bank affiliates.

Obtain and review the following information:

- Supervisory strategy.
- Results from supervisory activities.
- Most recent committee minutes and information packages.

- Asset management organizational chart.
- Most recent financial reports, including budget and variance reports.
- Appropriate UBPR pages.
- Policies and procedures if significant changes or additions have been made.
- Asset management risk assessment.
- Audit and compliance reports and follow-up.
- Call report Schedule RC-T, "Fiduciary and Related Services," for significant changes in account types and volumes.
- Customer complaint data from the OCC's Customer Assistance Group and the bank. Coordinate with the examiner reviewing consumer compliance to avoid duplication of efforts.

Follow up on significant asset management-related audit or IT issues identified by the examiners reviewing the bank's audit and IT programs:

- Discuss outstanding asset management audit or IT issues with bank management.
- If warranted based on the foregoing discussions or if requested by the examiners reviewing audit and IT, obtain and review a risk-based sample of internal asset management audit or IT reports and management follow-up.
- Discuss with management changes in scope, personnel, or frequency of the asset management audit function that could increase or decrease the function's reliability.
- Discuss with bank management changes in asset management IT processes or MIS that could increase or decrease their reliability.

Select a risk-based sample of fiduciary accounts. The sample should be representative of the type and size of accounts opened during the time period of the review and should focus on accounts with higher risk potential such as personal trusts with complex family relationships or unique asset types, insider accounts, complex retirement accounts, and successor and co-trustee accounts. Determine whether

- new accounts were opened in compliance with bank policy and applicable laws and regulations.
- risks associated with new accounts are consistent with the bank's business plan and risk appetite.
- accounts are administered in compliance with bank policy, the governing instrument, and applicable laws and regulations.

Develop preliminary assessments of the quantity of risk and quality of risk management using the asset management risk indicators in the "Other Risks" section of this booklet. If the bank's activities, risk profile, or risk controls have changed significantly or if review of the foregoing information raises substantive issues, the examiner should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the review of asset management activities by completing objective 10.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition and risks. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the asset management review.

1. Review the supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. As necessary, obtain and review the following information:

   - Asset management organizational chart and manager job descriptions.
   - Policies and operating procedures.
   - Strategic and business plans.
   - Committee minutes and information reports.
   - Asset management reports provided to the board or committee(s).
   - Compliance reviews and management responses.
   - Descriptions of data processing and accounting systems, including third-party relationships.
   - Management reports, including those used to monitor new and closed accounts, account investment reviews, overdrafts, financial results, exceptions, and compliance/risk information related to asset management.
   - Information on investment activities, including investment performance and approved securities lists.
   - Operational reports, such as transaction volumes and reconcilement reports.
   - Fee schedules.
   - A report on significant losses and settlements sustained since the last fiduciary supervisory activity.
   - Regulatory reports.

3. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is required.

4. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about integrity, confidentiality, or availability of data and require follow-up.

5. Discuss pending litigation and insurance coverage pertaining to asset management activities with the examiner responsible for evaluating bank management.

Objective 2: Determine quality and effectiveness of board and bank management's supervision of asset management lines of business.

1. Evaluate board supervision by considering the following:

   - Committee structures, responsibilities, and reporting standards.
   - Management selection and appraisal processes.
   - Oversight of compensation or incentive plans. If the bank offers incentive compensation plans, refer to OCC Bulletin 2010-24, "Incentive Compensation: Interagency Guidance on Sound Incentive Compensation Policies."
   - Strategic planning and monitoring processes.
   - Information reports received from committees and bank management.
   - Policy review and approval processes.
   - Oversight of audit and compliance functions.
   - Use of legal counsel and the monitoring of litigation.
   - Insurance coverage reviews.
   - Adequacy of oversight and approval of new, modified, or expanded products or services. Refer to OCC Bulletin 2017-43.

2. Evaluate bank management's supervision by reviewing the quality of the following:

   - Management and support staff, including competence, turnover, and succession planning.
   - Policies and procedures, including compliance.
   - Department reports provided to management committees on a monthly, quarterly, or annual basis.
   - Internal controls, including system access and segregation of duties.
   - Audit and compliance functions, including responses to deficiencies and recommendations.
   - Oversight of third-party service providers. Refer to OCC Bulletin 2013-29 and OCC Bulletin 2017-21.
   - Insurance coverage and review processes.
   - Litigation management. Refer to the "Litigation and Other Legal Matters" booklet of the *Comptroller's Handbook*.
   - Compensation or incentive plans. If the bank offers incentive compensation plans, refer to OCC Bulletin 2010-24.
   - Complaint resolution processes. If the bank has a centralized complaint resolution process, coordinate with the examiner reviewing consumer compliance to avoid duplication of efforts.

   Refer to the "Corporate and Risk Governance" booklet of the *Comptroller's Handbook* for more information regarding board oversight.

3. Determine whether the bank's fiduciary audit program meets the requirements of 12 CFR 9.9 (national banks) or 12 CFR 150.440-480 (FSAs). Coordinate with the

examiner responsible for the "Internal Controls and Audit" section of the core assessment.

4. Evaluate the earnings of asset management activities. Identify nonrecurring income or expense items and assess trends.

5. For trust banks, determine the adequacy of capital and liquidity monitoring. Refer to OCC Bulletin 2007-21, "Supervision of National Trust Banks: Revised Guidance: Capital and Liquidity." (This guidance applies to national banks and FSAs that are trust banks.)

6. Consider the findings from the other examination sections and incorporate them into the board and bank management's evaluation for asset management.

Objective 3: Determine the quantity of risk and quality of risk management relating to the administration of fiduciary accounts.

1. Determine types and level of risk associated with the administration of fiduciary and related accounts. Discuss the following with bank management:

    - Volume and types of fiduciary accounts under administration.
    - Types and level of policy exceptions, audit and internal control deficiencies, and violations of law internally identified and reported.
    - Amount and status of significant litigation and client complaints. For client complaints, review data from the OCC's Customer Assistance Group and the bank to assess the level, volume, and themes. Customer complaints are a *potential* indicator of risk management weaknesses, or other deficiencies, such as violations of laws or regulations.

2. Review account acceptance processes. For fiduciary accounts, evaluate compliance with the pre-acceptance review requirements of 12 CFR 9.6(a) (national banks) or 12 CFR 150.200 (FSAs). Determine whether the process

    - is formalized and adequately documented.
    - includes enhanced due diligence and customer identification program procedures.
    - obtains and effectively uses appropriate information.
    - includes appropriate approval processes for accepting accounts and policy exceptions.

3. Review policies and procedures for fiduciary account administration. Policies and procedures should address the following:

    - Compliance with applicable fiduciary laws and regulations
    - Account administration guidelines
    - Policy exceptions, including monitoring and reporting processes
    - Customer complaint resolution procedures

4. Evaluate cash management processes.

    - For discretionary fiduciary accounts, identify and review large, uninvested, or undistributed funds, and discuss them with bank management. Determine whether administration is appropriate and complies with the requirements for fiduciary funds awaiting investment or distribution under 12 CFR 9.10 (national banks) or 12 CFR 150.290 (FSAs).
    - Review account overdrafts, giving attention to large and long-standing items. Determine why they exist, and discuss bank management's plans to resolve them.

5. Select a risk-based sample of recently accepted fiduciary accounts. The sample should focus on accounts with higher-risk potential, such as personal trusts with complex family relationships or unique asset types, insider accounts, complex retirement accounts, and successor and co-trustee accounts. Consider requirements of objectives 4 and 5 when selecting the sample. For each account, determine compliance with internal bank policy, the governing instrument, and applicable laws and regulations and whether the account acceptance process was adequate and effective. For discretionary fiduciary accounts, include both the pre-acceptance and initial post-acceptance review required by 12 CFR 9.6(a)-(b) (national banks) or 12 CFR 150.200-210 (FSAs).

6. Select a risk-based sample of established fiduciary accounts, including personal, retirement, and corporate trust accounts and individual retirement accounts. Review each account and determine whether administrative processes and controls are adequate and effective. Consider whether account administration

    - complies with terms of the governing instrument, applicable law, court orders, and directions and is consistent with needs and circumstances of account beneficiaries.
    - includes annual account reviews in accordance with 12 CFR 9.6(c) (national banks) or 12 CFR 150.220 (FSAs) and other applicable laws or regulations.
    - avoids unauthorized conflicts of interest and self-dealing.
    - charges and reports accurate account fees and complies with compensation provisions of 12 CFR 9.15 (national banks) or 12 CFR 150.380-390 (FSAs), document provisions, and the Uniform Principal and Income Act.

7. For personal fiduciary accounts, evaluate the discretionary distribution processes:

    - Is the decision-making authority for discretionary distributions expressly defined and communicated to all personnel?
    - Are decisions fully documented and authorized by designated personnel or committees?
    - Are distributions consistent with the guidelines established in the governing instrument?

8. For individual retirement accounts, determine whether the bank is fulfilling its duties and responsibilities in compliance with Internal Revenue Code section 408 and the prohibited transaction provisions of Internal Revenue Code section 4975. Refer to the "Retirement

Plan Products and Services" booklet of the *Comptroller's Handbook* for more information. (Updated in version 1.1)

9. For retirement accounts, determine compliance with the applicable sections of the Employee Retirement Income Security Act (ERISA),[45] including prudence requirements of section 404 (asset diversification), section 406 (prohibited transactions), and plan provisions. Refer to the "Retirement Plan Products and Services" booklet of the *Comptroller's Handbook*.

   If potential violations of ERISA were identified during the retirement account review, consult with the EIC and ADC and report to the OCC Asset Management Group for possible referral to the U.S. Department of Labor. Refer to OCC Bulletin 2006-24, "Interagency Agreement on ERISA Referrals: Information Sharing Between the FFIEC Agencies and the DOL."

10. For corporate trust accounts, determine whether the bank is fulfilling its duties and responsibilities as paying agent, disbursing agent, registrar, or trustee in accordance with the governing instrument and applicable laws and regulations.

Objective 4: Determine the quantity of risk and the quality of risk management relating to conflicts of interest and self-dealing.

1. Determine whether conflicts of interests have been reported internally. Discuss the following with bank management:

   - Processes used to identify, assess, and resolve conflicts of interest
   - Significant changes in policies, processes, personnel, or controls
   - Internal or external factors that could affect conflicts of interests

2. Review policies and procedures developed to control the risks associated with conflicts of interest and self-dealing. Consider the following:

   - Compliance with 12 CFR 9.5 (national banks) or 12 CFR 150.140 (FSAs) regarding policies and procedures.
   - Compliance with 12 CFR 9.12 (national banks) or 12 CFR 150.330-370 and 12 USC 1464(n)(7) (FSAs) regarding self-dealing and conflicts of interest.
   - Compliance with 12 CFR 12.7 (national banks) or 12 CFR 151.140 (FSAs) regarding securities trading policies and procedures.
   - Compliance with ERISA (29 USC 1001 et seq.). (Updated in version 1.1)
   - Compliance with other federal and state laws and regulations and court rulings.
   - Industry practices and OCC guidance relating to employee ethics and acceptable behaviors.

[45] Refer to 29 USC 1001 et seq., "Employee Retirement Income Security Program." (Footnote added in version 1.1)

3. Determine whether conflicts of interest or self-dealing were identified during the fiduciary account administration review and whether policies, processes, and controls are effective.

4. Review processes and controls for discretionary fiduciary funds awaiting investment or distribution and determine compliance with the provisions of 12 CFR 9.10(a) (national banks) or 12 CFR 150.290 (FSAs). Determine whether the bank

   - does not allow discretionary funds to remain uninvested or undistributed any longer than is reasonable for proper management of the account.
   - obtains rate of return for the funds that is consistent with applicable law.

5. Review processes and controls for fiduciary funds awaiting investment or distribution and determine compliance with the provisions of 12 CFR 9.10(b) (national banks) or 12 CFR 150.300-320 (FSAs). Determine whether the bank

   - does not self-deposit fiduciary funds when prohibited by applicable law.
   - sets aside adequate collateral for the portion of the funds deposited with the bank that exceed the FDIC insurance limit.
   - for FSAs, sets aside adequate collateral for the portion of funds deposited with or by an affiliate that exceed the FDIC insurance limit.

6. Review processes and controls governing fiduciary compensation and compliance with 12 CFR 9.15 (national banks) or 12 CFR 150.380-400 (FSAs) regarding fiduciary compensation, as well as the Uniform Principal and Income Act. Consider whether

   - fiduciary-related compensation complies with applicable laws and regulations. If not set or governed by applicable law, fees should be reasonable for services provided.
   - bank officers or employees act as co-fiduciary with the bank in the administration of fiduciary accounts and receive compensation for such services. Payment of compensation to a bank officer or employee serving as a co-fiduciary with the bank is prohibited unless specifically approved by the bank's board of directors.
   - revisions or changes in fees charged to fiduciary accounts with set or fixed-fee schedules are appropriate and properly authorized.
   - fee concessions for officers, directors, and other employees are granted under a general policy that is uniformly applied and approved.
   - cash sweep and termination fees are only charged with proper authorization and disclosure and in accordance with applicable law.
   - policies and procedures address the receipt and acceptance of 12b-1 fees in a manner consistent with applicable law.
   - policies and procedures prohibit any officer or employee from accepting a bequest or gift of fiduciary assets except as permitted under 12 CFR 150.400 (FSAs). National banks are not subject to 12 CFR 150.400; however, the OCC views these types of policies and procedures to be consistent with safe and sound banking practices. (Updated in version 1.1)

7. Review process used by the bank to administer own bank and holding company stock. This includes decisions and documentation to retain stock and procedures for voting proxies. Determine whether the bank (Updated in version 1.1)

   - has a policy in place that prevents purchase of own bank and holding company stock in discretionary accounts.
   - has a policy in place that requires that the retention of own bank and holding company stock in discretionary accounts is authorized by applicable law and remains an appropriate investment for the account.
   - complies with 12 USC 61 (national banks) and does not vote shares of own bank stock in the election of directors. Refer to the "Conflicts of Interest" booklet of the *Comptroller's Handbook* for more information (national banks and FSAs).
   - has a process in place to avoid conflicts of interest with respect to voting national bank stock in matters other than the election of the board of directors, voting FSA stock in all matters, voting holding company stock, and voting shares of companies in which directors, officers, employees, or related organizations have a controlling interest.

8. If proprietary mutual funds (mutual funds sponsored by the bank or an affiliate, or for which the bank or affiliate is the investment advisor or provides other services to the fund for a fee) are used in discretionary accounts, evaluate the bank's procedures for ensuring that the proprietary funds are appropriate fiduciary investments. Consider whether

   - such investment is authorized by applicable law.
   - proprietary mutual funds are monitored in the same way as unaffiliated funds.
   - fee practices are authorized by and disclosed in accordance with applicable law.
   - disclosures are made or the investment prospectus is delivered to appropriate parties in accordance with applicable law.

9. Review brokerage placement practices. Determine whether

   - brokerage allocation decisions and brokerage fees are monitored for reasonableness relative to the services provided.
   - soft-dollar arrangements fall within safe harbor provisions of section 28(e) of the Securities Exchange Act of 1934 (refer to 15 USC 78bb(e)). Refer to appendix D of the "Conflicts of Interest" booklet of the *Comptroller's Handbook* for more information. (Updated in version 1.1)
   - the bank obtains best execution for its clients.
   - any payments for order flow received by related parties and interests from third parties such as brokers, exchanges, trading networks, or market makers are
     - authorized by applicable law.
     - disclosed in accordance with applicable law.
     - subject to adequate oversight to ensure compliance with applicable law and that the bank has obtained best execution for client securities transactions.
   - trades are fair and equitably allocated to all accounts, subject to applicable law.

10. If the bank uses an affiliated broker to effect securities transactions for fiduciary accounts, determine whether

    - applicable law does not prohibit use of an affiliated broker.
    - the bank does not profit from securities transactions executed through an affiliated broker. (Payment by bank to the affiliated broker can cover only the cost of executing the transaction.)
    - the bank provides adequate disclosure of such relationships to affected clients or obtains consent from parties with capacity to give consent.

Objective 5: Determine the quantity of risk and the quality of risk management relating to investment management services.

1. Review investment management policies and procedures. Policies should address the following:

    - Compliance with applicable law, including 12 CFR 9.11 (national banks) or 12 CFR 150.260 (FSAs) and state laws' prudent investor requirements.
    - Business goals and objectives, investment philosophy, fiduciary responsibilities, ethical culture, risk appetite, and risk management framework.
    - Descriptions of investment products and services.
    - Approval of new or modified investment products.
    - Use of investment policy statements.
    - Use of asset allocation and other portfolio models.
    - Periodic investment portfolio reviews.
    - Investment research, including economic and capital market analyses and reporting.
    - Securities trading policies and procedures (12 CFR 12.7, "Securities Trading Policies and Procedures" (national banks), or 12 CFR 151.140, "What Policies and Procedures Must I Maintain and Follow for Securities Transactions?" (FSAs)).
    - Brokerage placement policies and procedures.
    - Selecting and monitoring third-party service providers.
    - Portfolio MIS and technology applications.
    - Proxy voting for discretionary accounts.

2. Evaluate processes used to develop, approve, implement, and monitor fiduciary account investment policies. Refer to the "Investment Management Services" booklet of the *Comptroller's Handbook.*

3. Evaluate investment selection, acquisition and sales processes. Consider the following:

    - Processes used to research, and estimate risk and return and other relevant attributes for potential investments.
    - Processes used to value portfolio assets and account for portfolio transactions.
    - Portfolio trading systems and controls.

4. Evaluate adequacy and effectiveness of risk reporting and exception tracking processes. Does the bank maintain appropriate management reports relating to investment performance, risk levels, and policy exception identification and follow-up?

5. If the bank delegates investment management authority, review process used to select and monitor third-party investment managers or advisors. Refer to the "Investment Management Services" booklet of the *Comptroller's Handbook*.

6. Select a sample of fiduciary accounts for which the bank has investment discretion or provides investment advice for a fee. If possible, select from the sample of accounts used in the fiduciary account administration review under objective 3. In reviewing these accounts,

   - determine compliance with investment objectives and guidelines in the governing instrument, the account-level investment policy statement, applicable laws and regulations, and bank policies and procedures.
   - determine whether the investment objective is current and assets are invested consistently with the bank's current asset allocation for the objective.
   - investigate holdings of securities not on approved lists and review asset concentrations exceeding 10 percent of the market value of the account. Determine if retention is prudent.
   - determine whether there are asset holdings (e.g., investments in own bank, affiliate stock, own bank or affiliate deposit products, or proprietary or affiliated investment products such as mutual funds) that could present a conflict of interest. If so, has the bank appropriately determined that the conflict of interest is authorized and the investment is in the best interest of the account?
   - verify that client or co-trustee approvals are obtained where necessary.
   - determine whether unique assets are managed appropriately.
   - evaluate effectiveness of investment review processes in identifying and addressing investment-related issues (12 CFR 9.6 (national banks) or 12 CFR 150.200-220 (FSAs)).

7. For marketable securities, review the following:

   - Quality of investment research and documentation, including use of third-parties.
   - Use of approved securities lists. Evaluate process for maintaining such lists, including follow-up on sale or other disposition of assets from the list.
   - Approval authorities and policy exception tracking systems.
   - Monitoring processes to govern compliance with applicable law and internal bank policies and procedures.

8. For investment company securities (mutual funds),

   - review quality of the investment analysis, selection, and approval processes.
   - review quality of information reports and ongoing monitoring. (Monitoring should consider such factors as investment performance, risks, and fees.)

- if the bank maintains an approved mutual fund list, determine the bank's policy on purchase or retention of unapproved mutual funds. If the bank retains or invests in funds not on the approved list, determine whether these investments
  – are appropriately approved and adequately documented.
  – comply with applicable law.
  – are included on exception reports and adequately monitored.

9. For closely held businesses, determine whether

- closely held ownership interests are managed in accordance with applicable law, including the terms of the governing instrument. Consider the following:
  – Role of the bank and its fiduciary duties and responsibilities.
  – Quality and timeliness of decisions to acquire, retain, or dispose of such assets.
  – Quality of business valuation processes. Determine whether adherence to Internal Revenue Service (IRS) Revenue Ruling 59-60 is part of the process.
  – Receipt and use of financial information on the business and its industry.
  – Management succession planning for closely held companies.
  – Quality of relationships with account beneficiaries, family members, and other investors.
- bank employees serve on the board of directors, or in a similar capacity, of a closely held company. If so, does the bank
  – maintain adequate insurance coverage?
  – reimburse the account for the payment of benefits or fees to the bank or its employees for representing the interests of beneficiaries, unless the governing document specifically authorizes the bank to receive such compensation?

Refer to the "Unique and Hard-to-Value Assets" booklet of the *Comptroller's Handbook*.

10. For real estate, determine whether

- decisions to acquire, retain or dispose of the investment were appropriate and supported.
- real estate valuation and inspection processes are adequate.
- appropriate financial information on real estate and its market is periodically obtained and evaluated.
- title to property is properly perfected.
- environmental review was performed and completed before acceptance or acquisition.
- adequate insurance coverage is maintained with the bank as loss payee.
- real estate taxes are paid on time.
- farm management accounts are properly administered and documented. Consider whether
  – bank has signed a contract with the owner that clearly details the bank's responsibilities.
  – bank has signed leases with tenants that detail each party's responsibilities.

  - farm manager keeps adequate records, including financial statements, tax returns, and periodic reports on the operation.

  Refer to the “Unique and Hard-to-Value Assets” booklet of the *Comptroller’s Handbook*.

11. For loans secured by real estate, evaluate the quality of the following, as applicable:

  - Loan underwriting standards
  - Collection processes and past-due trends
  - Collateral valuation and inspections processes
  - Tax payment processes
  - Insurance coverage
  - Management of environmental liability issues

  Refer to the “Unique and Hard-to-Value Assets” booklet of the *Comptroller’s Handbook*.

12. For mineral interests, determine whether

  - receipt of lease, royalty, and delay rental payments is timely.
  - the bank takes appropriate action if payments are not received.
  - working interests are reviewed for profitability and potential environmental hazards.
  - expenditures are analyzed and approved before they are paid.

  Refer to the “Unique and Hard-to-Value Assets” booklet of the *Comptroller’s Handbook*.

13. Review a sample of the bank’s CIFs, and determine whether such funds are managed in compliance with 12 CFR 9.18 (national banks; also applicable to FSAs pursuant to 12 CFR 150.260(b)). Evaluate effectiveness of the bank’s processes for limiting participation in funds to eligible accounts. (Updated in version 1.1)

  Refer to the “Collective Investment Funds” booklet of the *Comptroller’s Handbook.*

Objective 6: Determine the quantity of risk and the quality of risk management for fiduciary operations.

Coordinate this review with examiners responsible for the major CAMELS/ITCC areas and the Internal Controls and Audit portion of the examination to avoid duplication of effort.

1. For asset management operations, consider audit and compliance reports of operational areas. Follow up on significant deficiencies and determine whether effective corrective action has been taken.

2. Discuss the following with the examiner reviewing IT, and follow up with bank management:

  - Existing IT systems and planned changes to IT systems.

- Whether IT systems are sufficient to support current and planned fiduciary activities.
- Quality of the bank’s information security and business resumption and contingency planning processes.
- Quality of the bank’s process for selecting and monitoring third parties.
- Logical access controls on computer systems to adequately segregate duties.

Assess integrity, confidentiality, and availability of data used to record, analyze, and report information related to fiduciary operations. Consider input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to data and procedures in place to monitor system activities. Determine if these controls have been independently validated. Coordinate this review with examiners responsible for all functional areas of the examination, including internal controls, to avoid duplication of effort. Share findings with the examiner reviewing IT.

3. If the bank has outsourced data processing or other operational functions, evaluate the bank’s process for selecting and monitoring third parties. Discuss the process with management and document significant weaknesses. For more information, refer to OCC Bulletin 2013-29, OCC Bulletin 2017-21, and the “Outsourcing” booklet of the *FFIEC IT Examination Manual*.

4. Evaluate the quality of written operations policies and procedures. Consider the following:

   - Approval authorities and accountability standards.
   - Separation of duties among transaction initiation, posting, settlement, asset control, and reconciling functions.
   - Cross training or rotation of duties.
   - Joint custody or control standards for client funds and assets.
   - Third-party risk management.
   - Information security, business resumption, and contingency planning systems.

5. Review record keeping for compliance with 12 CFR 9.8 (national banks) or 12 CFR 150.410-430 (FSAs), 12 CFR 12 (national banks) or 12 CFR 151 (FSAs), and other applicable laws and regulations. Determine whether the bank

   - adequately documents establishment and termination of each fiduciary account and maintains adequate records.
   - retains fiduciary account records for three years from the termination of the account or the termination of litigation relating to the account, whichever comes later.
   - maintains fiduciary account records separate and distinct from other records of the bank.
   - maintains securities transaction trading records required under 12 CFR 12.3 (national banks) or 12 CFR 151.50 (FSAs) for a minimum of three years.

6. Determine whether the bank provides securities transaction customer notifications consistent with the requirements of 12 CFR 12.4 (national banks), 12 CFR 12.5 (national banks), or 12 CFR 151, subpart B (FSAs).

7. Review controls over asset set-up and maintenance, including pricing, administration of corporate actions, proxy voting, and income collection. Consider the following:

   - Use of independent sources for information on assets.
   - Use of asset models and secondary review over asset set-ups.
   - Controls over changes to the security master file.
   - Periodic asset pricing.
   - Use of exception reports to identify stale prices and unusual fluctuations.
   - Timely and accurate processing of corporate actions, such as stock dividends, stock splits, and bond calls.
   - Whether controls are in place to take timely action on voluntary corporate actions, including obtaining approval from outside parties.
   - Whether distribution of proxy materials and disclosure of information about shareholders whose securities are registered in a bank nominee name comply with SEC Rules 17 CFR 240.14-17. Determine whether the bank
     – obtains a clear consent or denial for disclosure of beneficial owner information for each account.
     – appropriately passes information received from issuers, such as proxies and annual reports, to beneficial owners.
     – responds to issuers' requests for information in a timely manner.
   - Controls over income collection, including dividends and interest.

8. Review transaction processing controls. Consider the following:

   - Timeliness and accuracy of transaction documentation and posting.
   - Management of routine and nonroutine manual instructions.
   - Transaction and account balancing processes and controls.
   - Controls over the release or disbursement of assets or funds.

9. Review balancing and reconcilement controls. Consider the following:

   - Transaction and account balancing processes and controls.
   - Timeliness and independence of reconcilement functions.
   - Exception reporting and escalation standards.
   - Controls for suspense (house) accounts.

10. Evaluate security trade settlement processes. Determine whether

    - proper trade instructions are received and documented.
    - trade tickets are properly controlled and contain required information.
    - broker confirmations are reconciled to trade tickets.

- failed trades are promptly identified and effectively addressed.
- confirmations are sent as required and contain required information.
- depository position changes are matched to changes on the bank's accounting system.

11. Evaluate asset custody and safekeeping processes and controls (12 CFR 9.13 (national banks) or 12 CFR 150.230-250 (FSAs)). Determine whether

    - fiduciary assets are placed in joint custody or control of not fewer than two fiduciary officers or employees.
    - fiduciary account assets are kept separate from bank assets and other fiduciary account assets.
    - third-party custodian or depository holds fiduciary assets. If so, determine whether such action is consistent with applicable laws and regulations and supported by adequate safeguards and controls (e.g., dual control over free deliveries).
    - fiduciary assets physically held by the bank are kept in a controlled vault or securities cage with access controls such as dual controls, vault entry records, asset tickets, physical security measures (12 CFR 21, subpart A, "Minimum Security Devices and Procedures" (national banks), or 12 CFR 168, "Security Procedures" (FSAs)), and periodic vault counts. (Updated in version 1.1)
    - bank has adequate controls over unissued checks and securities.

    Refer to the "Custody Services" and "Asset Management Operations and Controls" booklets of the *Comptroller's Handbook*.

12. Review processes and controls for the escheatment of unclaimed items such as outstanding checks and suspense account entries. Consider whether the bank identifies escheatable items and follows the notification, reporting, and escheatment requirements of the proper jurisdiction.

13. Determine whether the bank engages in transfer agent activity. If so,

    - if the bank is required to register as transfer agent under section 17A(c) of the Securities Exchange Act of 1934 (15 USC 78q-1(c)), determine whether the bank has followed the appropriate process for registration with the OCC including filing Form TA-1. Refer to 12 CFR 9.20(a)(1) for specific requirements for national banks and 12 USC 78q-1(c) for national banks and FSAs. (Updated in version 1.1)
    - if the bank is required to register as a transfer agent, determine whether the bank is following SEC rules applicable to transfer agents, including reporting requirements under 17 CFR 240.17Ac2-2 and operational requirements found in 17 CFR 240.17Ad-1 through 240.17Ad-20. Note that 17 CFR 240.17Ad-4 contains exemptions from certain of these reporting and operational requirements.
    - if the bank is a transfer agent that is neither registered nor required to register, determine whether appropriate internal controls are in place.

Objective 7: Assess the bank's RNDIP sales program and determine the level of risk it poses to the bank and the effectiveness of RNDIP program risk management.

Most retail RNDIP sales programs involve arrangements with affiliated or unaffiliated securities brokers that are regulated by the SEC, the Financial Industry Regulatory Authority (FINRA), and state insurance regulators. Refer to the "Retail Nondeposit Investment Products" booklet of the *Comptroller's Handbook*.

1. If not previously reviewed, obtain and analyze the following bank-level information applicable to the retail brokerage program:

   - Board and oversight committee minutes and reports.
   - Bank program policies and procedures.
   - Program management statement.
   - Management's expectations for RNDIP sales including business plan sales projections.
   - Third party service providers and product offerings.
   - Sales volume (by product, by registered representative, etc.).
   - Compensation and incentive programs for bank referrals and investment sales.
   - Bank employee training.
   - Sales setting, disclosures, and advertisement.
   - Vendor management.
   - Risk management, compliance, and internal audit reports.
   - Financial information, including revenue and expense data.
   - Written agreement between the bank and the retail broker.
   - Audit, compliance, or risk management testing results.
   - Complaints, litigation, and settlement information. For customer complaints, review data from the OCC's Customer Assistance Group and the bank to assess the level, volume, and themes. Complaints are a *potential* indicator of risk management weaknesses or other deficiencies, such as violations of laws or regulations. (Updated in version 1.1)

2. Determine level of risk to the bank from the program. Consider the following:

   - Nature and complexity of activities.
   - Financial significance to the bank's earnings and capital.
   - Identified deficiencies.

3. Assess effectiveness of the bank's RNDIP oversight and risk management systems:

   - Evaluate appropriateness of the board and senior management reports for overseeing the bank's retail brokerage program.
   - Evaluate effectiveness of the initial and ongoing due diligence process in selecting and monitoring the securities broker.

- Determine effectiveness of the bank's controls systems (compliance, internal audit, independent risk management).
- Determine the bank's compliance with applicable banking laws and regulations including 15 USC 6801 et seq. (Gramm–Leach–Bliley Act [GLBA]), 12 CFR 218 (Regulation R), 17 CFR 247 (particularly networking exemption requirements), 12 CFR 14 (Consumer Protection in Sales of Insurance), 12 USC 371c and 371c-1 (transactions between affiliates and the bank), and 12 CFR 1016 (privacy of consumer information). (Updated in version 1.1)
- Evaluate the effectiveness of the bank's consumer complaint resolution, monitoring, and reporting processes. For more information, refer to the "Compliance Management Systems" booklet of the *Comptroller's Handbook*.

Objective 8: Determine whether to expand the procedures or develop a plan for corrective action. Consider whether

- management can adequately manage the bank's risks.
- management can correct fundamental problems.
- to propose a strategy to address identified weaknesses and discuss strategy with the supervisory office.

Refer to the "Asset Management" series of booklets of the *Comptroller's Handbook* for expanded procedures.

Objective 9: After completing expanded procedures, determine whether verification procedures should be performed.

The extent to which examiners perform verification procedures is decided case by case after consultation with the ADC. Direct confirmation with the bank's customers must have prior approval of the ADC and district deputy comptroller. The Enforcement and Compliance Division, the district counsel, and the district accountant should also be notified when direct confirmations are being considered.

Objective 10: Conclude the review of the bank's asset management activities.

1. If applicable, discuss deficiencies with management and obtain commitments for corrective action.

2. Consult with the EIC and other examining personnel to identify and communicate to other examiners conclusions and findings from the asset management review that are relevant to other areas being reviewed.

3. Use the results of the foregoing procedures and other applicable examination findings to compose comments (e.g., asset management activities, retail brokerage, violations, and MRAs) for the ROE.

4. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View (e.g., ratings, core knowledge, MRAs, and violations). (Updated in version 1.1)

5. In discussion with the EIC, provide preliminary conclusions about the following:

   - Quantity of risk.
   - Quality of risk management.
   - Aggregate level and direction of asset management risk and aggregate level and direction of operational, compliance, reputation, and strategic risks as they relate to asset management.
   - Complete the summary conclusions in the “Risk Assessment System” and “Other Risks” sections of this booklet.
   - Supervisory strategy recommendations.

Bank Secrecy Act/Anti-Money Laundering

Conclusion: The bank's BSA/AML compliance program is (strong, satisfactory, insufficient, or weak).

Introduction

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Specialty Area Considerations" > "Bank Secrecy Act/Anti-Money Laundering"

The OCC is required to review the BSA compliance program of each bank during every supervisory cycle.[46] The BSA/AML review must include a conclusion about the adequacy of the bank's BSA program.

Examiners focus on areas of highest BSA/AML compliance risk for community banks. Examiners generally use data from the Financial Crimes Enforcement Network's reporting database, the OCC's money laundering risk system, and other information as appropriate when determining a bank's BSA/AML risks.

Findings are considered in a safety and soundness context as a part of the management component of the bank's CAMELS ratings. Serious deficiencies in the bank's BSA/AML compliance create a presumption that the bank's management component rating will be adversely affected because risk management practices are less than satisfactory.[47] Examiners should be alert to situations in which management weaknesses identified in other areas of the bank reveal potential deficiencies in BSA/AML program oversight.

While BSA/AML/OFAC compliance is not a defined RAS category, examiners assess the quantity of risk and quality of risk management using the matrix in the "Other Risks" section of this booklet as a guide. These assessments are then considered when determining the bank's overall compliance risk (and other appropriate risks) and used by the portfolio manager, along with the potential impact of those risks on the bank as a whole, to develop the scope of future BSA/AML/OFAC supervisory activities.

Complete this section's objectives to assess the adequacy of the bank's BSA/AML compliance program and compliance with BSA/AML/OFAC regulations. When assessing BSA/AML/OFAC compliance, examiners should refer to the *FFIEC BSA/AML Examination Manual*. (Updated in version 1.1)

[46] 12 USC 1818(s) requires the OCC to review the BSA compliance program of each insured depository institution.

[47] Refer to OCC Bulletin 2012-30.

Objectives and Procedures

Minimum Objective

(Section updated in version 1.1)

Review Financial Crimes Enforcement Network (FinCEN) data and the OCC's money laundering risk system report to assist in the scoping and planning of the BSA/AML examination. This information should assist the examiner in determining the highest-risk areas of the bank, identify the appropriate examination procedures, and help determine areas for transaction testing.

Assess the adequacy of the bank's BSA/AML compliance program and determine compliance with BSA/AML regulations. While OFAC regulations are not part of the BSA, evaluation of OFAC compliance is generally included in BSA/AML examinations. The OFAC review evaluates the sufficiency of the bank's implementation of policies, procedures, and processes governing compliance with OFAC laws and regulations, using applicable procedures from the OFAC section of the *FFIEC BSA/AML Examination Manual*.

Perform the minimum examination procedures in the "Core Examination Overview and Procedures for Assessing the BSA/AML Compliance Program" section of the *FFIEC BSA/AML Examination Manual* as well as any additional core or expanded procedures identified during the scoping and planning of the BSA/AML examination. Consider whether

- BSA/AML compliance program includes effective controls for compliance with BSA requirements and effectively controls the risks within the bank.
- policies, procedures, and processes are effective for compliance with OFAC sanctions.

Develop preliminary assessments of the quantity of risk and quality of risk management using the BSA/AML/OFAC risk indicators in the "Other Risks" section of this booklet.

After completing the minimum examination procedures in the "Core Examination Overview and Procedures for Assessing the BSA/AML Compliance Program" section of the *FFIEC BSA/AML Examination Manual* and any additional core or expanded procedures from the *FFIEC BSA/AML Examination Manual*, conclude the BSA/AML review by completing objective 2.

Other Assessment Objectives

(Section updated in version 1.1)

Objective 1: Complete selected examination procedures from the *FFIEC BSA/AML Examination Manual*. (Note: This objective pertains to completion of additional procedures beyond the minimum examination procedures in the "Core Examination Overview and Procedures for Assessing the BSA/AML Compliance Program" section of the *FFIEC BSA/AML Examination Manual*.)

Objective 2: Conclude the BSA/AML/OFAC review.

1. Refer to the “Developing Conclusions and Finalizing the Examination” section of the *FFIEC BSA/AML Examination Manual.*

2. If considering a BSA/AML enforcement action, consult with the EIC and ADC to determine whether to recommend an enforcement action, including CMPs. The EIC and ADC should also consult with the assigned OCC compliance officer and OCC legal counsel. The OCC is required by statute to issue a cease-and-desist order when citing BSA compliance program violations, or if the bank fails to correct a previously reported problem with the BSA compliance program. Refer to 12 USC 1818(s); 12 CFR 21.21; OCC Bulletin 2007-36, “Bank Secrecy Act/Anti-Money Laundering: BSA Enforcement Policy”; and OCC Bulletin 2016-6, “Bank Secrecy Act/Anti-Money Laundering: Process for Administrative Enforcement Actions Based on Noncompliance With BSA Compliance Requirements or Repeat or Uncorrected BSA Compliance Problems.”

3. Provide and discuss with bank management a preliminary list of deficiencies and violations. BSA/AML conclusions should not be discussed with bank management before vetting the findings though established processes. OCC Bulletin 2016-6 sets forth the general process to be followed in enforcement cases based on BSA violations.

4. In discussion with the EIC, provide preliminary conclusions about the following:

   - Adequacy of the BSA/AML and OFAC compliance programs.
   - Compliance with BSA/AML regulations. OFAC-related MRAs and suspected violations regarding OFAC must be reported to the Compliance Risk Policy Division of the OCC’s Bank Supervision Policy Department for referral to OFAC. The OCC generally does not cite violations of OFAC laws and regulations. Deficiencies in a bank’s policies, procedures, and processes to comply with OFAC laws and regulations are addressed through other supervisory actions, such as MRAs or enforcement actions.
   - Quantity of risk.
   - Quality of risk management.
   - Aggregate level and direction of BSA/AML/OFAC risk and aggregate level and direction of compliance, operational, reputation, and strategic risks as they relate to BSA/AML/OFAC compliance. Examiners may use appendixes A and B of this booklet as necessary.
   - Supervisory strategy recommendations.

5. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View, including core knowledge.

Consumer Compliance

Conclusion: Consumer compliance is rated (1, 2, 3, 4, or 5).

Introduction

Related "Bank Supervision Process" Booklet Section

- "Examination Authority and Full-Scope, On-Site Examination Requirement" > "Specialty Area Considerations" > "Consumer Compliance"
- "Uniform Interagency Consumer Compliance Rating System"

Consumer compliance encompasses reviews of the bank's compliance with consumer protection-related laws and regulations. The consumer compliance examination should be risk-based, though examination scopes must be consistent with statutory mandates, OCC minimum standards, and interagency commitments regarding examination frequency or minimums. The consumer compliance review should focus on areas of highest consumer compliance risk for community banks—for example, those with potential to cause consumer harm.

Banks are required to comply with all applicable consumer protection-related laws and regulations. Evaluating the bank's compliance management system (CMS) as it pertains to consumer compliance is a critical component of the consumer compliance examination. As part of rating consumer compliance, examiners must review the bank's CMS as it pertains to consumer compliance at least once per supervisory cycle. The overall bank's CMS should cover all applicable laws and regulations and cover all areas of the bank. Examiners should consider aspects of the bank's CMS that do not pertain to consumer protection-related laws and regulations when assessing the bank's overall risk management program and determining the management component rating. Refer to the "Compliance Management Systems" booklet of the *Comptroller's Handbook* for more information regarding the assessment of CMS and determining the consumer compliance rating.

The consumer compliance section of the core assessment is structured to evaluate the effectiveness of the bank's CMS relative to the bank's products, services, and activities. Examiners consider the following areas of consumer compliance:

- Fair lending
- Lending regulations
- Deposit regulations
- Other consumer protection-related regulations

Examiners should identify and evaluate compliance risk associated with all laws and regulations applicable to these four areas of consumer compliance each examination cycle and assess the effectiveness of the bank's CMS in managing risks. Examiners are also required to

- assess the bank's compliance with the Flood Disaster Protection Act (FDPA) each examination cycle.
- assess the bank's Servicemembers Civil Relief Act (SCRA) risk each examination cycle.
- conduct an SCRA examination that includes risk-based transaction testing at least once every three examination cycles.

While the risks arising from the four areas of consumer compliance are not formally defined RAS categories, examiners should assess quantity of risk and quality of risk management for each area. The "Other Risks" section of this booklet includes indicators for examiners to use as needed to assist in this assessment. These assessments are then considered when determining the overall compliance risk (and other appropriate risks)[48] and used by the portfolio manager, along with the potential impact of those risks on the bank as a whole, to develop the scope of future consumer compliance supervisory activities.

Complete this section's objectives to assign the consumer compliance rating using the Uniform Interagency Consumer Compliance Rating System. The consumer compliance rating reflects the effectiveness of the bank's CMS to ensure compliance with consumer protection-related laws and regulations and reduce the risk of harm to consumers. The consumer compliance rating system is organized under three broad categories—board and bank management oversight, compliance program, and violations of law and consumer harm. Examiners should assess each category and its assessment factors (summarized in table 3) when assigning the consumer compliance rating. When assigning the rating, examiners should consult with the EIC, examiners assigned to review internal controls and audit, and other examining staff as appropriate.

Table 3: Consumer Compliance Rating Categories and Assessment Factors

	Compliance management system components		**Violations of law and consumer harm**
Category	**Board and management oversight**	**Compliance program**	
Assessment factors	• Oversight and commitment including third-party risk management • Change management • Comprehension, identification, and management of risk • Self-identification and corrective action	• Policies and procedures • Training • Monitoring and audit • Consumer complaint response	• Root cause • Severity • Duration • Pervasiveness

Refer to the "Compliance Management Systems" booklet of the *Comptroller's Handbook* for more information regarding components of CMS related to consumer compliance and assigning the consumer compliance rating. The consumer compliance rating system can be found in the "Uniform Interagency Consumer Compliance Rating System" section of the "Bank Supervision Process" booklet or appendix A of the "Compliance Management Systems" booklet of the *Comptroller's Handbook*. (Updated in version 1.1)

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[48] Examples of other risks commonly interrelated with, or correlated to, compliance risk include operational, reputation, and strategic.

For areas of low compliance risk, examiners should use procedures in the minimum objective as a starting point to scope the remaining consumer compliance work. Even when all consumer compliance areas are consistently identified as low risk, examiners should periodically expand supervisory activities beyond the minimum objective to include transaction testing to validate that the bank's compliance process continues to be effective.

For banks with more than $10 billion in total assets, refer to the "Bank Supervision Process" booklet for information regarding the OCC and Consumer Financial Protection Bureau's (CFPB) statutory authorities. (Updated in version 1.1)

If the bank is identified on the final fair lending screening test, a full-scope fair lending examination must be completed using the procedures in the "Fair Lending" booklet of the *Comptroller's Handbook*.

Objectives and Procedures

Minimum Objective

Determine the consumer compliance rating, quantity of compliance risk, and quality of compliance risk management, aggregate compliance risk, and direction of compliance risk. Factors to consider when assessing the quantity of risk and quality of risk management for consumer lending regulations, consumer deposit regulations, fair lending, and other consumer protection-related regulations can be found in the "Other Risks" section of this booklet. If the bank's total assets are over $10 billion, examiners must consider the bifurcated authorities of the OCC and CFPB. For more information, refer to the "Bank Supervision Process" and "Compliance Management Systems" booklets of the *Comptroller's Handbook*. (Updated in version 1.1)

Discuss with bank management actual or planned changes in the bank's compliance management system as it relates to consumer compliance and other factors that could affect the bank's compliance risk, including

- changes in compliance structure and key personnel responsible for compliance that weaken or strengthen the bank's compliance program.
- changes in policies, processes, or control systems relating to consumer compliance.
- changes in the bank's policies, processes, or control systems for compliance with the FDPA or in the volume of loans originated in special flood hazard areas.
- changes in the bank's policies, processes, or controls for compliance with the SCRA or in the volume of loans subject to SCRA (50 USC 3901 et seq.). (Updated in version 1.1)
- changes in products, services, customer base, or delivery channels that could affect compliance risk, including those offered through affiliates or third parties.
- significant changes in products and services offered that could affect consumer compliance.
- significant changes in third-party relationships, contracts, and activities.
- changes in the bank's compliance training process, particularly the process for training employees regarding new regulations or changes to existing regulations.

- other factors that may have changed the bank's compliance risk profile.

Refer to OCC Bulletin 2017-43, OCC Bulletin 2013-29, and OCC Bulletin 2017-21.

Perform the following:

- Review the supervisory strategy and EIC's scope memorandum.
- Determine whether there are any supervisory activity recommendations resulting from any licensing applications submitted by the bank.
- Review the results of the OCC's consumer compliance supervisory activities since the last examination. Identify any items that require follow-up (e.g., MRAs, violations, or enforcement actions).
- Review the results of the most recent CRA evaluation.
- Review the bank's compliance reviews and risk assessments, including those related to the FDPA, the SCRA, and fair lending. Assess bank management's responses and the adequacy of corrective actions.
- Review compliance committee minutes to assess bank management and the board's ongoing commitment to compliance, including timely corrective action for deficiencies.
- Review the results of the most recent fair lending supervisory activity (fair lending screening results if there has not been a recent full-scope fair lending examination). Perform a fair lending risk assessment if the OCC has not performed a fair lending risk assessment during the current supervisory cycle. Considering the bank's high-risk factors, determine whether the bank should be added to the fair lending screening list.
- Review the bank's compliance with the FDPA. The risk-based examination of the bank's flood insurance program should review any audit of the bank's flood protection program and conduct transaction testing of a sample of mortgage files if the audit does not include transaction testing. At a minimum, examiners must perform transaction testing once during every three supervisory cycles.
- Assess the bank's SCRA risk and determine whether an SCRA examination should be performed. A risk-based SCRA examination that includes transaction testing must be conducted at least once during every three supervisory cycles.
- Review complaint data or reports from the OCC's Customer Assistance Group and the bank. For banks with more than $10 billion in total assets, also review CFPB complaint data. Assess the volume, themes, and trends of complaints. Reviewing customer complaint data can provide examiners with indicators of potential risk management weaknesses or other deficiencies, such as violations of laws or regulations. Such deficiencies can affect any risk area. Communicate relevant information from the complaint data review to examiners of other functional areas and the EIC, as appropriate. (Updated in version 1.1)
- Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is required. As requested, follow up on significant compliance-related audit issues identified by the examiner reviewing the bank's audit program:
  - Discuss outstanding compliance audit issues with bank management.

- If warranted based on the foregoing discussions or if requested by the examiner reviewing audit, obtain and review a risk-based sample of internal compliance audit reports and work papers.
- Discuss with bank management changes in the scope, personnel, or frequency of the compliance review or audit function that could increase or decrease the function's reliability.
- Contact the examiner assigned to review IT to determine whether there have been changes in third-party systems, software, and applications used to support compliance activities. If yes, determine what due diligence process the bank used to test the systems or software and whether appropriate training was provided to staff. As requested, follow up on significant compliance-related audit or IT issues identified by the examiner reviewing the bank's audit or IT program.

If the bank's activities, risk profile, or consumer compliance policies, processes, or control systems have changed significantly or if the review of the foregoing information raises substantive issues, examiners should expand the activity's scope to include additional objectives or procedures. If this review does not result in significant changes or issues, conclude the consumer compliance review by completing objective 9.

Other Assessment Objectives

Examiners should choose only those objectives and procedures necessary to assess the bank's condition, risks, and effectiveness of the CMS as it pertains to consumer compliance. Examiners typically do not need to carry out every procedure listed.

Objective 1: Determine the scope of the consumer compliance review and what transaction testing should be included. The extent of transaction testing should reflect the bank's compliance risk profile, compliance review and audit coverage and results, and time elapsed since the last examination. If the bank's total assets are over $10 billion, examiners must consider the bifurcated authorities of the OCC and CFPB. For more information, refer to the "Bank Supervision Process" and "Compliance Management Systems" booklets of the *Comptroller's Handbook*. (Updated in version 1.1)

1. Review the supervisory information to determine whether previously identified deficiencies require follow-up in this area.

2. Obtain and review the following information to determine the complexity of the bank's compliance environment. Determine whether the systems that bank management uses to supervise compliance adequately identify, measure, monitor, and control compliance risk. Obtain and review the following:

    - Organizational charts, job descriptions, turnover, and communication channels to determine how bank management communicates and manages risk through policies, procedures, compliance reviews, and internal controls.

- The bank's training programs and criteria for compliance training for key personnel. Determine whether programs are appropriate based on functions performed and likelihood of noncompliance.
- If applicable, documentation supporting new, modified, or expanded products or services, or initiatives to determine the effectiveness of compliance and planning.
- Complaint data or reports from the OCC's Customer Assistance Group and the bank. Assess the volume, themes, and trends of complaints. For banks with over $10 billion in total assets, also review CFPB complaint data. Reviewing customer complaint data can provide examiners with indicators of potential risk management weaknesses or other deficiencies, such as violations of laws or regulations. Such deficiencies can affect any risk area. Communicate relevant information from the complaint data review to examiners of other functional areas and the EIC, as appropriate. (Updated in version 1.1)

3. Discuss with the examiner responsible for completing the Internal Controls and Audit section of the core assessment whether significant audit findings require follow-up or whether a review of audit work papers is required. If needed, compliance worksheets in the *Consumer Compliance* series of booklets of the *Comptroller's Handbook* can be used as a guide for the work paper review.

4. Using overall results from the Internal Controls and Audit section of the core assessment in this booklet, determine to what extent examiners can rely on compliance reviews or audits by area to set the scope of the compliance supervisory activities. Consider the following:

   - Whether compliance reviews or audits cover all applicable consumer protection-related laws and regulations for all products and services and all bank departments, such as trust and private banking, as well as the bank's website and e-banking activities.
   - Whether compliance reviews and audits address areas with moderate and high quantities of risk and include appropriate sample sizes.
   - Adequacy of documentation and frequency of reviews or audits.
   - Whether the system for ensuring corrective action is effective.

5. Discuss with the examiner responsible for completing the IT section of the core assessment whether significant deficiencies raise questions about integrity, confidentiality, or availability of data and require follow-up.

6. Assess integrity, confidentiality, and availability of data used to record, analyze, and report information related to consumer compliance. Consider input, processing, storage, access, and disposal of data. Focus on measures taken to limit access to data and procedures in place to monitor system activities. Determine if these controls have been independently validated. Coordinate this review with examiners responsible for all functional areas of the examination, including internal controls, to avoid duplication of effort. Share findings with the examiner reviewing IT.

Objective 2: Assess the bank's fair lending risk. (Updated in version 1.1)

Examiners must perform a fair lending risk assessment of each bank during every supervisory cycle. For banks with total assets over $500 million, examiners must use the OCC's fair lending risk assessment tool. Examiners may use the factors in the "Fair Lending Risk Indicators" section of this booklet for community banks with assets under $500 million. Based on this risk assessment, examiners may initiate appropriate supervisory activities to assess compliance with fair lending laws and regulations.

The OCC's fair lending screening process uses Home Mortgage Disclosure Act[49] (HMDA) and other information and is designed to assist supervisory offices in the annual identification of banks believed to present the highest fair lending risk. The screening process only complements the supervisory office's fair lending risk assessment activities. Supervisory offices may consult with the appropriate OCC compliance officer to request that banks be added or removed from the fair lending examination list that results from the screening process, to request modifications to the proposed fair lending examination scope, or for more guidance (for example, regarding allocation of examiner resources.) In addition, supervisory offices should review compliance management systems in community banks to identify those with inadequate fair lending processes or systems. If activities in the core assessment are insufficient to determine whether the bank's fair lending processes and systems are adequate, or if the core assessment or other supervisory activities result in substantive concerns about fair lending, the steps that follow assist the examiner in determining whether the bank should be added to the OCC's fair lending examination list. Regardless of the outcome, the analysis should be documented in Examiner View.

If the bank is selected for a fair lending examination through the screening process or if the supervisory office determines that the bank should be added to the fair lending examination list, the supervisory office should update the bank strategy to address the areas of focus. The supervisory office may consider requesting that a compliance specialist assist or conduct the examination.

1. Review findings from objective 1 and identify higher-risk areas for fair lending. (Refer to quantity of risk and quality of risk management indicators in the "Other Risks" section of this booklet).

2. If the bank has performed a fair lending self-evaluation, review the results. Refer to appendix H, "Using Self-Tests and Self-Evaluations to Streamline the Examination," in the "Fair Lending" booklet of the *Comptroller's Handbook.*

3. Considering the high-risk factors present, consult with and obtain approval from the EIC and ADC before determining whether the bank should be added to the fair lending examination list and whether a fair lending examination should be initiated. Examiners and the supervisory office should also consult with the assigned OCC compliance officer when determining whether to add the bank to the fair lending examination list and

[49] Refer to 12 USC 2801 et seq., "Home Mortgage Disclosure," and 12 CFR 1003, "Home Mortgage Disclosure (Regulation C)." (Footnote added in version 1.1)

whether a fair lending examination should be initiated. If a fair lending examination is to be initiated during this supervisory activity, use selected procedures from the "Fair Lending" booklet of the *Comptroller's Handbook* to conduct the examination.

If the bank's total assets are over $10 billion, examiners must consider the bifurcated authorities of the OCC and CFPB. For more information, refer to the "Bank Supervision Process" and "Compliance Management Systems" booklets of the *Comptroller's Handbook*. (Updated in version 1.1)

Violations of the Fair Housing Act[50] may require notification to the U.S. Department of Housing and Urban Development. Violations of the Equal Credit Opportunity Act[51] or the Fair Housing Act that are the result of a pattern or practice require referral to the U.S. Department of Justice. If these conditions are identified, discuss with the ADC and the appropriate OCC compliance officer. (Updated in version 1.1)

Objective 3: Assess the bank's compliance with consumer protection-related lending laws and regulations. If the examiner, after completing these procedures, identifies other areas of high consumer compliance risk that require further review, consult with the appropriate OCC compliance officer and refer to the relevant booklets in the *Consumer Compliance* series of the *Comptroller's Handbook* for more information. (Updated in version 1.1)

1. Consider findings from objective 1 and identify higher-risk areas in consumer protection-related lending laws and regulations. (Refer to quantity of risk and quality of risk management indicators in the "Other Risks" section of this booklet.)

2. Assess the bank's compliance with the FDPA. Examiners must assess the bank's compliance with the FDPA every supervisory cycle, if the bank is an insured depository institution (refer to 12 USC 1820(i)). At a minimum, examiners must perform transaction testing once during every three supervisory cycles.

   If the bank's lending area contains a participating community and has special flood hazard areas, determine whether the bank has internal systems in place to comply with national flood insurance program requirements, including notifying borrowers, obtaining flood insurance at loan origination, maintaining flood insurance throughout the life of the loan, escrowing flood insurance premiums, and force placing insurance as required.

   Select a sample of residential and commercial real estate loans in special flood hazard areas for testing, if necessary. The testing should include a review of the standard flood hazard determination forms, borrower notification, amount of coverage and, as necessary, the bank establishing escrow accounts for flood insurance premiums.

[50] Refer to 42 USC 3601 et seq., "Fair Housing."

[51] Refer to 15 USC 1691 et seq., "Equal Credit Opportunity," and 12 CFR 1002, "Equal Credit Opportunity Act (Regulation B)."

For more information, refer to the "Interagency Flood Disaster Protection Act Examination Procedures" (see OCC Bulletin 2019-42) and 12 CFR 22, "Loans in Areas Having Special Flood Hazards." (Updated in version 1.1)

3. Based on the assessment of the bank's SCRA compliance risk performed in the "minimum objective," assess the bank's compliance with the SCRA by conducting a risk-based SCRA examination that includes transaction testing. For more information, refer to the "Servicemembers Civil Relief Act of 2003" booklet of the *Comptroller's Handbook*.

4. If the bank actively markets to new customers by offering alternative delivery channels or internet banking, or engages in widespread advertising, determine whether the bank has adequate internal controls and trained staff to handle these delivery channels. Determine whether all advertisements and marketing programs are reviewed and approved by the bank's compliance officer for compliance with applicable laws and regulations (e.g., the Truth in Lending Act (TILA),[52] and for the potential for unfair or deceptive acts and practices (UDAP) and unfair, deceptive, or abusive acts and practices (UDAAP) concerns).

5. If the bank offers complex loan products or the bank's products change frequently, determine whether the bank has adequate systems and knowledgeable personnel to monitor for compliance with applicable laws and regulations, such as the Real Estate Settlement Procedures Act (RESPA),[53] TILA, and the Homeowners Protection Act (HPA),[54] and for potential UDAP and UDAAP concerns.

6. If the bank uses third-party loan originators or brokers to make or purchase loans, determine whether the bank engages in appropriate third-party risk management. Refer to OCC Bulletin 2013-29 and OCC Bulletin 2017-21.

7. If the bank offers nontraditional or subprime mortgage products, determine whether the bank has

   - implemented adequate control systems for compliance with consumer protection-related laws and regulations.
   - taken appropriate measures to avoid UDAP and UDAAP.

   For more information, refer to OCC Bulletin 2007-26, "Subprime Mortgage Lending: Statement on Subprime Mortgage Lending"; OCC Bulletin 2006-41, "Nontraditional Mortgage Products: Guidance on Nontraditional Mortgage Product Risks"; and OCC Bulletin 2001-6, "Subprime Lending: Expanded Guidance for Subprime Lending Programs."

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[52] Refer to 15 USC 1601 et seq., "Consumer Credit Cost Disclosure," and 12 CFR 1026, "Truth in Lending (Regulation Z)." (Footnote added in version 1.1)

[53] Refer to 12 USC 2601 et seq., "Real Estate Settlement Procedures," and 12 CFR 1024, "Real Estate Settlement Procedures Act (Regulation X)." (Footnote added in version 1.1)

[54] Refer to 12 USC 4901 et seq., "Homeowners Protection." (Footnote added in version 1.1)

8. If the bank has a broker relationship and either pays or receives a high amount of fees, verify that the disclosure and charging of fees comply with applicable laws and regulations such as TILA and RESPA.

9. If the bank offers or extends consumer credit to covered members of the armed forces or their dependents, determine whether the bank has appropriate controls in place to comply with Military Lending Act[55] (MLA) requirements including the military annual percentage rate (MAPR), written and oral disclosures, and certain transaction and loan terms limitations. Refer to the "Military Lending Act" booklet of the *Comptroller's Handbook.*

Objective 4: Determine the bank's compliance with consumer protection-related deposit laws and regulations. If the examiner, after completing these procedures, identifies other areas of high consumer compliance risk that require further review, consult with the appropriate OCC compliance officer and the relevant *Consumer Compliance* booklets of the *Comptroller's Handbook* for more information.

1. Review findings from objective 1 and identify higher-risk areas in consumer deposit regulations. (Refer to quantity of risk and quality of risk management indicators in the "Other Risks" section of this booklet.)

2. If the bank actively markets to new customers by offering alternative delivery channels (e.g., Internet banking) and widespread advertising, determine whether the bank has adequate internal controls and trained staff to handle these delivery channels. Determine whether all advertisements and marketing programs are reviewed and approved by the bank's compliance officer for compliance with all applicable laws and regulations, such as the Truth in Savings Act[56] (TISA), and for potential UDAP and UDAAP concerns.

3. Determine whether the bank has trained staff and adequate procedures to comply with requirements of the Electronic Fund Transfer Act[57] (EFTA), such as handling unauthorized transactions and errors reported by customers, and requirements pertaining to overdraft services. For more information, refer to the "Electronic Fund Transfer Act" booklet of the *Comptroller's Handbook;* OCC Bulletin 2010-15, "Overdraft Protection: Opt-In Requirements and Related Marketing Issues"; and OCC Bulletin 2005-9, "Overdraft Protection Programs: Interagency Guidance."

4. Determine whether the bank has adequate systems and knowledgeable personnel to comply with TISA requirements, such as calculating and disclosing annual percentage yields.

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[55] Refer to 10 USC 987, "Terms of Consumer Credit Extended to Members and Dependents: Limitations." (Footnote added in version 1.1)

[56] Refer to 12 USC 4301 et seq., "Truth in Savings," and 12 CFR 1030, "Truth In Savings (Regulation DD)." (Footnote added in version 1.1)

[57] Refer to 15 USC 1693 et seq., "Electronic Fund Transfers," and 12 CFR 1005, "Electronic Fund Transfers (Regulation E)." (Footnote added in version 1.1)

5. Determine whether the bank has adequate systems and knowledgeable personnel to comply with check hold requirements of the Expedited Funds Availability Act[58] (Regulation CC), such as funds availability timing, disclosures, and employee training.

Objective 5: Determine the bank's compliance with other consumer protection-related laws and regulations. If the examiner, after completing these procedures, identifies other areas of high consumer compliance risk that require further review, consult with the appropriate OCC compliance officer and the relevant *Consumer Compliance* booklets of the *Comptroller's Handbook* for more information. (Updated in version 1.1)

1. Review findings from objective 1, and identify higher-risk areas in other consumer protection-related laws and regulations. (Refer to quantity of risk and quality of risk management indicators in the "Other Risks" section of this booklet.)

2. If the bank discloses information to nonaffiliated third parties (outside the statutory exceptions), determine whether the bank has adequate systems for providing customers a clear, conspicuous opt-out notice when required. For more information, refer to the "Privacy of Consumer Financial Information" booklet of the *Comptroller's Handbook*.

3. If the bank receives requests from government agencies for customer's financial records, determine whether the bank has adequate procedures for compliance with the Right to Financial Privacy Act (refer to 12 USC 3401 et seq., "Right to Financial Privacy"). (Updated in version 1.1)

4. If the bank uses prescreened lists for solicitation purposes, verify that the bank uses the same criteria to evaluate the application that it used to prescreen the applicant and that record retention requirements are maintained. Refer to the "Fair Credit Reporting" booklet of the *Comptroller's Handbook* and the Equal Credit Opportunity Act information within the "Fair Lending" booklet of the *Comptroller's Handbook*.

5. If the bank operates a website that collects information from, or is directed to, children younger than 13, determine whether the bank has adequate procedures and trained personnel regarding compliance with the requirements of the Children's Online Privacy Protection Act (COPPA) (refer to 15 USC 6501 et seq., "Children's On-Line Privacy Protection"). For more information, refer to the "Other Consumer Protection Laws and Regulations" booklet of the *Comptroller's Handbook*. (Updated in version 1.1)

6. If the bank acts as a "debt collector," determine whether there is bank staff responsible for ensuring that the bank complies with the Fair Debt Collection Practices Act (refer to 15 USC 1692 et seq., "Debt Collection Practices"). (Updated in version 1.1)

[58] Refer to 12 USC 4001 et seq., "Expedited Funds Availability," and 12 CFR 229, "Availability of Funds and Collection of Checks (Regulation CC)." (Footnote added in version 1.1)

Objective 6: Assess the bank's CMS as it pertains to consumer compliance. For more information, refer to the "Compliance Management Systems" booklet of the *Comptroller's Handbook*.

1. Assess the adequacy of bank management and board oversight of consumer compliance. Consider the following:

   - Is there sufficient compliance staffing with the requisite knowledge and expertise, relative to the bank's size, complexity, and risk profile?
   - Does the compliance officer have the necessary resources and authority to effectively carry out his or her responsibilities?
   - Does bank management comprehend, identify, and manage consumer compliance risks arising from the bank's products, services, or activities?
   - Does bank management sufficiently self-identify and self-correct consumer compliance issues?
   - Does the board engage in appropriate oversight over consumer compliance?

2. Assess the adequacy of the bank's consumer compliance program. Consider whether

   - policies and procedures cover all applicable consumer compliance-related laws and regulations and are appropriate for the complexity and risk in the bank's products, services, and activities, including an appropriate third-party risk management process.
   - consumer compliance training is current and tailored to risk and staff responsibilities. Consider the following:
     – Do employees receive appropriate consumer compliance training relative to their job responsibilities?
     – Is appropriate monitoring in place to determine whether employees complete required training?
     – How are employees held accountable for completing training in a timely manner?
     – Does the board and management receive appropriate training, including higher-level training that focuses on the board's and management's individual responsibilities to oversee and govern the bank's consumer compliance function?
   - monitoring and audit encompasses consumer compliance risks throughout the bank.
   - the bank's consumer complaint process is responsive and effective. Communicate findings and conclusions to other examining staff, as appropriate (e.g., asset management examiner). Consider the following:
     – Does the bank track complaints?
     – Do the bank's complaint-related policies and procedures address how various complaints are documented and tracked?
     – Is the bank's complaint resolution process centralized or decentralized?
     – Does the bank's process consider complaints across all products and services, business units, and affiliates, and from all channels (e.g., in-person, telephone, email, litigation, regulatory, and social media)?
     – Does the bank's process include monitoring and analyzing complaints received about and by its third-parties?

3. Assess the adequacy of the compliance monitoring and testing function, including internal audit. Coordinate with the examiner performing the Internal Controls and Audit section of the core assessment and determine whether a review of audit work papers is necessary. Consider

   - the frequency and scope and transaction sampling methodology.
   - qualifications of staff responsible for monitoring and testing.
   - the adequacy of reporting findings to the board and bank management.
   - whether findings include a root cause determination and are corrected appropriately and in a timely manner.

Objective 7: Using the findings from meeting the foregoing objectives, determine whether the bank's risk exposure from consumer compliance is significant.

Develop preliminary assessments of quantity of compliance risk, quality of compliance risk management, aggregate compliance risk, and direction of compliance risk. Refer to the "Risk Assessment System" section of this booklet. Comment as necessary.

Objective 8: Determine whether to expand the procedures or develop a plan for corrective action. Consider whether

- bank management can adequately manage the bank's risks.
- bank management can correct fundamental problems.
- to propose a strategy to address identified weaknesses and discuss strategy with the supervisory office.

Refer to the *Consumer Compliance* series of booklets of the *Comptroller's Handbook* for expanded procedures.

Objective 9: Conclude the consumer compliance review.

1. Provide and discuss with bank management a list of deficiencies and violations.

2. Consult with the EIC and ADC to determine whether to recommend CMPs or an enforcement action (refer to the "Enforcement Actions" section of the "Bank Supervision Process" booklet).

3. Consult with the EIC and other examining staff to identify and communicate to other examiners conclusions and findings from the consumer compliance review that are relevant to other areas being reviewed.

4. Use results of the foregoing procedures and other examination findings to compose comments (e.g., compliance, MRAs, and violation write-ups) for the ROE or other supervisory communication.

5. Update, organize, and reference work papers in accordance with OCC policy. Update Examiner View (e.g., ratings, core knowledge, MRAs, and violations). (Updated in version 1.1)

6. In discussion with the EIC, provide preliminary conclusions about the following:

   - Quantity of compliance risk as it relates to consumer compliance.
   - Quality of risk management, as it relates to consumer compliance.
   - Aggregate level and direction of compliance, operational, and reputation risk, or other risks, as they relate to consumer compliance. Complete the summary conclusions in the "Community Bank Risk Assessment" section of this booklet.
   - Supervisory strategy recommendations.

   Compliance risk is not limited to risk from failure to comply with consumer protection-related laws and regulations; it encompasses the risk of noncompliance with *all* laws and regulations, as well as prudent ethical standards and contractual obligations. It also includes the exposure to litigation (known as legal risk) from all aspects of banking, traditional and nontraditional. Therefore, the examiner generally provides the EIC with conclusions regarding the compliance RAS as it relates to consumer compliance to incorporate into the compliance RAS.

Examination Conclusions and Closing

Conclusion: Bank is composite rated (1, 2, 3, 4, or 5).
Bank's overall risk profile is (low, moderate, or high).

Introduction

To conclude the supervisory cycle, examiners must meet all objectives under this section, regardless of the bank's risk designation.

Objectives and Procedures

Objective 1: Determine and update the bank's composite rating and other regulatory ratings.

1. Consider findings from the following areas:

    - Internal controls and audit
    - Capital adequacy
    - Asset quality
    - Management and board oversight
    - Earnings
    - Liquidity
    - Sensitivity to market risk
    - IT
    - Asset management
    - Compliance with BSA/AML/OFAC laws and regulations
    - Consumer compliance
    - Performance under the CRA

2. Verify that the evaluation of all component ratings has considered the following items as outlined in the interagency rating systems:

    - The bank's size
    - The bank's sophistication
    - Nature and complexity of bank activities
    - The bank's risk profile

    Although regulatory ratings are judgments of the bank's financial, managerial, operational, and compliance performance, descriptions of each component contain explicit language emphasizing bank management's ability to manage risk. Therefore, the conclusions drawn in the RAS should be considered when assigning the corresponding component and the composite rating.

Objective 2: Determine the risk profile using the RAS.

Draw and record conclusions about quantity of risk, quality of risk management, aggregate risk, and the direction of risk for each of the applicable risk categories. Refer to the "Community Bank Risk Assessment" section of this booklet for more information on assessing aggregate risk.

Risk Assessment Summary				
Risk category	**Quantity of risk**	**Quality of risk management**	**Aggregate level of risk**	**Direction of risk**
	(Low, moderate, high)	(Weak, insufficient, satisfactory, strong)	(Low, moderate, high)	(Increasing, stable, decreasing)
Credit				
Interest rate				
Liquidity				
Price				
Operational				
Compliance				
Strategic				
Reputation				

Using the assessments made of the eight individual risks, the examiner can establish the bank's overall risk profile. The overall risk profile is not an average, but a combination of the assessments of the eight individual risks. In establishing the overall risk profile, examiners use judgment to weigh the eight risks by the relative importance of each risk.

Objective 3: Finalize the examination.

At a minimum, the ROE examination conclusions and comments should include the following:

- Summary of scope and major examination objectives, including
  - recap of significant supervisory activities during the examination cycle and how those activities were used to evaluate the bank's overall condition.
  - discussions of significant expansion of the standard core assessment.
- Statements of the bank's overall condition and conclusions on ratings.
- Discussions of excessive risks or deficient risk management practices and their root causes.
- Summary of actions and commitments to correct supervisory concerns and planned supervisory follow-up.
- Notice to the board if CMP referrals are being made.

- Statement about applicable section 914 (12 USC 1831i and 12 CFR 5.51) requirements. For more information, refer to the “Changes in Directors and Senior Executive Officers” booklet of the *Comptroller’s Licensing Manual*. (Updated in version 1.1)

1. The EIC, or designee, should finalize required ROE comments. The comments should include significant risk-related concerns. Refer to the “Report of Examination” section of the “Bank Supervision Process” booklet for a detailed summary on requirements for the content of the ROE.

2. In consultation with key examining staff, the EIC should determine whether there are deficient practices, and communicate the OCC’s concern with the bank’s deficient practices as MRAs in the ROE. MRAs are necessary when bank practices

   - deviate from sound governance, internal control, or risk management principles, and have the potential to adversely affect the bank’s condition, including its financial performance or risk profile, if not addressed.
   - result in substantive noncompliance with laws and regulations, enforcement actions, or conditions imposed in writing in connection with the approval of any application or other request by the bank.

3. Discuss examination conclusions and review required draft comments with the ADC or the appropriate supervisory office official.

4. Summarize examination conclusions and the bank’s condition in the “Examination Conclusions and Comments” page of the report.

5. If any component area is rated 3 or worse, or if the risk profile causes sufficient concern, the EIC should contact the supervisory office before the exit meeting to develop a strategy for addressing the bank’s deficiencies.

6. Hold an on-site exit meeting with bank management to summarize examination findings:

   - Inform bank management of areas of strengths as well as weaknesses.
   - Solicit bank management’s commitment to correct material weaknesses.
   - Discuss the bank’s risk profile, including conclusions from the RAS.
   - Offer examples of acceptable solutions.

7. Provide bank management with an approved draft of examination conclusions, MRA comments, and violations write-ups to allow managers to review the comments for accuracy.

8. Perform a final technical check to make sure that the ROE is accurate and consistent with OCC requirements. The check should determine whether

   - ROE meets established guidelines.
   - comments support all regulatory ratings, as applicable.

- numerical totals are accurate.
- numerical data in the report and other supervisory comments are consistent with the bank's records.
- violations of laws and regulations are cited accurately.

For more information, refer to the "Report of Examination" section of the "Bank Supervision Process" booklet of the *Comptroller's Handbook*.

9. If there are MRA comments in the report, they should provide specific information regarding

   - the concern.
   - the root cause of the concern and contributing factors.
   - potential consequence or effects on the bank from inaction.
   - supervisory expectations for corrective action.
   - bank management's commitment to corrective action and the time frame and person responsible for corrective action.

10. Report OFAC-related MRAs or suspected OFAC violations to the Compliance Risk Policy Division of the OCC's Bank Supervision Policy department. (Updated in version 1.1)

11. Verify that all appropriate information, including updates to core knowledge and other pertinent areas, has been entered in Examiner View and approve the examination.

12. Update the supervisory strategy for the next supervisory cycle. Refer to the "Planning" section of this booklet and in the "Bank Supervision Process" booklet of the *Comptroller's Handbook.* (Updated in version 1.1)

13. Complete and distribute assignment evaluations.

14. Schedule the board meeting.

Objective 4: Prepare for and conduct a meeting with the board.

1. Before completing the supervisory cycle, prepare for the meeting by

   - drafting a preliminary agenda (formal or informal).
   - preparing handouts, graphics, or audiovisual material for the meeting.
   - reviewing the backgrounds of all board members.
   - drafting responses to expected questions and comments.

2. Conduct the meeting after the board, or an authorized committee, has had the opportunity to review the draft report or a synopsis of examination findings. At the meeting, provide graphics and handouts to describe the following:

- Objectives of the OCC's supervision and how the OCC pursues those objectives.
- Strategic issues, including growth, products, and strategies.
- Major concerns or issues, including significant risks facing the bank.
- The bank's success or failure in correcting previously identified concerns.
- Potential impact of failing to correct concerns.
- What the OCC expects the bank to do and when (e.g., action plans, supervisory strategies, and commitments).
- What the bank is doing well.
- Industry issues affecting the bank.

During the supervisory cycle, the ADC must attend at least one board meeting or an examination exit meeting that includes board member participation.

3. Document details of the meeting in Examiner View as a significant event. Include the following information:

- Date and location of the meeting and names of attendees.
- Major items discussed.
- Brief summary of the directors' reactions to the OCC briefing. (The entry documenting the meeting can refer the reader to the follow-up analysis comment for further details on commitments obtained from the board or senior management.)

Community Bank Risk Assessment System

Credit Risk

Credit risk is the risk to current or projected financial condition and resilience arising from an obligor's failure to meet the terms of any contract with the bank or otherwise perform as agreed. Credit risk is found in all activities in which settlement or repayment depends on counterparty, issuer, or borrower performance. Credit risk exists any time bank funds are extended, committed, invested, or otherwise exposed through actual or implied contractual agreements, whether reflected on or off the balance sheet.

Credit risk is the most recognizable risk associated with banking. This definition encompasses more than the traditional definition associated with lending activities. Credit risk also arises in conjunction with a broad range of bank activities, including selecting investment portfolio products, derivatives trading partners, or foreign exchange counterparties. Credit risk also arises due to country or sovereign exposure, as well as indirectly through guarantor performance.

Examiners should consider both the quantity of credit risk and the quality of credit risk management to derive the aggregate and direction of credit risk.

Summary Conclusions

	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
Credit risk summary conclusions	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of Credit Risk

Quantity of credit risk is derived from the absolute amount of credit exposure and the quality of that exposure. How much credit exposure a bank has is a function of the following:

- Level of loans and other credit or credit-equivalent exposures relative to total assets and capital.
- Extent to which earnings are dependent on loan or other credit or credit-equivalent income sources.

All else being equal, banks that have higher loans-to-assets and loans-to-equity ratios and that depend heavily on the revenues from credit activities have a higher level of credit risk. The degree of exposure is a function of the risk of default and risk of loss in assets and exposures composing the credit exposure. The risk of default and loss, however, is not always apparent from currently identified problem assets. It also includes potential default and loss that are affected by such factors as bank risk selection and underwriting practices; portfolio composition; concentrations; portfolio performance; and global, national, and local economic and business conditions. All credit activities should be considered, including off-balance-sheet exposures, loans held for sale, and credit risk in the investment portfolio.

An assessment of low, moderate, or high credit risk should reflect the bank's standing relative to existing financial risk benchmarks or peer or historical standards and should take into consideration relevant trends in risk direction. When considering the effect of trends on quantity of risk, examiners must consider the rate of change as well as the base level of risk from which the change occurs. (For example, a modest adverse trend in a bank with a moderate quantity of credit risk should weigh more heavily on the examiner's decision to change the quantity of risk rating than a modest adverse trend in a low-risk bank.) These factors represent minimum standards, and examiners should consider additional factors.

To determine the quantity of credit risk, examiners consider an array of quantitative and qualitative risk measurements. These indicators can be leading (rapid growth), lagging (high past-due levels), static (point-in-time evaluation/gauge), relative (exceeds peer/historical norms), or dynamic (trend or change in portfolio mix). Many of these indicators are readily available from internal reports as well as call report and UBPR information. Other indicators, such as a bank's risk appetite or underwriting practices, while more subjective, should also be considered. (Updated in version 1.1)

It is extremely important to note that banks can exhibit increasing or high levels of credit risk even though many or all traditional lagging indicators or asset quality indicators are low. Although qualitative and quantitative indicators may have opposite effects on credit risk (the one may mitigate the other's effect), the indicators may also work together (the one may add to the other's effect). Although each type of measure can provide valuable insights about risk when viewed individually, they become much more powerful for assessing the quantity of risk when viewed together.

Quantity of Credit Risk Indicators

Examiners should use the following indicators when assessing quantity of credit risk.

Quantity of Credit Risk Indicators		
Low	**Moderate**	**High**
The level of loans outstanding is low relative to total assets and equity capital.	The level of loans outstanding is moderate relative to total assets and equity capital.	The level of loans outstanding is high relative to total assets and equity capital.
Growth rates are supported by local, regional, and/or national economic and demographic trends and level of competition. Growth (including off-balance-sheet activities) has been planned for and appears consistent with management and	Growth rates exceed local, regional, and/or national economic and demographic trends and level of competition. Some growth (including off-balance-sheet activities) has not been planned for or exceeds planned levels and may test management and staff	Growth rates significantly exceed local, regional, and/or national economic and demographic trends and level of competition. Growth (including off-balance-sheet activities) was not planned for or exceeds planned levels, and stretches management and staff expertise and/or operational

Quantity of Credit Risk Indicators		
Low	**Moderate**	**High**
staff expertise and/or operational capabilities.	expertise or operational capabilities.	capabilities. Growth may be in new products or with out-of-area borrowers.
The bank has well-diversified income, and dependence on interest and fees from loans and leases is commensurate with asset mix. Loan yields are low and risks/returns are well balanced.	The bank is dependent on interest and fees from loans for the majority of its income, but income sources within the loan portfolio are diversified. Loan yields are moderate. Imbalances between risk and return may exist but are not significant.	The bank is highly dependent on interest and fees from loans and leases. Bank may target higher-risk loan products for their earnings potential. Loan income is highly vulnerable to cyclical trends. Loan yields are high and reflect an imbalance between risk and return, and/or risk is disproportionately high relative to return.
The bank's portfolio is well diversified with no single large concentrations and/or a few moderate concentrations. Concentrations are well within internal limits. Change in portfolio mix is neutral or reduces overall risk profile.	The bank has one or two material concentrations. Concentrations are in compliance with internal guidelines but may be approaching the limits. Change in portfolio mix may increase overall risk profile.	The bank has one or more large concentrations. Concentrations may have exceeded internal limits. Change in portfolio mix significantly increases overall risk profile.
Existing and/or new extensions of credit reflect conservative underwriting and risk-selection standards. Policies are conservative, and exceptions are nominal.	Existing and/or new extensions of credit generally reflect conservative to moderate underwriting and risk-selection standards. Policies and exceptions are moderate.	Existing and/or new extensions of credit reflect liberal underwriting and risk-selection standards. Policies either allow such practices or practices have resulted in a large number of exceptions.
Underwriting policies are reasonable. Underwriting standards for loans held for sale or originated to distribute are reasonable and consistent with loans made with the intention of being held for the bank's portfolio. The bank has only occasional loans with structural weaknesses and/or underwriting exceptions. Those loans are well mitigated and do not constitute an undue risk.	Underwriting policies are satisfactory. Underwriting standards for loans held for sale or originated to distribute are reasonable but are inconsistent with loans made with the intention of being held for the bank's portfolio. The bank has an average level of loans with structural weaknesses and/or exceptions to sound underwriting standards consistent with balancing competitive pressures and reasonable growth objectives.	Underwriting policies are inadequate. Underwriting standards for loans held for sale or originated to distribute are inconsistent with loans made with the intention of being held for the bank's portfolio. The bank has a high level of loans with structural weaknesses and/or underwriting exceptions that expose the bank to heightened loss in the event of default.
Collateral requirements are conservative. Collateral valuations are timely and well supported.	Collateral requirements are acceptable. Bank practices result in moderate deviations from policy. A moderate number of collateral valuations are not well supported or reflect inadequate protection. Soft (intangible) collateral is sometimes used in lieu of hard (tangible) collateral.	Collateral requirements are liberal, or if policies incorporate conservative requirements, there are substantial deviations. Collateral valuations are not always obtained, are frequently unsupported, and/or reflect inadequate protection. Soft (intangible) collateral is frequently used rather than hard (tangible) collateral.
The level of loan documentation and/or collateral exceptions is	The level of loan documentation and/or collateral exceptions is	The level of loan documentation and/or collateral exceptions is high.

Quantity of Credit Risk Indicators		
Low	**Moderate**	**High**
low and has minimal impact on risk of loss.	moderate, but exceptions are corrected in a timely manner and generally do not expose the bank to risk of loss.	Exceptions are outstanding for inordinate periods, and the bank may be exposed to heightened risk of loss.
Distribution across pass categories is consistent with a conservative risk appetite. Migration trends within the pass category are balanced or favor the higher or less risky ratings. Lagging indicators, such as past dues and nonaccruals, are low, and the trend is stable.	Distribution across pass categories is consistent with a moderate risk appetite. Migration trends within the pass category are starting to favor the lower or riskier pass ratings. Lagging indicators, such as past dues and nonaccruals, are moderate, and the trend is stable or rising slightly.	Distribution across pass categories is heavily skewed toward the lower or riskier pass ratings. Downgrades dominate rating changes within the pass category. Lagging indicators, such as past dues and nonaccruals, are moderate or high, and the trend is rising.
Classified and special mention loans represent a low percentage of loans and capital and are not skewed to the more severe categories (doubtful or loss).	Classified and special mention loans represent a moderate percentage of loans and capital and are not skewed to the more severe categories (doubtful or loss).	Classified and special mention loans represent a high percentage of loans and capital or a moderate percentage of loans and capital and are growing or are skewed to the more severe categories (doubtful or loss).
Bank re-aging, extension, renewal, and refinancing practices raise little or no concern about the accuracy/transparency of reported problem loan, past due, nonperforming, and loss numbers.	Bank re-aging, extension, renewal, and refinancing practices raise some concern about the accuracy/transparency of reported problem loan, past due, nonperforming, and loss numbers.	Bank re-aging, extension, renewal, and refinancing practices raise substantial concern about the accuracy/transparency of reported problem loan, past due, nonperforming, and loss numbers.
Loan losses to total loans are low. ALLL coverage of problem and noncurrent loans and loan losses is high. Provision expense is stable.	Loan losses to total loans are moderate. ALLL coverage of problem and noncurrent loans is moderate, but provision expense may need to be increased.	Loan losses to total loans are high. ALLL coverage of problem and noncurrent loans is low. Special provisions may be needed to maintain acceptable coverage.

Quality of Credit Risk Management Indicators

Examiners should use the following indicators when assessing quality of credit risk management. (For comprehensive guidelines on portfolio management, refer to the “Loan Portfolio Management” booklet of the *Comptroller’s Handbook* (national banks) and *OTS Examination Handbook* section 201, “Overview: Lending Operations and Portfolio Risk Management” (FSAs).) (Updated in version 1.1)

Quality of Credit Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
There is a clear, sound credit culture. Board and management risk appetite is well communicated and fully understood.	The credit culture is generally sound but may vary by product line or business unit. Risk appetite may not be clearly communicated	Credit culture may not be well understood. Risk appetite may be inconsistent with strategic goals or not uniformly communicated	Credit culture is absent or is materially flawed. Risk appetite may not be well understood.

Quality of Credit Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
	throughout the institution.	throughout the institution.	
Strategic and/or business plans are consistent with risk appetite and promote an appropriate balance between risk-taking and growth and earnings objectives. New loan products/initiatives are well researched, tested, and approved before implementation.	Strategic and/or business plans are consistent with risk appetite. Anxiety for income may lead to some higher-risk transactions. Generally, there is an appropriate balance between risk-taking and growth and earnings objectives. New loan products/initiatives may be launched with some limited testing and risk analysis. This analysis is likely not robust but is sufficient to quantify the potential risk.	Strategic and/or business plans are not fully consistent with risk appetite. Anxiety for income may lead to some higher-risk transactions that may not be well understood. There are concerns between risk-taking and growth and earnings objectives. New loan products/initiatives may be launched without sufficient testing and risk analysis.	Strategic and/or business plans are inconsistent with risk appetite or may encourage taking on excessive levels of risk. Anxiety for income dominates planning activities. The bank engages in new loan products/initiatives without conducting sufficient due diligence testing.
Management is effective. Loan management and personnel possess extensive expertise to effectively administer the risk assumed. Responsibilities and accountability are clear and appropriate, and timely remedial or corrective action is taken when they are breached.	Management is adequate to administer assumed risk, but improvements may be needed in one or more areas. Loan management and personnel generally possess the expertise required to effectively administer assumed risks, but additional expertise may be required in one or more areas. Responsibilities and accountability may require some clarification. Generally, appropriate remedial or corrective action is taken to address the root causes of problems.	Management requires improvement and strengthening in one or more key areas. Responsibilities and accountability likely require some clarification or do not reflect the bank's current structure. Management may take remedial or corrective actions to address root causes of problems, but these actions are not always effective or timely.	Management is deficient. Loan management and personnel may not possess sufficient expertise and/or experience, or otherwise may demonstrate an unwillingness to effectively administer the risk assumed. Responsibilities and accountability are not clear. Remedial or corrective actions are lacking or do not address root causes of problems.
Diversification management is active and effective. Concentration limits are set at reasonable levels. The bank identifies and reports concentrated exposures and initiates actions to limit, reduce or otherwise mitigate their risk. Management identifies and	Diversification management is adequate. Concentrated exposures are identified and reported. Management has set reasonable concentration limits, but these limits may require minor enhancements or further stratification. Management generally takes action to limit,	Diversification management needs improvement. Management has set concentration limits, but these limits may not be reasonable, are outdated, or may not adequately address the primary exposures at the bank. Management may identify when the bank exceeds these limits but	Diversification management is deficient or altogether absent. The bank takes little or no action to limit, reduce, or mitigate risk. Management does not understand exposure correlations. Concentration limits, if any, may be exceeded or are raised frequently.

Quality of Credit Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
understands correlated exposure risks.	reduce, or otherwise mitigate risk. Correlated exposures are understood but may not be formally discussed or well documented.	does not always take appropriate or timely actions to reduce or mitigate risk when limits are exceeded. Correlated exposures are not well understood or clearly identified.	
Loan management and personnel compensation structures provide appropriate balance among loan/revenue production, loan quality, and portfolio administration, including risk identification.	Loan management and personnel compensation structures provide reasonable balance among loan/revenue production, loan quality, and portfolio administration.	Loan management and personnel compensation structures may be skewed toward loan/revenue production. There may be inadequate incentives or accountability for loan quality and portfolio administration.	Loan management and personnel compensation structures are skewed to loan/revenue production. There is little evidence of substantive incentives and/or accountability for loan quality and portfolio administration.
Staffing levels and expertise are robust for the size and complexity of the loan portfolio. Staff turnover is reasonable and allows for the orderly transfer of responsibilities. Training programs facilitate ongoing staff development.	Staffing levels and expertise are generally adequate for the size and complexity of the loan portfolio. Staff turnover is moderate, but management addresses gaps in portfolio management timely. Training initiatives are effective but may need minor enhancements.	Staffing levels need improvement. High turnover may result in significant gaps in some areas. Management and the board do not respond to these needs timely. Training initiatives may be present but are likely inconsistent.	Staffing levels are inadequate in numbers or skill level. Turnover is high, and management and the board are ineffective at addressing staffing gaps or shortfalls. Training is lacking or wholly insufficient.
Lending policies effectively establish and communicate portfolio objectives, risk appetite, and loan-underwriting and risk-selection standards.	Policies are fundamentally adequate. Enhancements can be achieved in one or more areas but are generally not critical. Specificity of risk appetite or loan-underwriting and risk-selection standards may need improvement to fully communicate policy requirements.	Credit-related policies require improvement. They may not be sufficiently clear or are too general to adequately communicate portfolio objectives and loan-underwriting and risk appetite or risk-selection standards. Policies may be outdated or do not reflect the board's risk appetite.	Policies are deficient in one or more ways and require significant improvement in several areas. Key policies may be absent or lack basic credit guidance on loan-underwriting criteria, risk appetite, or risk-selection standards.
Bank effectively identifies, approves, tracks, and reports significant policy, underwriting, and risk-selection exceptions individually and in aggregate, including risk exposures associated with off-balance-sheet activities.	Bank identifies, approves, and reports significant policy, underwriting, and risk-selection exceptions on a loan-by-loan basis, including risk exposures associated with off-balance-sheet activities. Little aggregation or trend analysis, however, is conducted to	Bank approves significant policy exceptions but may not report them individually or in aggregate, or may not analyze their effect on portfolio quality. Risk exposures associated with off-balance-sheet activities may not be considered.	Bank does not have an effective process to identify or approve significant policy exceptions. Risk exposures associated with off-balance-sheet activities are not considered or understood.

Quality of Credit Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
	determine the effect on portfolio quality.		
Credit analysis is thorough and timely both at underwriting and periodically thereafter.	Credit analysis appropriately identifies key risks and is conducted within reasonable time frames. Analysis after underwriting is effective but may need minor enhancements.	Credit analysis needs improvement. Moderate errors may be evident, key risks may be overlooked, or analyses may not be consistently timely. Further employee training or assistance is likely required.	Credit analysis is deficient. Analysis is not timely, accurate, or complete and cannot be relied on for underwriting or risk-rating decisions. Employees lack basic knowledge or understanding of how to complete these analyses.
Internal or outsourced risk rating and problem loan review/identification systems are accurate and timely. They effectively stratify credit risk in both problem and pass-rated credits. They serve as an effective early warning tool and support risk-based pricing, ALLL, and capital allocation processes.	Internal or outsourced risk rating and problem loan review/identification systems are effective in identifying problem and emerging problem credits. Examiners or loan review may have identified a small but explainable number of exceptions. The graduation of pass ratings may need to be expanded to facilitate early warning, risk-based pricing, or capital allocation.	Internal or outsourced risk rating and problem loan review/identification systems require improvement. Problem credits may be identified, but not in a timely manner, and exceptions are moderate to high. The graduation of pass ratings is insufficient to stratify risk in pass credits for early warning or other purposes (loan pricing, ALLL, capital allocation).	Internal or outsourced risk rating and problem loan review/identification systems are deficient. The bank does not have an effective system to accurately or timely identify problem credits; as a result, portfolio risk is significantly misstated.
Loan review (either internal or external) is comprehensive, timely, and effective. Loan review identifies underwriting, financial, and collateral exceptions and also evaluates the adequacy of overall credit risk management. Management and personnel are qualified, experienced, and independent, and report directly to the board or its designated committee. Identified issues are resolved timely and effectively. Work papers fully support conclusions.	Loan review (either internal or external) is adequate in scope, timely, and generally effective. Minor weaknesses may be evident. Loan review identifies underwriting, financial, and collateral exceptions but may not evaluate the overall credit risk management function. Management and personnel are qualified, experienced, and independent (whenever possible), and report directly to the board or its designated committee. Identified issues are generally resolved timely and effectively. Work papers adequately support conclusions.	The scope of loan review (either internal or external) may require some expansion to be sufficient, or reviews may not always be timely. Reviews may not consistently identify underwriting, financial, and collateral exceptions and likely do not include an evaluation of overall credit risk management. Management or personnel may lack extensive experience, require further training, or may not be fully independent. Reporting to the board or a designated committee may be indirect. Work papers may not fully support all findings.	The scope of loan review (either internal or external) is inadequate, and reviews are not timely, resulting in excessive lapses in coverage. The bank does not have a system to accurately identify underwriting, financial, or collateral exceptions. Management and personnel lack experience and competence, and independence may be in question. Key issues are not properly reported to the board or designated committee. Work papers are inadequate to support findings.

Quality of Credit Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Special mention ratings do not indicate any management problems administering the loan portfolio.	Special mention ratings generally do not indicate management problems administering the loan portfolio.	Special mention ratings may indicate management problems administering the loan portfolio.	Special mention ratings clearly indicate management is not properly administering the loan portfolio.
MIS provide accurate, timely, and complete portfolio information. Management and the board receive comprehensive reports to analyze and understand the bank's credit risk profile, including off-balance-sheet activities. MIS facilitate exception reporting, and MIS infrastructure can support ad hoc queries in a timely manner.	MIS may require minor improvement in one or more areas, but management and the board generally receive appropriate reports to analyze and understand the bank's credit risk profile. MIS facilitate exception reporting, and MIS infrastructure can support ad hoc queries in a timely manner.	MIS require improvement. Reports may be incomplete or are not consistently produced in a timely fashion. As a result, management and the board may not be receiving complete information to fully analyze and understand the bank's credit risk profile. Exception reporting requires improvement, and MIS infrastructure may not support ad hoc queries in a timely manner.	MIS are deficient, lacks key information, are not timely, or are not reliable due to significant inaccuracies. As a result, management and the board are not receiving accurate or sufficient information to analyze and understand the bank's credit risk profile. The bank lacks exception reporting, and MIS infrastructure does not support ad hoc queries.

Interest Rate Risk

Interest rate risk is the risk to current or projected financial condition and resilience arising from movements in interest rates. Interest rate risk results from differences between the timing of rate changes and the timing of cash flows (repricing risk); from changing rate relationships among different yield curves affecting bank activities (basis risk); from changing rate relationships across the spectrum of maturities (yield curve risk); and from interest-related options embedded in bank products (options risk).

The assessment of interest rate risk should consider risk from both an accounting perspective (i.e., the effect on the bank's accrual earnings) and an economic perspective (i.e., the effect on the market value of the bank's portfolio equity). In some banks, interest rate risk is included in the broader category of market risk. In contrast with price risk, which focuses on the mark-to-market portfolios (e.g., trading accounts), interest rate risk focuses on the value implications for accrual portfolios (e.g., HTM and AFS accounts).

Examiners should consider both the quantity of risk and the quality of risk management to derive the aggregate and direction of IRR.

Summary Conclusions

	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
IRR summary conclusions	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of IRR Indicators

Examiners should use the following indicators when assessing quantity of IRR.

Quantity of IRR Indicators		
Low	**Moderate**	**High**
No significant mismatches on longer-term positions exist. Shorter-term exposures are simple and easily adjusted to control risk.	Mismatches on longer-term positions exist but are manageable and could be effectively hedged.	Re-pricing mismatches are longer-term and may be significant, complex, or difficult to hedge.
Potential exposure to financial performance is negligible under a +/- 200 basis point rate change over a 12-month horizon.	Potential exposure to financial performance is not material under a +/- 200 basis point rate change over a 12-month time horizon.	Potential exposure to financial performance is significant under a +/- 200 basis point rate change over a 12-month time horizon.
There is little or no exposure to multiple indexes that price assets and liabilities, such as prime, Libor, constant maturity Treasury	Potential exposure to multiple indexes that price assets and liabilities, such as prime, Libor,	Potential exposure to multiple indexes that price assets and liabilities, such as prime, Libor,

Quantity of IRR Indicators		
Low	**Moderate**	**High**
(CMT), and cost-of-funds index (COFI).	CMT, and COFI, is reasonable and manageable.	CMT, and COFI, is significant. Positions may be complex.
Potential exposure to changes in the level and shape of the yield curve is absent or negligible.	Potential exposure to changes in the level and shape of the yield curve is not material and is considered manageable.	Potential exposure to changes in the level and shape of the yield curve is significant. Positions may be complex.
Potential exposure to assets and/or liabilities with embedded options is low. Positions are neither material nor complex.	Potential exposure to assets and/or liabilities with embedded options is not material. The impact of exercising options is not projected to adversely affect earnings or capital.	Potential exposure to assets and/or liabilities with embedded options is material. Positions may be complex and the impact of exercising options may adversely affect earnings or capital.
Volume and complexity of servicing assets is either insignificant or nonexistent, presenting virtually no exposure to financial performance from changes in interest rates.	Volume and complexity of servicing assets is relatively modest and does not present material exposure to financial performance from changes in interest rates.	Volume and complexity of servicing assets is material and potentially exposes financial performance to significant exposure from changes in interest rates.
Support provided by low-cost, stable nonmaturity deposits is significant and absorbs or offsets exposure arising from longer-term re-pricing mismatches or options risk.	Support provided by low-cost, stable nonmaturity deposits absorbs some, but not all, of the exposure associated with longer-term re-pricing mismatches or options risk.	Support provided by low-cost, stable nonmaturity deposits is not significant or sufficient to offset risk from longer-term re-pricing mismatches or options risk.

Quality of IRR Management Indicators

Examiners should use the following indicators when assessing quality of IRR management.

Quality of IRR Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Board-approved policies are sound and effectively communicate guidelines for management of IRR, functional responsibilities, and risk appetite.	Board-approved policies adequately communicate guidelines for management of IRR, functional responsibilities, and risk appetite. Minor weaknesses may be evident.	Board-approved policies require improvement. Policies may not reflect current risk appetite and may not clearly communicate guidelines for management of IRR or note specific functional responsibilities.	Board-approved policies are missing or inadequate in communicating guidelines for management of IRR, functional responsibilities, and risk appetite.
Risk-limit structures provide clear risk parameters for risk to earnings and economic value consistent with risk appetite of the board. Limits reflect sound understanding of risk under adverse rate scenarios. The board	Risk-limit structures for earnings and economic value are reasonable and consistent with risk appetite of the board. Management generally takes action to limit, reduce, or otherwise mitigate risk when risk exposure is near or	Risk-limit structures to control risk to earnings and economic value require improvement. Limits may be inconsistent with the board's true risk appetite. Management may or may not identify when the bank exceeds	Risk-limit structures to control risk to earnings and economic value are absent, ineffective, unreasonable, or inconsistent with risk appetite of the board. The board and management take little

Quality of IRR Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
and management are proactive when initiating action to limit, reduce, or otherwise mitigate the bank's risk.	exceeds board-approved limits.	board-approved limits and does not take timely action to reduce or mitigate risk when these limits are exceeded.	or no action to limit, reduce, or mitigate risk.
Management demonstrates a thorough understanding of IRR. Management anticipates and responds proactively and appropriately to adverse conditions or changes in economic conditions. Management identifies and manages risks involved in new products, services, and systems.	Management demonstrates an adequate understanding of IRR and generally responds timely and appropriately to adverse conditions or changes in economic conditions. Management adequately identifies and manages the risks involved in new products, services, and systems.	Management of IRR is reactive, and the board and management may not anticipate or respond appropriately to adverse conditions or changes in economic conditions. Weaknesses are evident in management's ability to identify or manage the risks involved in new products, services, and systems.	Management either does not demonstrate an understanding of IRR or does not anticipate or respond appropriately to adverse conditions or changes in economic conditions. Management does not identify or inadequately identifies and manages the risks involved in new products, services, and systems.
Risk measurement processes are robust given the size and complexity of the bank's on- and off-balance-sheet exposures. Data input processes for the accuracy and integrity of management information are effective. Assumptions are reasonable, regularly reviewed, and well documented. IRR is measured over a wide range of rate movements to identify vulnerabilities and stress points.	Risk measurement processes are appropriate given the size and complexity of the bank's on- and off-balance-sheet exposures. Data input processes for the accuracy and integrity of management information are adequate. Assumptions are reasonable. IRR is measured over an adequate range of rate movements to identify vulnerabilities and stress points. Minor enhancements may be needed.	Risk measurement processes require improvement. Modest weaknesses may exist in data input and interest rate scenario measurement processes. Assumptions may not be reviewed periodically and are not well supported. IRR may only be measured over a limited range of rate movements.	Risk measurement processes are deficient given the size and complexity of the bank's on- and off-balance-sheet exposures. Material weaknesses may exist in data input and interest rate scenario measurement processes. Assumptions may not be realistic, supported, or documented, and are not tailored to the individual bank.
EAR is measured as well as economic value-at-risk when significant longer-term or options risk exposure exists. No weaknesses are evident.	EAR is measured as well as economic value-at-risk when significant longer-term or options risk exposure exists. Minor enhancements may be needed.	EAR may not be appropriately measured. Economic value-at-risk may not be appropriately considered despite significant exposure to longer-term or options risk.	EAR is not appropriately measured. Economic value-at-risk may not be considered despite significant exposure to longer-term or options risk.

Quality of IRR Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
MIS provide timely, accurate, and complete information on IRR to appropriate levels in the bank. No weaknesses are evident.	MIS are adequate and provides complete information on IRR to appropriate levels of management. Minor weaknesses may be evident.	MIS may not be timely or provide complete information on IRR. Weaknesses potentially affect the board's ability to comprehensively identify and measure risk in the bank.	MIS are inadequate, inaccurate, or incomplete. Remedial actions are necessary, as material weaknesses in MIS are evident and materially affect management and the board's ability to identify and measure IRR.
A well-designed, independent, and competent review function has been implemented to periodically validate and test the effectiveness of risk measurement systems. The process assesses the reasonableness and validity of scenarios and assumptions. The system is effective, and no corrective actions are required.	An acceptable review function is in place. The review periodically validates and tests the effectiveness of risk measurement systems, including the reasonableness and validity of scenarios and assumptions. The review is independent and competent. Minor weaknesses may exist but can be easily corrected.	A review function is in place, but it requires enhancement. The review does not sufficiently validate and test the effectiveness of risk measurement systems, including the reasonableness and validity of scenarios and assumptions. The review may not be fully independent, may not occur with enough frequency, or may not be completed by competent staff.	A review function to periodically validate and test the effectiveness of risk measurement systems either does not exist or is inadequate in one or more material respects. The review is not independent or completed by competent staff. Processes to evaluate the reasonableness and validity of rate scenarios and assumptions used are absent or have significant deficiencies.

Liquidity Risk

Liquidity risk is the risk to current or projected financial condition and resilience arising from an inability to meet obligations when they come due. Liquidity risk includes the inability to access funding sources or manage fluctuations in funding levels. Liquidity risk also results from a bank's failure to recognize or address changes in market conditions that affect its ability to liquidate assets quickly and with minimal loss in value.

The nature of liquidity risk has changed in recent years. Increased investment alternatives for retail depositors and sophisticated off-balance-sheet products with complicated cash-flow implications are examples of factors that increase the complexity of liquidity risk.

Examiners should consider both the quantity of risk and the quality of risk management to derive the aggregate and direction of liquidity risk.

Summary Conclusions

	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
Liquidity risk summary conclusions	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of Liquidity Risk Indicators

Examiners should use the following indicators when assessing quantity of liquidity risk.

Quantity of Liquidity Risk Indicators		
Low	**Moderate**	**High**
Funding sources are abundant and provide a competitive cost advantage.	Funding sources are sufficient and provide cost-effective liquidity.	Funding sources and liability structures suggest current or potential difficulty in maintaining long-term and cost-effective liquidity.
Funding is widely diversified. There is little or no reliance on wholesale funding sources or other credit-sensitive funds providers.	Funding is generally diversified, with a few providers that may share common objectives and economic influences but no significant concentrations. Modest reliance on wholesale funding may be evident.	Borrowing sources may be concentrated among a few providers or providers with common investment objectives or economic influences. Significant reliance on wholesale funds is evident.
Market alternatives exceed demand for liquidity with no adverse changes expected.	Market alternatives are available to meet demand for liquidity at reasonable terms, costs, and tenors. Liquidity position is not expected to deteriorate in the near term.	Liquidity needs are increasing, but sources of market alternatives at reasonable terms, costs, and tenors are declining.
Capacity to augment liquidity through asset sales and/or securitization is strong, and the bank has an established record in accessing these markets, even in distressed conditions.	Bank has the potential capacity to augment liquidity through asset sales and/or securitization but has little experience in accessing these markets. Distressed conditions could make this more problematic.	Bank exhibits little capacity or potential to augment liquidity through asset sales or securitization. Lack of experience accessing these markets or unfavorable reputation may make this option questionable, particularly in distressed conditions.
Volume of wholesale liabilities with embedded options is low.	Some wholesale funds contain embedded options, but potential impact is not significant.	Material volumes of wholesale funds contain embedded options. The potential impact is significant.
Bank is not vulnerable to funding difficulties should a material adverse change occur in market perception, even in distressed conditions.	Bank is not excessively vulnerable to funding difficulties should a material adverse change occur in market perception. Distressed conditions could make this more problematic.	Bank's liquidity profile makes it vulnerable to funding difficulties should a material adverse change occur, particularly in distressed conditions.

Quantity of Liquidity Risk Indicators		
Low	**Moderate**	**High**
Parent company provides strong support.	Parent company provides adequate support.	Parent company provides little or unknown support.

Quality of Liquidity Risk Management Indicators

Examiners should use the following indicators when assessing quality of liquidity risk management.

Quality of Liquidity Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Board-approved policies effectively communicate guidelines for liquidity risk management and designate responsibility.	Board-approved policies adequately communicate guidance for liquidity risk management and assign responsibility. Minor weaknesses may be present.	Board-approved policies may not adequately communicate guidance regarding liquidity risk management or appropriately assign responsibility.	Board-approved policies are deficient in one or more material respects and fail to communicate guidance regarding liquidity risk management or assign responsibility.
Liquidity risk management process is effective in identifying, measuring, monitoring, and controlling liquidity risk. The process reflects a sound culture that has proven effective over time.	Liquidity risk management process is generally effective in identifying, measuring, monitoring, and controlling liquidity risk. There may be minor weaknesses given the risks undertaken and complexity of exposures, but these are easily corrected.	Liquidity risk management process may not be adequate in identifying, measuring, monitoring, and controlling liquidity risk. There may be several areas of weakness given the risks undertaken and the complexity of exposures, although these weaknesses can be addressed in a timely manner.	Liquidity risk management process is ineffective in identifying, measuring, monitoring, and controlling liquidity risk. This may hold true in one or more material respects, given the risks undertaken and complexity of exposures.
Management fully understands all aspects of liquidity risk and incorporates all key aspects of liquidity risk into its overall risk management process. Management anticipates and responds well to changing market conditions.	Management reasonably understands the key aspects of liquidity risk and generally incorporates key aspects of liquidity risk into its overall risk management process. Management adequately responds to changes in market conditions.	Management has a marginally adequate understanding of key aspects of liquidity risk and may not adequately incorporate key aspects of liquidity risk into its overall risk management process. Management may not consistently and adequately respond to changes in market conditions.	Management does not understand or chooses to ignore key aspects of liquidity risk. Management does not anticipate or take timely or appropriate actions in response to changes in market conditions.

Quality of Liquidity Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
CFP is well developed, effective, and useful. The plan incorporates reasonable assumptions, scenarios, and crisis management planning and is tailored to the bank's needs. CFP clearly establishes strategies that address liquidity shortfalls in a distressed environment. Stress testing (including bank-specific and market-wide scenarios) is performed and is effective.	CFP is adequate. The plan is current, reasonably addresses most relevant issues, and contains an adequate level of detail, including multiple scenario analysis. The plan may require minor refinement. CFP adequately establishes strategies that address liquidity shortfalls in a distressed environment but may require some minor changes. Stress testing is adequately performed but may require some enhancement.	CFP may need improvement because it may not be sufficiently current, may not reasonably address most relevant issues, may lack sufficient detail or scenario analyses, or may not adequately establish strategies addressing liquidity shortfalls in a stressed environment. Stress testing needs improvement.	CFP is inadequate or nonexistent. Plan may exist but is not tailored to the institution, is not realistic, or is not properly implemented. The plan may not consider cost-effectiveness or availability of funds in a noninvestment grade or CAMELS 3 environment. CFP does not establish or inadequately establishes strategies that address liquidity shortfalls in a distressed environment. Stress testing is not performed or is inadequately performed.
MIS focus on significant issues and produce timely, accurate, complete, forward-looking, and meaningful information to enable effective management of liquidity, even in a distressed environment.	MIS adequately capture concentrations and rollover risk and are timely, accurate, forward-looking, and complete, even in a distressed environment. Recommendations are minor and do not affect effectiveness.	MIS may not sufficiently capture concentrations and rollover risk or may not be sufficiently timely, accurate, forward-looking, and complete, particularly when considering a stressed environment.	MIS are deficient, particularly in a distressed environment. Material information may be missing or inaccurate, and reports are not meaningful.

Price Risk

Price risk is the risk to current or projected financial condition and resilience arising from changes in the value of either trading portfolios or other obligations that are entered into as part of distributing risk. These portfolios typically are subject to daily price movements and are accounted for primarily on a mark-to-market basis. This risk occurs most significantly from market-making, dealing, and position-taking in interest rate, foreign exchange, equity, commodities, and credit markets.

Price risk also arises from bank activities whose value changes are reflected in the income statement, such as in lending pipelines, other real estate owned, and mortgage servicing rights. The risk to earnings or capital resulting from the conversion of a bank's financial statements from foreign currency translation also should be assessed under price risk. As with interest rate risk, many banks include price risk in the broader category of market risk.

Examiners should consider both the quantity of risk and the quality of risk management to derive the aggregate and direction of price risk.

Summary Conclusions

Price risk summary conclusions	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of Price Risk Indicators

Examiners should use the following indicators when assessing quantity of price risk.

Quantity of Price Risk Indicators		
Low	**Moderate**	**High**
Exposures are primarily confined to those arising from customer transactions and involve liquid and readily manageable products, markets, and levels of activity. Bank does trades back-to-back for customers, taking no or negligible risk positions. No proprietary trading exists. Trading personnel merely execute customer orders. Financial performance has no vulnerability to volatility from revaluation requirements.	Trading positions exist only to position securities for sale to customers. No proprietary trading exists. Open positions are small and involve liquid instruments that allow for easy hedging. Limited trading exists in option-type products. Financial performance has limited vulnerability to volatility from revaluation requirements.	Trading activity includes proprietary transactions, with positions unrelated to customer activity. Exposures reflect open or unhedged positions, including illiquid instruments, options, and/or longer maturities, which subject financial performance to significant volatility from revaluation requirements.
Daily trading gains/losses do not occur, because bank takes no or negligible risk.	Daily trading gains/losses are small and occur infrequently. Quarterly trading losses do not occur because of limited risk appetite and emphasis on customer revenues.	Daily trading gains/losses occur periodically because the bank either does not have customer transaction revenue support or takes positions that can create losses that eclipse customer revenues. Quarterly trading profits and losses can be large relative to budget and may occasionally result in a negative public perception.
Bank has a sales-driven culture, with sales personnel exercising greater authority than traders do.	Compensation programs reflect sales orientation but do provide limited incentives for trading profits.	Compensation programs reward traders for generating trading profits, reflecting a trader-dominated operation.
Policy limits reflect no risk appetite for price risk. Customer sales activities pose no or negligible threat to financial performance.	Policy limits reflect limited risk appetite for price risk.	Policy limits reflect excessive risk appetite, with the bank willing to risk losses that can impact quarterly earnings and/or capital.
Bank has non-dollar-denominated positions that are completely hedged. Assets denominated in foreign	Bank may have a small volume of unhedged, non-dollar-denominated positions, but it can readily hedge at a reasonable	Exposure reflects a large volume of unhedged, non-dollar-denominated positions, or a smaller volume of unhedged positions in illiquid

Quantity of Price Risk Indicators		
Low	**Moderate**	**High**
currencies equal liabilities denominated in foreign currencies. Financial performance is not vulnerable to changes in foreign exchange rates.	cost. There is limited vulnerability to changes in foreign currency exchange rates.	currencies for which hedging can be expensive. Changes in foreign currency exchange rates can adversely affect financial performance.
Bank has limited or no mortgage banking activities. The mortgage servicing asset, if any, is small relative to capital.	Bank is active in mortgage banking. The mortgage servicing asset is material relative to capital, and valuation adjustments can have a meaningful impact on financial performance.	Mortgage banking activities are a key business line for the bank. The mortgage servicing asset is large relative to capital, and valuation adjustments can be significant.
Bank has no current or limited exposure to OREO.	Bank has a modest amount of or exposure to OREO, but it is in property types or areas that are not expected to realize significant value changes that could negatively impact earnings.	Bank has a large amount of or exposure to OREO, which may be concentrated in property types or areas that may realize value changes that cause significant write-downs.
Held-for-sale portfolios, if any, are small and pose minimal risk to earnings.	Bank carries a small held-for-sale loan portfolio as part of its business of distributing risk into the capital markets. Write-downs to this portfolio, however, would not have a significant impact on earnings.	Originating and distributing loans into the capital markets is a key business line for the bank. Write-downs occasionally have, or are anticipated to have, a significant impact on earnings.

Quality of Price Risk Management Indicators

Examiners should use the following indicators when assessing quality of price risk management.

Quality of Price Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Policies reflect board's risk appetite and provide clear authorities, conservative limits, and assigned responsibilities. Policies permit risk-taking authority consistent with the expertise of bank personnel. Policies clearly and reasonably limit the volume of translation risk and assign responsibilities.	Policies provide generally clear authorities, reasonable limits, and assignment of responsibilities. Risk-taking authority is generally consistent with expertise of bank personnel. Policies address translation risk in a general way but may not provide specific management guidelines.	Policies require further clarification and more specific guidelines. Assignment of responsibilities may be incomplete. Risk-taking authority may not be consistent with expertise of bank personnel. Policies likely do not adequately address translation risk.	Policies do not reflect the risk appetite of the board. Policies do not clearly assign responsibilities. Risk-taking authority does not reflect the expertise of bank personnel. The bank does not have a policy addressing translation risk or policy limits are not reasonable given management expertise, the bank's capital position, and/or volume of assets and liabilities denominated in foreign currencies.

Quality of Price Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Management has broad mortgage servicing rights experience and has established strong policy controls and risk limits. Policy exceptions are rare and properly approved. The bank has a robust, well-documented, and well-supported valuation process.	Management has sufficient mortgage servicing rights and hedging experience. Policies generally address key risk management practices. Exceptions to policies occasionally occur but are properly approved. The bank has an adequate valuation process.	Management may lack extensive mortgage servicing rights and hedging experience. Policies may address some, but not all, key risk management practices. Exceptions to policies occasionally occur and may not be consistently approved. The valuation process may not be well supported or well documented.	Management attention to mortgage servicing is not commensurate with the risk, or management lacks sufficient experience in hedging mortgage servicing rights exposures. Policies do not address key risk management practices; exceptions frequently occur and are not properly approved. The valuation process is inadequate and unreliable and may result in material misstatements.
When the bank has OREO, management proactively obtains appraisals and takes any required write-downs on a timely basis. Management actively tries to sell OREO properties. Accounting for OREO expenses is appropriate and conforms to accounting guidance.	Management obtains appraisals, takes any required write-downs, and actively tries to sell OREO properties. Accounting for OREO expenses is appropriate. Minor exceptions or weaknesses may be present, but exceptions are not material or indicative of a pattern or practice.	Appraisals for OREO are occasionally out-of-date or of lower quality. Management's actions to sell OREO properties do not always demonstrate an active interest in timely disposition. Potential weaknesses exist in OREO accounting that may indicate a pattern or practice.	The quality of appraisals for OREO properties is questionable and/or the appraisals are significantly out-of-date. Management does not actively try to sell OREO properties (e.g., the bank may list the property for sale at an inflated price). Accounting for OREO expenses is not appropriate and may result in material inaccuracies.
Policies and controls for trading or available-for-sale assets effectively limit risk. Exceptions to policy are quickly identified and promptly raised to appropriate levels of management.	Policies and controls for trading or available-for-sale assets are generally effective. Policy exceptions are typically identified but may not be raised to appropriate levels of management on a timely basis.	Policies and controls for trading or available-for-sale assets show moderate weaknesses and may require improvement. Policy exceptions are not always identified and/or may not be raised to appropriate levels of management.	The bank lacks effective controls on trading or available-for-sale assets. Policy exceptions are not identified and are not raised to appropriate levels of management.

Quality of Price Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Management effectively understands, measures, and has technical expertise in managing translation risk. Management and the board regularly review currency translation risk exposures and direct changes, if necessary, given market conditions and the size of the exposure.	Management has a reasonable understanding of translation risk and how to measure and hedge it. Management and the board regularly review translation risk exposures but generally do not direct changes even in unsettled markets.	Management has some understanding of translation risk but may not measure and hedge it appropriately. Management and the board only periodically review translation risk exposures and generally do not direct changes.	Management does not demonstrate an understanding of translation risk and does not have the ability to manage it effectively. Neither management nor the board is aware of the magnitude of translation risk or does not review reports outlining translation risks.
Trading and sales personnel have broad experience in the products traded, are technically competent, and are comfortable with the bank's culture. Risk management personnel have an in-depth understanding of risk and risk management principles. Policy exceptions are rare, and formal procedures exist to report how/why they occurred and how they were resolved.	Trading and sales personnel are generally experienced and technically competent. Risk management personnel have a reasonable understanding of risk and risk management principles. Policy exceptions occur occasionally, but the bank has a process to report them and track resolution.	Trading and sales personnel have some experience but may demonstrate modest weaknesses in technical competency. Risk management staff require a better understanding of risk and risk management principles given the bank's complexity and risk profile. Policy exceptions are moderate, and the bank may not have a formal process to report them and track resolution.	Trading and sales personnel do not have broad experience in the products they trade. A risk management unit does not exist or is not independent and staffed by personnel familiar with risk management principles. Policy exceptions regularly occur or are not reported or tracked for resolution.
Management reports are prepared independently of the trading desk and provide a comprehensive and accurate summary of trading activities. Reports are timely, assess compliance with policy limits, and measure loss potential in both normal (e.g., value at risk) and stressed markets. Management at all levels understands and monitors price risk.	Management reports are prepared independently of the trading desk and provide a general summary of trading activities. Reports are timely but may not fully assess loss potential. Trading unit management reviews risk reports, and management at higher levels has a sufficient understanding to review trading activities regularly, though possibly not in depth.	Management reports may not be prepared independently of the trading desk. Reports may not provide a sufficient summary of trading activities, are not always timely, and may not fully assess loss potential. Trading unit management reviews risk reports, but management at higher levels may lack the understanding to review trading activities on a frequent basis and in depth.	Management reports are not independent of the trading desk, do not provide risk-focused information, and may not be prepared regularly. Higher-level managers do not understand price risk and do not review risk management reports.
Price risk monitoring, valuation, and control functions are independent from the business unit.	Price risk monitoring and control functions exist but may not have complete independence from the business unit.	Price risk monitoring and control functions may not be adequate and may lack independence from the business unit.	Price risk control functions do not exist or are not independent from the business unit. Trading positions are frequently valued on trader prices, with limited independent verification.

Operational Risk

Operational risk is the risk to current or projected financial condition and resilience arising from inadequate or failed internal processes or systems, human errors or misconduct, or adverse external events. Operational losses may result from internal fraud; external fraud; inadequate or inappropriate employment practices and workplace safety; failure to meet professional obligations involving clients, products, and business practices; damage to physical assets; business disruption and systems failures; and failures in execution, delivery, and process management. Operational losses do not include opportunity costs, forgone revenue, or costs related to risk management and control enhancements implemented to prevent future operational losses.

The quantity of operational risk and the quality of operational risk management are heavily influenced by the quality and effectiveness of a bank's system of internal control. The quality of the audit function, although independent of operational risk management, also is a key assessment factor. Audit can affect the operating performance of a bank by helping to identify and validate correction of weaknesses in risk management or controls. The quality of due diligence, risk management of third-party relationships, business continuity planning, and controls protecting the confidentiality, integrity, and availability of bank information are other key assessment factors for mitigating operational risk.

Examiners should consider both the quantity of risk and the quality of risk management to derive the aggregate and direction of operational risk.

Summary Conclusions

	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
Operational risk summary conclusions	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of Operational Risk Indicators

Examiners should use the following indicators when assessing quantity of operational risk.

Quantity of Operational Risk Indicators		
Low	**Moderate**	**High**
Exposure to risk from fraud, errors, or processing disruptions is minimal given the volume of transactions, complexity of products and services, and state of internal systems. Risk to financial performance is negligible.	Exposure to risk from fraud, errors, or processing disruptions is modest given the volume of transactions, complexity of products and services, and state of internal systems. Deficiencies that have potential impact on earnings or	Exposure to risk from fraud, errors, or processing disruptions is significant given the volume of transactions, complexity of products and services, and state of internal systems. Deficiencies

Quantity of Operational Risk Indicators		
Low	**Moderate**	**High**
	capital can be addressed in the normal course of business.	exist that represent significant risk to financial performance.
Risks from transaction-processing failures, technology changes, outsourcing, planned conversions, merger integration, or new products and services are minimal.	Risks from transaction-processing failures, technology changes, outsourcing, planned conversions, merger integration, or new products and services are moderate.	Risks from transaction-processing failures, technology changes, outsourcing, planned conversions, merger integration, or new products and services are high.
Volume of operational losses is minimal.	Volume of operational losses is moderate.	Volume of operational losses is high.
Volume of fraud and intrusions/attacks is minimal.	Volume of fraud and intrusions/attacks is moderate.	Volume of fraud and intrusions/attacks is high.
Employee turnover is low and has not affected any mission-critical areas.	Employee turnover is moderate, but effect on mission-critical areas is limited.	Employee turnover is excessive and has severely affected key areas of operations.
Number of third-party service providers is low.	Number of third-party service providers is moderate.	Number of third-party service providers is high.
Level of insurance bond claims is low.	Level of insurance bond claims is moderate.	Level of insurance bond claims is high.

Quality of Operational Risk Management Indicators

Examiners should use the following indicators when assessing quality of operational risk management.

Quality of Operational Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Governance activities are sound. Directors are qualified, appropriately compensated, ethical, and provide effective oversight. Corporate roles are clear, goals are effectively communicated, and disclosure is transparent.	Governance activities are satisfactory. Directors are qualified, appropriately compensated, and ethical. Oversight provided is adequate but may have subtle weaknesses. Corporate goals and responsibilities may be clear but are not fully communicated. Disclosure is adequate.	Governance activities need improvement. Corporate structure may not be adequately defined or communicated. Directors' qualifications, ethical standards, or compensation may be questionable. Oversight may need improvement. Disclosures may contain inaccuracies.	Governance activities are deficient. Corporate structure is not defined or communicated. Directors' qualifications, ethical standards, or compensation are highly questionable. Oversight is inadequate or ineffective. Disclosure is inaccurate and process is significantly flawed.
Management has developed a comprehensive and effective internal control environment. A commitment to internal controls is evident and well disseminated throughout the	Control environment is appropriate for the size and sophistication of the institution. Commitment to internal controls is evident but may not be well disseminated. Structure may not be fully communicated across	Control environment needs improvement given the size and sophistication of the institution. Commitment to internal controls may not be readily evident or well disseminated. Structure may not be well	Control environment is deficient. Findings indicate a lack of awareness, commitment, and/or focus on the importance of effective and appropriate internal controls. Board oversight is ineffective. Volume

Quality of Operational Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
enterprise. Board oversight is strong. Integrity of control systems is tested on a regular basis.	the organization. Board oversight/control culture is considered effective, although modest weaknesses may be present. Control integrity is tested on a periodic basis.	communicated or understood throughout the organization. Board oversight needs improvement, as weaknesses may be present. Control integrity testing may not be performed with sufficient consistency.	and severity of control exceptions are high. Exposure to potential or realized losses from key operational areas may be present. Control integrity testing is nonexistent or is performed inconsistently.
Management anticipates and responds effectively to risks associated with operational changes, emerging/changing technologies, and external threats.	Management adequately responds to risks associated with operational changes, emerging/changing technologies, and external threats.	Management may not adequately or consistently respond to risks associated with operational changes, emerging/changing technologies, and external threats.	Management does not take timely and appropriate actions to respond to operational changes, emerging/changing technologies, and external threats.
Management fully understands operational risks and has expertise to evaluate key technology-related issues.	Management reasonably understands operational risks and has sufficient expertise to evaluate key technology-related issues.	Management may not adequately understand operational risks and may lack adequate expertise to evaluate key technology-related issues.	Management does not understand, or has chosen to ignore, key aspects of operational risk. Expertise to evaluate key technology-related issues is insufficient.
New/nontraditional product development and implementation is well managed with low risk exposure.	New/nontraditional product development and implementation is adequately managed, with some weaknesses and risk exposure evident.	New/nontraditional product development and implementation needs improvement, with weaknesses and elevated risk exposure.	New/nontraditional product development and implementation is inadequately managed, with significant weaknesses and high risk exposure.
Third-party risk management activities are sound. Risk exposure is well managed. Management comprehensively provides for continuity and reliability of services furnished by third parties.	Third-party risk management activities are satisfactory but may contain modest weaknesses. Risk exposure is satisfactorily managed. Management adequately provides for continuity and reliability of services furnished by third parties.	Third-party risk management activities need improvement. Risk exposure may not be adequately managed. Management may not adequately provide for continuity and reliability of services furnished by third parties.	Third-party risk management activities are severely limited or nonexistent. Risk exposure is inadequately managed. Management has not provided for continuity and reliability of services furnished by third parties.
Controls to safeguard physical assets, data, and personnel are comprehensive and effective in appropriately mitigating risks. Information security program is comprehensive, effective, and tested on a regular basis. Procedures to	Controls to safeguard physical assets, data, and personnel are satisfactory but may have modest weaknesses. Information security program is acceptable overall but may require minor enhancement and/or more frequent testing to be fully	Controls to safeguard physical assets, data, and personnel may not be adequate. Information security program may need substantive improvements. Procedures to identify and report potential data losses may need improvement. Privacy	Controls to safeguard physical assets, data, and personnel are deficient or nonexistent. Information security program is significantly flawed, incomplete, and/or inadequate. Annual testing and/or reporting have not occurred, and

Quality of Operational Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
identify and report potential data losses are effective. Privacy practices are sound.	comprehensive and effective. Procedures to identify and report potential data losses are satisfactory. Privacy practices are satisfactory.	practices may need improvement.	procedures to identify and report potential data losses are absent. Privacy practices are inadequate.
Processes and systems to monitor, track, and categorize operating losses are sound.	Processes and systems to monitor, track, and categorize operating losses are satisfactory but may contain modest weaknesses.	Processes and systems to monitor, track, and categorize operating losses need improvement.	Processes and systems to monitor, track, and categorize operating losses are weak or nonexistent.
MIS provide appropriate monitoring of transaction volumes, error reporting, fraud, suspicious activity, security violations, etc. MIS are accurate, timely, complete, and reliable.	MIS for transaction processing are adequate, although moderate weaknesses may exist.	MIS for transaction processing need improvement.	MIS for transaction processing are unsatisfactory and inadequate and exhibit significant weaknesses or may not exist.
Insurance coverage is sufficient and policies are current. An effective process for provider/agent selection and monitoring is present and overall coverage adequacy is reviewed at least annually.	Insurance coverage is sufficient and policies are current. Provider/agent selection process is acceptable and ongoing monitoring is limited. Coverage adequacy is reviewed on a periodic basis.	Insurance coverage may not be adequate in consideration of the exposures present. Tracking procedures may have allowed some policies to lapse and may need improvement. Due diligence programs for provider/agent selection and/or ongoing monitoring may need improvement.	Insurance coverage is insufficient for the exposure present. Inadequate tracking procedures have allowed policies to lapse. Due diligence programs for provider/agent selection and/or ongoing monitoring are inadequate, flawed, or ineffective.
Audit coverage is strong. Audit activities are frequent and ongoing and address all key areas of operations. Audit function is fully independent and competent, and scope is comprehensive. Risk assessment is effective and current. Follow-up and correction of deficiencies is proactive and effective. Repeat issues are rare or nonexistent. Board oversight is effective.	Audit coverage is satisfactory. Function is fully independent and competent, but scope may be limited. Risk assessment is acceptable overall but may be missing substance in some areas or require updating. Follow-up and correction of deficiencies is adequate but with moderate weaknesses noted therein. Repeat issues are few. Board oversight is adequate.	Audit coverage needs improvement. Independence may be impaired. Competency may be questionable, and scope may be limited. Risk assessment may need improvement. Follow-up and correction of deficiencies may be inconsistent, and several repeat issues may be found. Board oversight may need improvement.	Audit coverage is inadequate. Independence is impaired. Competency is questionable. Scope is inappropriate. Risk assessment is ineffective or nonexistent. Follow-up and correction of deficiencies is highly inconsistent. Repeat issues are numerous. Board oversight is limited, and ability to self-police is impaired.

Compliance Risk

Compliance risk is the risk to current or projected financial condition and resilience arising from violations of laws or regulations, or from nonconformance with prescribed practices, internal bank policies and procedures, or ethical standards. This risk exposes a bank to potential fines, CMPs, payment of damages, and the voiding of contracts. Compliance risk can result in diminished reputation, harm to bank customers, limited business opportunities, and lessened expansion potential. (Updated in version 1.1)

Compliance risk is not limited to risk from failure to comply with consumer protection-related laws and regulations; it encompasses the risk of noncompliance with *all* laws and regulations, as well as prudent ethical standards and contractual obligations. It also includes the exposure to litigation (known as legal risk) from all aspects of banking, traditional and nontraditional.

Examiners should consider both the quantity of risk and the quality of risk management to derive the aggregate and direction of compliance risk.

Summary Conclusions

	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
Compliance risk summary conclusions	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of Compliance Risk Indicators

Examiners should use the following indicators when assessing quantity of compliance risk.

Quantity of Compliance Risk Indicators		
Low	**Moderate**	**High**
Violations or compliance program weaknesses are insignificant in number or do not exist.	Violations or compliance program weaknesses exist and represent technical issues with some reimbursement to consumers that are resolved in a timely manner.	Violations or compliance program weaknesses are significant in number, resulting in large consumer reimbursements or regulatory fines and penalties.
No e-banking or the Web site is informational or nontransactional.	Bank is beginning e-banking and offers limited products and services.	Bank offers a wide array of e-banking products and services (e.g., account transfers, e-bill payments, or accounts opened via the internet).
All loans are originated in-house with no broker or third-party relationships.	Low volume of consumer and business loans are originated by local brokers or other third parties.	High volume of consumer or business loans is originated by multiple statewide or nationwide brokers or other third parties.

Quantity of Compliance Risk Indicators		
Low	**Moderate**	**High**
Limited/no marketing or advertising of products and services.	Limited marketing or advertising practices commensurate with strategic focus.	Marketing and advertising of new products offered through multiple channels (branch network, internet, direct mail, solicitations, etc.).
Bank offers traditional mix of noncomplex lending, investment, and deposit products.	Bank offers traditional investment and deposit products and a mix of traditional and complex lending products.	Bank offers a broad array of traditional and complex lending, investment, and deposit products.
Bank offers products and services to local market/service area.	Bank offers products and services to regional market/service area.	Bank offers products and services to national market/service area.
Financial institution competition within its marketplace is minimal.	Financial institution competition within its marketplace is considerable.	Financial institution competition within its marketplace is significant and may include large national and international companies.
Volume of products and services offered is reasonable considering its financial strength and capability, and growth is stable.	Volume of products and services offered is increasing considering its financial strength and capability, and growth is steady.	Volume of products and services offered is outpacing its financial strength and capability, and growth is unstable.
Bank has few offices, some automated teller machines (ATM), and centralized operations.	Bank has statewide branching and ATM network with decentralized operations.	Bank has regional or national branching and ATM network with decentralized operations.
Volume of customer complaints is minimal. (Updated in version 1.1)	Volume of customer complaints is moderate. (Updated in version 1.1)	Volume of customer complaints is high. (Updated in version 1.1)

Quality of Compliance Risk Management Indicators

Examiners should use the following indicators when assessing quality of compliance risk management.

Quality of Compliance Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Board has adopted compliance risk management policies that are consistent with business strategies and risk appetite.	Board has adopted compliance risk management policies that are generally consistent with business strategies and risk appetite.	Board has adopted compliance risk management policies that may not be consistent with business strategies and risk appetite.	Board has adopted compliance risk management policies that are inconsistent with business strategies and risk appetite.
Management fully understands all aspects of compliance risk and exhibits clear commitment to compliance. Commitment is	Management reasonably understands the key aspects of compliance risk. Commitment to compliance is reasonable and satisfactorily	Management may not understand or appreciate the key aspects of compliance risk. Commitment to compliance may not be evident or adequately	Management does not understand or has chosen to ignore key aspects of compliance risk. Importance of compliance is not emphasized or

Quality of Compliance Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
communicated throughout the bank.	communicated throughout the bank.	communicated throughout the bank.	communicated throughout the bank.
Authority and accountability are clearly defined and enforced.	Authority and accountability are defined, although some refinements may be needed.	Authority and accountability may not be defined or adequately enforced.	Management has not established or enforced accountability.
Management anticipates and responds well to market, technological, or regulatory changes.	Management adequately responds to market, technological, or regulatory changes.	Management may not consistently or adequately anticipate and respond to market, technological, or regulatory changes.	Management does not anticipate or take timely or appropriate actions in response to market, technological, or regulatory changes.
Compliance considerations are incorporated into product/system development and modification processes, including changes made by third parties.	Compliance is generally considered when developing products and systems; issues are addressed before they are fully implemented.	Compliance considerations may not adequately or consistently be incorporated into product and system development.	Compliance considerations are not incorporated into product and system development.
Control systems effectively identify violations or compliance system weaknesses, and corrective action is prompt and reasonable.	Control systems are adequate for identifying violations or compliance system weaknesses but not always in a timely manner. Management is usually responsive, and corrective action is generally timely.	Control systems need improvement for identifying violations or compliance system weaknesses and may not consistently identify weaknesses. Management may fail to respond and implement corrective actions in a timely manner.	Control systems are ineffective in identifying violations and compliance system weaknesses. Management is unresponsive, and corrective action is weak.
Management provides effective resources/training programs to appropriate personnel.	Management provides adequate resources/training, given the complexity of products/operations.	Management may not provide adequate resources or training, given the complexity of products/operations.	Management does not provide resources or training.
Bank has a strong record of compliance. Considering the scope and complexity of its operations and structure, compliance risk management systems are sound and minimize the likelihood of significant or frequent violations or instances of noncompliance.	Bank has a satisfactory record of compliance. Considering scope and complexity of operations and structure, compliance risk management systems are adequate to avoid significant or frequent violations or instances of noncompliance.	Bank's record of compliance needs improvement. Considering the scope and complexity of operations and structure, compliance risk management systems may reflect a lack of sufficient commitment to risk management.	Bank has an unsatisfactory record of compliance. Considering scope and complexity of operations and structure, compliance risk management systems are deficient, reflecting inadequate commitment to risk management.
Bank has a strong record of acting on and	Bank has a satisfactory record of acting on and	Bank has an insufficient record of acting on and	Bank has a weak record of acting on and

Quality of Compliance Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
monitoring consumer complaints.	monitoring consumer complaints.	monitoring consumer complaints.	monitoring consumer complaints.

Strategic Risk

Strategic risk is the risk to current or projected financial condition and resilience arising from adverse business decisions, poor implementation of business decisions, or lack of responsiveness to changes in the banking industry and operating environment. This risk is a function of a bank's strategic goals, business strategies, resources, and quality of implementation. The resources needed to carry out business strategies are both tangible and intangible. They include communication channels, operating systems, delivery networks, and managerial capacities and capabilities.

The assessment of strategic risk includes more than an analysis of a bank's written strategic plan. It focuses on opportunity costs and how plans, systems, and implementation affect the bank's financial condition and resilience. It also incorporates how management analyzes external factors, such as economic, technological, competitive, regulatory, and other environmental changes, that affect the bank's strategic direction.

Examiners should consider both the quantity of risk and the quality of risk management to derive the aggregate and direction of strategic risk.

Summary Conclusions

	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
Strategic risk summary conclusions	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of Strategic Risk Indicators

Examiners should use the following indicators when assessing quantity of strategic risk.

Quantity of Strategic Risk Indicators		
Low	**Moderate**	**High**
Board has adopted policies that are fully consistent with business strategies and risk appetite.	Board has adopted policies that are generally consistent with business strategies and risk appetite.	Board has adopted policies that are inconsistent with business strategies and risk appetite.
Initiatives are well supported by capital for the foreseeable future and pose only nominal possible effects on financial condition. Decisions can be reversed with little difficulty and manageable costs.	Initiatives are reasonable considering the capital, communication channels, operating systems, and service delivery networks. Decisions are unlikely to have significant adverse impact on financial condition. Decisions can be reversed without significant cost or difficulty.	Initiatives are aggressive or incompatible with developed business strategies, communication channels, operating systems, and service delivery networks. Impact of strategic decisions is expected to significantly affect financial

Quantity of Strategic Risk Indicators		
Low	**Moderate**	**High**
		condition. Decisions are difficult or costly to reverse.
Compensation programs achieve an appropriate balance between risk appetite and controls. Compensation strategies reflect core principle of "pay for performance." Performance goals and metrics to measure achievement are reasonably transparent.	Compensation programs are appropriately balanced between risk appetite and controls but may be informal or reflect modest weaknesses. Incentives are appropriate. Performance goals and metrics to measure achievement are reasonably transparent overall but may contain some minor obscurities.	Compensation programs unduly focus on short-term performance. Incentives may be inappropriate. Use of performance goals and metrics to measure achievement are obscure.
Due diligence for new products and services is robust. Process considers all appropriate factors, including assessing the impact to the bank's strategic direction, assessing the associated risks, consulting with relevant functional areas, determining regulatory requirements, determining the expertise needed, researching any third parties, developing a realistic business plan, and developing viable alternatives.	Due diligence for new products and services is satisfactory. Process may not fully consider all appropriate factors but provides for a general understanding of the risks associated with any new product or service.	Due diligence for new products and services is insufficient. Process does not consider the appropriate factors, and the risks associated with any new product or service are not known.

Quality of Strategic Risk Management Indicators

Examiners should use the following indicators when assessing quality of strategic risk management.

Quality of Strategic Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
The depth and technical expertise of staff enables management and the board to effectively set strategic direction and achieve organizational efficiency.	The depth and technical expertise of staff generally enables management and the board to set strategic direction and achieve organizational efficiency.	The depth and technical expertise of staff may prevent management and the board from being effective in setting strategic direction or achieving organizational efficiency.	Lack of depth and technical expertise of staff often prevents management and the board from effectively setting strategic direction and achieving organizational efficiency.
Management and the board have a well-defined planning process and a successful record in accomplishing stated strategic goals.	Management and the board have a well-defined planning process and a reasonable record in accomplishing stated strategic goals.	Management and the board's planning process needs improvement. The bank has on occasion failed to achieve a key strategic goal.	Management and the board do not have an effective planning process or consistently fail to accomplish stated strategic goals.
Initiatives are supported by sound due diligence and	The quality of due diligence and risk management is	The quality of due diligence and risk management, while	Less-than-effective risk management systems or a lack of adequate due

Quality of Strategic Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
effective risk management systems, which are an integral part of strategic planning.	consistent with the strategic issues confronting the organization. Risk management, while a part of strategic planning, may be less than comprehensive.	consistent with the strategic issues confronting the organization, may overlook a key consideration. Risk management, while a part of strategic planning, may be less than comprehensive or inadequately address a key issue.	diligence has resulted in deficiencies in management decisions and may undermine effective evaluation of resources and commitment to new products and services or acquisitions. Risk management is not a material factor in strategic planning.
The impact of reversing or modifying strategic decisions is fully assessed as part of the planning process.	The impact of reversing or modifying strategic decisions is assessed as part of the planning process, with only minor omissions.	The impact of reversing or modifying strategic decisions is assessed as part of the planning process but may fail to address a key factor.	The impact of reversing or modifying strategic decisions is not assessed as part of the planning process.
Strategic goals are effectively communicated and evident throughout the organization.	Strategic goals are communicated and evident throughout the organization.	Strategic goals may not be communicated and evident throughout the organization.	Strategic goals are not clearly communicated or evident throughout the organization.
MIS effectively support the bank's strategic direction and initiatives.	MIS reasonably support the bank's strategic direction.	MIS may not fully support the bank's strategic direction.	MIS do not support the bank's strategic direction or address a changing environment.
Management and the board are aware of and effectively incorporate technology management into strategic plans.	Management and the board are aware of and usually incorporate technology management into strategic plans.	Management and the board are aware of and usually incorporate technology management into strategic plans, although there may be key gaps.	Management and the board do not effectively incorporate technology management into strategic plans.

Reputation Risk

Reputation risk is the risk to current or projected financial condition and resilience arising from negative public opinion. This risk may impair a bank's competitiveness by affecting its ability to establish new relationships or services or continue servicing existing relationships. Reputation risk is inherent in all bank activities, and management should deal prudently with stakeholders, such as customers, counterparties, correspondents, investors, regulators, employees, and the community.

A bank that actively associates its name with products and services offered through outsourced arrangements or asset management affiliates is more likely to have higher reputation risk exposure. Significant threats to a bank's reputation also may result from negative publicity regarding matters such as unethical or deceptive business practices, violations of laws or regulations, high-profile litigation, or poor financial performance. The assessment of reputation risk should take into account the bank's culture, the effectiveness of its problem-escalation processes and rapid-response plans, and its engagement with news media.

Examiners should consider both the quantity of risk and the quality of risk management to derive the aggregate and direction of reputation risk.

Summary Conclusions

	Quantity of risk	Quality of risk management	Aggregate level of risk	Direction of risk
Reputation risk summary conclusions	☐ Low ☐ Moderate ☐ High	☐ Strong ☐ Satisfactory ☐ Insufficient ☐ Weak	☐ Low ☐ Moderate ☐ High	☐ Decreasing ☐ Stable ☐ Increasing

Quantity of Reputation Risk Indicators

Examiners should use the following indicators when assessing quantity of reputation risk.

Quantity of Reputation Risk Indicators		
Low	**Moderate**	**High**
Management demonstrates outstanding performance in meeting community's credit needs. Community reinvestment is a formal part of strategic planning and daily business. Bank is routinely seen in a leadership role in community development. Lending programs targeted to low/moderate income borrowers and areas are innovative and	Management demonstrates satisfactory performance in meeting community's credit needs. Bank generally participates in community development activities but not in a leadership role. Lending programs targeted to low/moderate income borrowers and areas exist but are not innovative or complex. Identified	Management's performance in meeting community's credit needs requires improvement or is unsatisfactory. Participation in community development activities is rare, and lending to low/moderate income borrowers or areas may be limited. Identified lending areas may arbitrarily exclude low/moderate income areas.

Quantity of Reputation Risk Indicators		
Low	**Moderate**	**High**
effective. Identified lending areas are appropriate and legal.	lending areas are appropriate and legal.	
There may be some plans for merger or acquisition activities or entrance into new businesses, product lines, technologies, or third-party relationships.	There are substantial plans for merger or acquisition activities, or entrance into new businesses, product lines, technologies, or third-party relationships.	There are significant and transformative plans for merger or acquisition activities, or entrance into new businesses, product lines, technologies, or third-party relationships.
The bank enjoys a favorable market and public perception. The level of litigation, losses, violations of laws and regulations, and customer complaints is minimal.	The level of litigation, losses, violations of laws and regulations, and customer complaints may adversely affect the bank's market and public perception.	Bank is substantially exposed to adverse market and public perception as shown in significant litigation, large dollar losses, substantive violations of laws and regulations, or a high volume of customer complaints.
Losses from asset management activities are low relative to the number of accounts and the transaction volume. The bank avoids conflicts of interest.	Losses from asset management activities are moderate relative to the number of accounts and the transaction volume. The bank has generally avoided conflicts of interest and other legal or control breaches.	Losses from asset management activities are elevated relative to the number of accounts and the transaction volume. Poor account administration, conflicts of interest, and other legal or control breaches may be evident.
Fair lending practices are strong, and management is committed to fair lending principles. Fair lending policies are comprehensive and well communicated to all areas of the bank. Fair lending requirements are well known, with ongoing training provided at least annually. Credit decision making is centralized. Underwriting policies are well defined and are followed with few exceptions. A formal second review process is in place, and annual testing is required.	Fair lending practices are satisfactory, and management's commitment is appropriate. Fair lending principles are informally understood throughout the bank but not fully integrated into all areas. Decision making may be decentralized, and underwriting requirements may be general in nature, with a modest level of exceptions. A second review function exists but is informal. Testing and training are acceptable but may display subtle weaknesses.	Management has not demonstrated an effective commitment to fair lending. Fair lending practices/policies are not well communicated, and concepts are not fully understood. Underwriting requirements are limited, and exceptions are excessive. No second review process exists. Testing and training programs are limited, ineffective, or absent. Potential for noncompliance is high.

Quality of Reputation Risk Management Indicators

Examiners should use the following indicators when assessing quality of reputation risk management.

Quality of Reputation Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Management anticipates and effectively responds to changes of a market, technological, or regulatory nature that may affect the bank's	Management adequately responds to changes of a market, technological, or regulatory nature that may affect the bank's	Management's response to changes of a market, technological, or regulatory nature may not be timely or appropriate.	Management does not take timely or appropriate actions in response to changes of a market, technological, or regulatory nature.

Quality of Reputation Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
reputation in the marketplace.	reputation in the marketplace.		
Management fosters a sound culture based on strong core values and ethics that are clearly communicated and monitored throughout the bank.	The bank's culture is sound, but core values or ethics may not be consistently communicated or monitored.	The bank's culture is generally sound, but there may be isolated incidents of employee misconduct.	Employee conduct demonstrates a disregard for or unawareness of ethics. There may be incentives for employees to take excessive risks or employees are not held accountable for their actions.
Management effectively self-polices risks. Processes to monitor, escalate, and mitigate issues, including those related to customer complaints, are well defined and tested periodically.	Management adequately self-polices risks. Processes to monitor, escalate, and mitigate issues may be informal.	Management's self-policing of risks needs improvement. Processes to monitor, escalate, and mitigate issues may not be timely or effective in one or more areas.	Management's self-policing of risks is deficient or absent in one or more critical areas.
Operational risk management is strong. Internal controls and audit are fully effective.	Operational risk management is satisfactory. Internal controls and audit are generally effective.	Operational risk management is insufficient. Internal controls and audit need improvement.	Operational risk management is weak. Internal controls and audit are not effective in reducing exposure.
Management has clear awareness of privacy issues and uses customer information responsibly.	Management understands privacy issues and generally uses customer information responsibly.	Management has gaps in knowledge of privacy issues, and there may be instances when customer information is not used responsibly.	Management is not aware of or concerned with privacy issues and may use customer information irresponsibly.
Management has effective, well-documented account administration, investment management, and retail sales policies and processes in place.	Management has adequate account administration, investment management, and retail sales policies and processes in place.	Account administration, investment management, and retail sales policies and processes need improvement. Control processes and MIS do not always capture violations of laws or regulations or exceptions to policy.	Account administration, investment management, and retail sales policies and processes are inadequate. Control processes and MIS regularly fail to capture violations of laws or regulations or exceptions to policy.

Other Risks

BSA/AML/OFAC Risk Indicators

Quantity of BSA/AML/OFAC Risk Indicators

Examiners should use the following indicators when assessing quantity of BSA/AML/OFAC risk. The quantity of risk indicators in this section includes information from appendixes J and M of the *FFIEC BSA/AML Examination Manual*.

Quantity of BSA/AML/OFAC Risk Indicators		
Low	**Moderate**	**High**
Stable, known customer base.	Customer base increasing due to branching, merger, or acquisition.	Large and growing customer base in a wide and diverse geographic area.
No e-banking or Web site is informational or nontransactional.	Bank offers limited products and services.	Bank offers a wide array of e-banking products and services (e.g., account transfers, e-bill payment, or accounts opened via the internet).
On the basis of information received from the BSA-reporting database, there are few or no large currency or structured transactions.	On the basis of information received from the BSA-reporting database, there is a moderate volume of large currency or structured transactions.	On the basis of information received from the BSA-reporting database, there is a significant volume of large currency or structured transactions.
A few high-risk customers and businesses.	A moderate number of high-risk customers and businesses.	A large number of high-risk customers and businesses.
Bank has no overseas branches and no foreign correspondent financial institution accounts. Bank does not engage in pouch activities, offer special-use accounts, offer payable through accounts (PTA), or provide U.S. dollar draft services.	Bank has overseas branches or a few foreign correspondent financial institution accounts, typically with financial institutions with adequate AML policies and procedures from low-risk countries, and minimal pouch activities, special-use accounts, PTAs, or U.S. dollar draft services.	Bank has overseas branches or maintains a large number of foreign correspondent financial institution accounts with financial institutions with inadequate AML policies and procedures, particularly those located in high-risk jurisdictions, or offers substantial pouch activities, special-use accounts, PTAs, or U.S. dollar draft services.
Few international accounts or very low volume of currency activity in the accounts.	Moderate level of international accounts with unexplained currency activity.	Large number of international accounts with unexplained currency activity.
Bank offers limited or no private banking services or trust and asset management products or services.	Bank offers limited domestic private banking services or trust and asset management products or services over which the bank has investment discretion. Strategic plan may be to increase trust business.	Bank offers significant domestic and international private banking or trust and asset management products or services. Private banking or trust and asset management services are growing. Products offered include investment management services, and trust accounts are predominantly nondiscretionary

Quantity of BSA/AML/OFAC Risk Indicators		
Low	**Moderate**	**High**
		versus where the bank has full investment discretion.
Limited number of funds transfers for customers, noncustomers; limited third-party transactions, and no foreign funds transfers.	Moderate number of funds transfers. Few international funds transfers from personal or business accounts with typically low-risk countries.	Large number of noncustomer funds transfer transactions and payable upon proper identification transactions. Frequent funds from personal or business accounts to or from high-risk jurisdictions, and financial secrecy havens or jurisdictions.
No other types of international transactions, such as trade finance, cross border automated clearinghouse, and management of sovereign debt.	Limited other types of international transactions.	A high number of other types of international transactions.
No history of OFAC actions. No evidence of apparent violation or circumstances that might lead to a violation.	A small number of recent actions (e.g., actions within the last five years) by OFAC, including notice letters, or CMPs, with evidence that the bank addressed the issues and is not at risk of similar violations in the future.	Multiple recent actions by OFAC, where the bank has not addressed the issues, thus leading to an increased risk of the bank undertaking similar violations in the future.
Bank is not located in a high-intensity drug trafficking area (HIDTA) or high-intensity financial crime area (HIFCA). No fund transfers or account relationships involve HIDTAs or HIFCAs.	Bank is located in a HIDTA or HIFCA. Bank has some fund transfers or account relationships that involve HIDTAs or HIFCAs.	Bank is located in a HIDTA and HIFCA. Large number of fund transfers or account relationships involve HIDTAs or HIFCAs.
No transactions with high-risk geographic locations.	Minimal transactions with high-risk geographic locations.	Significant volume of transactions with high-risk geographic locations.
Low turnover of key personnel or frontline personnel (e.g., customer service representatives, tellers, or other branch personnel).	Low turnover of key personnel, but frontline personnel in branches may have changed.	High turnover, especially in key personnel positions.

Quality of BSA/AML/OFAC Risk Management Indicators

Examiners should use the following indicators when assessing quality of BSA/AML/OFAC risk management.

Quality of BSA/AML/OFAC Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Management fully understands the aspects of compliance risk and exhibits strong commitment to compliance.	Management reasonably understands key aspects of compliance, and commitment is generally clear and satisfactorily communicated.	Management may not have a sufficient understanding of key aspects of compliance risk. The importance of compliance may not be adequately emphasized or communicated throughout the organization.	Management does not understand or has chosen to ignore key aspects of compliance risk. Importance of compliance is not emphasized or communicated throughout the organization.
Compliance considerations are effectively incorporated into all products and areas of the bank.	Compliance considerations are generally incorporated into products and areas of the bank.	Compliance considerations may not be adequately incorporated into a key product or area of the bank.	Compliance considerations are not adequately incorporated into several key products or areas of the bank.
Deficiencies are usually self-identified. Such deficiencies are minor, and when identified, management promptly implements meaningful corrective action.	Deficiencies are generally self-identified, and management is responsive to identified deficiencies. Deficiencies can be corrected in the normal course of business without significant investment of money or management attention.	Deficiencies may not be self-identified. Management may not be sufficiently responsive to identified deficiencies. Deficiencies may not be correctable in the normal course of business.	Deficiencies are not self-identified. Management may only respond when violations are cited. Deficiencies are significant and may require substantial time and resources to correct.
Authority and accountability for compliance are clearly defined and enforced, including designation of a qualified BSA officer.	Authority and accountability are defined, but some refinements are needed. A qualified BSA officer has been designated.	Authority and accountability for compliance need improvement. A qualified BSA officer may have been designated, but the role and responsibilities of the BSA officer may not be clear.	Authority and accountability for compliance have not been clearly established. No BSA officer or an unqualified one may have been appointed. The role of the BSA officer is unclear.
Independent testing is in place and is effective.	Overall, independent testing is in place and effective. Some weaknesses, however, are noted.	Independent testing is in place but may not be sufficiently effective.	Independent testing is not in place and/or is ineffective.
Board has approved a BSA compliance program that includes well-defined policies, procedures, controls, and information systems.	Board has approved a BSA compliance program that addresses most policies, procedures, controls, and information systems.	Board has approved a BSA compliance program, but the program may not sufficiently address policies, procedures, controls, and information systems.	Board may not have approved a BSA compliance program. Policies, procedures, controls, and information systems are significantly deficient. For example, there may be substantial failures to file currency transaction reports (CTR) and/or suspicious activity reports.

Quality of BSA/AML/OFAC Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Training is appropriate and effective, and covers applicable personnel, and necessary resources have been provided to appropriate personnel.	Training is conducted and management provides adequate resources given the bank's risk profile; some areas, however, are not covered within the training program.	Training is conducted consistently but may not sufficiently cover important regulatory and risk areas. Management may need to provide additional resources given the bank's risk profile.	Training is either not performed or not consistent and does not cover important regulatory and risk areas. Management does not provide necessary resources given the bank's risk profile.
Effective customer and beneficial ownership identification processes and account-opening procedures are in place.	Customer and beneficial ownership identification processes and account-opening procedures are generally in place but not well applied to all high-risk areas.	Customer and beneficial ownership identification and processes and account-opening procedures may not be adequately in place or effective.	Customer and beneficial ownership identification processes and account-opening procedures are absent or ineffective.
Management has identified and developed controls that are applied appropriately to high-risk areas, products, services, and customers of the bank.	Management is aware of high-risk areas, products, services, and customers, but controls are not always appropriately applied to manage this risk.	Management is not sufficiently aware of high-risk areas, products, services, and customers, and controls to manage this risk may need improvement.	Management is not aware of or chooses to ignore high-risk areas of the bank. Inadequate policies, procedures, and controls have resulted in instances of unreported suspicious activity, unreported large currency transactions, structured transactions, and/or substantive violations of law.
Compliance systems and controls quickly adapt to changes in various government lists (e.g., OFAC, FinCEN, and other government provided list(s)).	Compliance systems and controls are generally adequate and adapt to changes in various government lists (e.g., OFAC, FinCEN, and other government provided list(s)).	Compliance systems and controls need improvement to comply with and adapt to changes in various government lists (e.g., OFAC, FinCEN, and other government provided list(s).	Compliance systems and controls are inadequate to comply with and adapt to changes in various government lists (e.g., OFAC, FinCEN, and other government provided list(s).
Compliance systems and controls effectively identify and appropriately report suspicious activity. Systems are commensurate with risk.	Compliance systems and controls identify suspicious activity. Monitoring systems, however, are not fully comprehensive or may have some weaknesses.	Compliance systems and controls need improvement to identify suspicious activity. Monitoring systems may need improvement.	Compliance systems and controls are ineffective in identifying and reporting suspicious activity.
Low volume of correspondence from IRS indicates that currency transaction reports (CTR) are accurate.	Volume of correspondence from IRS indicates minor errors in CTR reporting.	Volume of correspondence from IRS indicates an elevated level of errors in CTR reporting.	Volume of correspondence from IRS indicates a substantive volume of CTR reporting errors.

Quality of BSA/AML/OFAC Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Appropriate compliance controls and systems are implemented to identify compliance problems and assess performance.	No shortcomings of significance are evident in compliance controls or systems. Probability of serious future violations or noncompliance is within acceptable tolerance.	Compliance controls or systems need improvement. Probability of future violations or noncompliance may be outside the acceptable tolerance.	Likelihood of continued compliance violations or noncompliance is high because a corrective action program does not exist or extended time is needed to implement such a program.

Fair Lending Risk Indicators

When assessing fair lending risk, examiners consider a bank's risks related to the Equal Credit Opportunity Act, Fair Housing Act, and implementing regulations.[59] Examiners should use the indicators in this section when assessing the quantity of fair lending risk and quality of fair lending risk management for banks with under $500 million in assets. Examiners must use the OCC's fair lending risk assessment tool for banks with assets of $500 million or greater. The fair lending risk assessment tool incorporates the factors in this section.

Quantity of Fair Lending Risk Indicators

Quantity of Fair Lending Risk Indicators		
Low	**Moderate**	**High**
Significant and explainable volume of consumer lending.	Lower volume of consumer lending, but explainable.	Low and unexplainable volume of consumer lending. (Bank could be discouraging applicants.)
Generic, noncomplex products offered.	Limited number of complex products offered.	Several complex products offered (e.g., subprime high-cost mortgages).
Low number of policy exceptions/overrides.	Modest number of policy exceptions/overrides and may exceed guidelines.	High number of policy exceptions/overrides.
Lending policies allow little or no lender discretion in the loan decision process.	Lending policies allow some lender discretion in the loan decision process.	Lending policies allow high level of lender discretion in the loan decision process.
Little or no disparities among approval/denial rates or pricing by prohibited basis groups.	Some disparities among approval/denial rates or pricing by prohibited basis groups.	Substantive disparities among approval/denial rates or pricing by prohibited basis groups.
Low proportion of withdrawn/incomplete applications for prohibited basis groups.	Moderate proportion of withdrawn/incomplete applications for prohibited basis groups.	Higher proportion of withdrawn/incomplete applications for prohibited basis groups.
No conspicuous gaps in lending patterns.	Explainable conspicuous gaps in lending patterns.	Unexplainable conspicuous gaps in lending.
Centralized underwriting and makes own loans.	Local brokers originate a low volume of loans.	Decentralized underwriting and high volume of loans originated by multiple statewide or nationwide brokers.
No marketing practices or products that are targeted to any specific group or location.	Limited marketing practices or products that are targeted to specific groups or locations. Activity is commensurate with strategic focus.	Marketing practices or products are targeted to specific groups or locations, (e.g., advertising sub-prime or higher cost consumer loans in a language other than English).

[59] Refer to 15 USC 1691 et seq., 42 USC 3601 et seq., 12 CFR 1002, and 24 CFR 100-110, "Fair Housing." (Footnote updated in version 1.1)

Quantity of Fair Lending Risk Indicators		
Low	**Moderate**	**High**
No fair lending complaints or complaints to the U.S. Departments of Justice or Housing and Urban Development regarding discrimination or discouraged applications.	Limited number of fair lending-related complaints.	Numerous fair lending-related complaints.
No fair lending lawsuits or claims regarding discrimination or discouraged applicants.	Community groups have raised fair lending issues. Some potential lawsuits (e.g., allegations of predatory lending).	Actual fair lending lawsuits or claims. Investigations of fair lending complaints by the U.S. Departments of Justice or Housing and Urban Development.
No special compensation incentives for lenders	Lenders do receive incentives for number of loans made, but activity is closely monitored.	Lenders receive incentives for number of loans made without review.

Quality of Fair Lending Risk Management Indicators

Quality of Fair Lending Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Bank conducts an effective fair lending risk assessment. Results are discussed with the board.	Bank conducts a fair lending risk assessment that is generally effective, but there may be some weaknesses in the system.	Bank conducts a fair lending risk assessment, but the system may need improvement to be fully effective.	Bank conducts little or no monitoring of compliance with fair lending laws and regulations.
Centralized decision making with ongoing monitoring for consistency. Bank adheres to well-defined underwriting standards and override procedures.	Centralized decision making, but some aspects of monitoring could be improved to achieve greater consistency. Staff generally adheres to underwriting standards and override procedures.	Decision-making processes may need greater centralization. Monitoring may be limited. Staff may not fully understand or adhere to underwriting standards and override procedures.	Decentralized decision making without monitoring of discretionary pricing, overrides, or policy exceptions.
Bank has an effective second review process in place.	Bank has a second review process, but it may have minor weaknesses in some areas.	Bank has implemented a second review process, which may have resulted in inconsistent consideration of denied applications, exceptions, or overrides.	No second review process.
Fair lending considerations are incorporated into all areas of the bank, (e.g., rollout of new products, advertising, changes in forms, disclosures, etc.).	Fair lending considerations are generally well incorporated, although a few areas may be overlooked or not fully incorporated. Management effects corrective action when the need is identified.	Fair lending considerations need improvement, as several areas may be overlooked or not incorporated. Management generally effects corrective action when weaknesses are identified.	Fair lending considerations are not incorporated in numerous areas of the bank. Management does not effect corrective action.

Quality of Fair Lending Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Policies and procedures are strong.	Policies and procedures are satisfactory, but minor weaknesses are noted.	Policies and procedures need improvement, as several weaknesses may be noted.	Policies and procedures are significantly flawed and do not provide meaningful guidance to explain why business reasons or other factors are not discriminatory.
When deficiencies are identified in the normal course of business or second review process, management promptly implements meaningful corrective action.	Management is responsive when deficiencies are identified in the normal course of business or second review process, but corrective actions may not always be fully effective.	Management is not consistently responsive when deficiencies are identified. Some deficiencies may not be self-identified.	Errors and deficiencies are not self-identified. Management may only respond when violations are cited.
Training regarding consistent treatment is appropriate and effective. Necessary resources have been provided to govern compliance. Bank has experienced, well-trained, and knowledgeable staff.	Training regarding consistent treatment is generally appropriate and effective. Resources are generally adequate to govern compliance. Overall, the staff is satisfactory in terms of its experience, training, and knowledge.	Training is conducted but may be conducted infrequently or not in a timely manner. Resources may not be adequate to govern compliance.	Training is sporadic and ineffective (as evidenced by inconsistent application of underwriting standards); high volume of withdrawn/incomplete applications may indicate bank is discouraging applicants.
Bank is responsive and resolves complaints promptly when received.	In general, complaints are promptly and adequately addressed.	Management needs to improve its monitoring of and responsiveness to complaints.	Management does not monitor or adequately and promptly address complaints.
Appropriate fair lending compliance controls and systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments) are implemented to identify compliance problems and assess performance.	No significant shortcomings are evident in fair lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). Probability of serious future violation or noncompliance is within acceptable tolerance.	Modest shortcomings are evident in fair lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). Probability of serious future violation or noncompliance may not be within acceptable risk tolerances.	Significant shortcomings are evident in fair lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). The probability of serious future violation or noncompliance is high.

Quality of Fair Lending Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Clear and objective standards exist for referring applicants to subsidiaries or affiliates, classifying applicants as prime or subprime, and deciding what alternative loan products should be offered. Standards are clearly communicated and well understood by staff.	Objective standards exist for referring applicants to subsidiaries or affiliates, classifying applicants as prime or subprime, and deciding what alternative loan products should be offered, but the standards may not be clearly communicated to staff.	Objective standards for referring applicants to subsidiaries or affiliates, classifying applicants as prime or subprime, and deciding what alternative loan products should be offered may exist for some but not all areas. Standards may not be consistently communicated to staff.	Missing clear and objective standards for referring applicants to subsidiaries or affiliates, classifying applicants as prime or subprime, or deciding what kinds of alternative loan products should be offered.

Consumer Lending Regulations Risk Indicators

The consumer lending regulations risk indicators are used for determining a bank's quantity of risk and quality of risk management regarding applicable consumer protection laws and regulations related to lending.

Quantity of Consumer Lending Regulations Risk Indicators

Examiners should use the following indicators when assessing quantity of consumer lending regulations risk.

Quantity of Consumer Lending Regulations Risk Indicators		
Low	**Moderate**	**High**
Noncomplex and stable types of products offered (e.g., fixed-rate long-term mortgages, simple consumer loans).	Limited number of complex loan products offered. Products change occasionally.	Complex loan products offered (e.g., adjustable rate mortgages, home equity lines of credit, or construction loans). Products change frequently.
Consistent, high volume of loan originations with no recently identified violations of law/regulation, indicating bank is accustomed to dealing with technical regulations.	Consistent high volume of loan originations with occasional less substantive noted.	Low level or infrequent loan originations and/or frequent violations noted.
Experienced, knowledgeable staff in key lending control positions. May be indicated by low staff turnover or frequency of training.	Experienced, knowledgeable staff in moderately critical lending control positions.	Inexperienced or untrained staff in key or high volume critical lending control positions. High turnover or infrequent training may be an indicator.
Stable software and processes with low errors in technical requirements (disclosures, notices, APRs, changes in indices, etc.).	Implementation of new software, or software conversions with some errors in technical requirements.	System conversions or software changes due to third-party changes or merger activity. Problems indicated by high level of errors in technical requirements.
Electronic banking is not offered or is limited to account inquiries.	Electronic banking is limited to nontransactional functions and is informational only. Information includes triggering terms. No on-line loan applications permitted.	Loan application and transactions accepted via the internet increasing the difficulty of delivering disclosures and makes bank more susceptible to fraud.
Marketing activities are limited to local area, stable environment, centralized.	Marketing activities are limited to standard products, decentralized channels (branches), and wider geographical area.	Active marketing of new products offered through multiple channels (internet, direct mail, solicitations, etc.).
Interest rate environment is stable.	Interest rate environment is changing, but loan volume is manageable.	Interest rate environment is unstable causing unmanageable loan volume.
Few competitors.	Multiple competitors. May result in bank offering some loan products it is not experienced in handling.	High level of competition causing increased loan volume, particularly in complex loan

Quantity of Consumer Lending Regulations Risk Indicators		
Low	**Moderate**	**High**
		products the bank is not experienced in handling.
Few or no consumer complaints are received. There is no obvious pattern as to regulation type when complaints are reviewed.	Some consumer complaints are received. There is no obvious pattern as to regulation type.	Several consumer complaints are received and may represent a pattern.
No special flood hazard areas in lending area (FDPA).	Lending area has few special flood hazard areas.	Lending area has numerous special flood hazard areas.
No broker relationship or limited broker relationships with low amount of unearned fees either paid or received (RESPA).	Moderate use of broker and moderate amount of unearned fees either paid or received.	Broker relationship coupled with high amount of unearned fee income either paid or received.
Bank does not offer products or services that require expanded, detailed regulatory compliance such as the following: • Credit cards (TILA) • Home equity loans/lines (TILA) • Consumer leases (Consumer Leasing Act)[60] • Escrow (RESPA, HPA) • Private mortgage insurance (TILA, HPA) • Required service providers (RESPA) • Controlled business arrangements	Bank may offer some products or services that require expanded, detailed regulatory compliance such as the following: • Credit cards (TILA) • Home equity loans/lines (TILA) • Consumer leases (Consumer Leasing Act) • Escrow (RESPA, HPA) • Private mortgage insurance (TILA, HPA) • Required service providers (RESPA) • Controlled business arrangements	Bank offers numerous products or services that require expanded, detailed regulatory compliance such as the following: • Credit cards (TILA) • Home equity loans/lines (TILA) • Consumer leases (Consumer Leasing Act) • Escrow (RESPA, HPA) • Private mortgage insurance (TILA, HPA) • Required service providers (RESPA) • Controlled business arrangements
Low number of consumer complaints received. No pattern as to type of complaint. Few or no substantive issues.	Moderate number of consumer complaints received without a pattern as to compliance type. Moderate number of substantive issues.	Several consumer complaints are received and may represent a pattern. Significant number of substantive issues. The OCC's Customer Assistance Group has notified the supervisory office.
Bank does not provide disclosures electronically.	Bank provides electronic and paper disclosures. Staff is knowledgeable of E-Sign Act, and there is effective consumer opt-in as required by the act.	Bank only provides disclosures electronically. Staff has some knowledge of E-Sign Act. Effective consumer opt-in, as required by the act, is inconsistent.
No loans subject to the SCRA and the MLA.	Some loans subject to the SCRA and the MLA.	Significant number of loans subject to the SCRA and the MLA.

[60] Refer to 15 USC 1667 et seq., "Consumer Leases," and 12 CFR 1013, "Consumer Leasing (Regulation M)." (Footnote added in version 1.1)

Quality of Consumer Lending Regulations Risk Management Indicators

Examiners should use the following indicators when assessing quality of consumer lending regulations risk management.

Quality of Consumer Lending Regulations Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Management fully understands all aspects of lending compliance risk and exhibits clear commitment to compliance. Commitment is communicated throughout affected areas of the institution.	Management reasonably understands the key aspects of lending compliance risk. Commitment to lending compliance is reasonable and satisfactorily communicated throughout affected areas of the institution.	Management has a marginal understanding of key aspects of lending compliance risk. The importance of compliance may not be adequately emphasized or consistently communicated throughout the affected areas of the institution.	Management does not understand or has chosen to ignore key aspects of lending compliance risk. Importance of lending compliance is not emphasized or communicated throughout affected areas of the institution.
Authority and accountability for lending compliance are clearly defined and enforced.	Authority and accountability for lending compliance are defined, although some refinements may be needed.	Authority and accountability for lending compliance may not be clearly defined or communicated.	Management has not established or enforced accountability for lending compliance performance.
Management anticipates and responds well to changes of a market, technological, or regulatory nature that affect lending regulations compliance.	Management adequately responds to changes of a market, technological, or regulatory nature that affect lending regulations compliance.	Management may not consistently respond to changes of a market, technological, or regulatory nature that affect lending regulations compliance.	Management does not anticipate or take timely or appropriate actions in response to changes of a market, technological or regulatory nature that affect lending regulations compliance.
Lending compliance considerations are incorporated into products and system development processes, including changes made by third parties or affiliates.	Lending compliance considerations may not always be formally considered when developing products and systems, although issues are typically addressed before products and systems are fully implemented.	Lending compliance considerations may not be consistently considered when developing products and systems. Issues may not be addressed before products and systems are fully implemented.	Lending compliance considerations are not incorporated into product and systems development.
When lending compliance deficiencies are identified, management promptly implements meaningful corrective action.	Lending compliance problems can be corrected in the normal course of business without a significant investment of money or management attention. Management is responsive when lending deficiencies are identified.	Lending compliance problems may require a greater degree of management attention and may not have been self-identified. Management may not consistently respond to identified lending compliance deficiencies.	Lending compliance errors are often not detected internally, corrective action is often ineffective, or management is unresponsive.

Quality of Consumer Lending Regulations Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Appropriate lending compliance controls and systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments) are implemented to identify compliance problems and assess performance.	Lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments) do not indicate any shortcomings of significance, although minor enhancements may be required. Probability of serious future violations or noncompliance is within acceptable tolerance.	Lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments) may indicate some shortcomings. Probability of serious future violations or noncompliance may not be within acceptable tolerance.	Significant deficiencies are evident in lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). Likelihood of continued lending compliance violations or noncompliance is high because a corrective action program does not exist, or extended time is needed to implement such a program.
Lending compliance training programs are effective, and the necessary resources have been provided to appropriate personnel.	Management provides adequate resources and training for compliance.	Management may not provide sufficient resources and training for compliance in all areas.	Management has not provided resources or training for compliance with lending regulations, or the resources or training provided are inadequate.
Compliance risk management processes and information systems are sound, and the bank has a strong control culture that has proven effective for lending compliance.	Compliance risk management processes and information systems are adequate to avoid significant or frequent violations or noncompliance with lending regulations.	Compliance risk management processes and information systems may not be sufficient to avoid significant or frequent violations or noncompliance with lending regulations.	Compliance risk management processes and information systems are deficient in identifying violations and noncompliance with lending regulations.
Effective control systems are in place to assure maintenance of flood insurance throughout the loan term. This includes an effective mechanism to force placement of flood insurance if necessary. (FDPA)	Control systems are in place to detect the expiration of insurance, but there is not a fully effective mechanism to provide for the timely forced placement of insurance (gaps in insurance can occur).	Control systems to detect the expiration of insurance and mechanisms to provide for timely forced placement of insurance need improvement.	Bank does not have an effective control system to detect the expiration of flood insurance or there is no mechanism to provide for the timely forced placement of insurance.
Control systems are effective to collect and accurately report all HMDA and CRA loans.	Control systems do not capture all loans or there are errors. Bank's internal control systems found data errors and corrected them.	Control systems do not capture all loans or there may be some errors. Bank's internal control systems may not consistently find and correct data errors.	Control systems are not capturing a significant percentage of loans or entire categories of loans. Bank does not have a quality control system to detect errors.

Quality of Consumer Lending Regulations Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
HMDA or Fair Housing Home Loan Data (FHHLD) system data are evaluated quarterly for trends and accuracy.	HMDA or FHHLD system data may not be consistently evaluated for trends, but accuracy is reviewed quarterly.	HMDA or FHHLD system data may not be evaluated for trends or consistently reviewed for accuracy.	HMDA or FHHLD system data are not evaluated for trends or reviewed for accuracy until prepared for submission to the FFIEC.

Consumer Deposit Regulations Risk Indicators

The consumer deposit regulations risk indicators are used to assess a bank's quantity of risk and quality of risk management regarding applicable consumer protection laws and regulations related to deposit accounts.

Quantity of Consumer Deposit Regulations Risk Indicators

Examiners should use the following indicators when assessing quantity of consumer deposit regulations risk.

Quantity of Consumer Deposit Regulations Risk Indicators		
Low	**Moderate**	**High**
Staff is experienced and knowledgeable regarding regulatory requirements that apply to their functions. Staff turnover is generally low.	Staff is generally experienced and knowledgeable regarding regulatory requirements that apply to their functions. Some turnover is identified.	Staff is inexperienced or is not knowledgeable regarding regulatory requirements that apply to their functions. Turnover may be high.
Noncomplex products are offered. Product types are stable. (Regulations D, DD, CC, and E)	Limited number of complex products is offered. Product types change occasionally. (Regulations. D, DD, CC, and E)	Several complex deposit products offered (e.g., index-powered certificates of deposit, tiered rate, stepped-rate). Product types change frequently. (Regulations D, DD, CC, and E)
Electronic banking is not offered or is limited to account inquiries. (Regulations D and DD)	Electronic banking is limited to nontransactional functions and is informational only (which may trigger Regulation DD advertising requirements). No account opening permitted. (Regulations. D and DD)	Accounts can be opened via the internet and transactions conducted (account-to-account transfers, electronic bill payment, etc.). (Regulations D, DD, CC, and E)
Marketing activities are limited to local area, stable environment, centralized. (Regulation DD)	Marketing activities are limited to standard products, decentralized channels (individual branches or lines of business). (Regulation DD)	Active marketing of new products offered through multiple channels (internet, direct mail, etc.). (Regulation DD)
Interest rate environment is stable. (Regulation DD)	Interest rate environment is unstable, but volume is manageable. (Regulation DD)	Interest rates are unstable. May result in rapid shift in demand for certain products (Regulation DD). May indicate a need for further disclosures to the consumer.
Few competitors. (Regulation DD)	Multiple competitors. May result in the bank developing more complex products. (Regulation DD)	High level of competition. May result in the bank offering premiums or bonuses for deposit products. (Regulation DD)

Quantity of Consumer Deposit Regulations Risk Indicators		
Low	**Moderate**	**High**
Tested and proven software and processes are in use. Few if any errors regarding technical requirements (disclosures, notices, APYs, etc.) are noted. (Regulations DD, CC, D, and E)	New software has been implemented, or software conversions have taken place. Some errors regarding technical requirements are noted. (Regulations DD, CC, D, and E)	System conversions or software changes have been implemented due to third-party changes or merger activity. Numerous errors regarding technical requirements are noted. (Regulations DD, CC, D, and E)
Next-day availability of deposits across the board. Few exception holds. (Regulation CC)	Case-by-case, new account and large deposit exceptions occur occasionally. Deposit holds are done infrequently. (Regulation CC)	Holds are placed frequently. (Regulation CC)
Low number of customer complaints received. No pattern as to type of complaint. Few or no substantive issues. (Updated in version 1.1)	Moderate number of customer complaints received without a pattern as to compliance type. Moderate number of substantive issues. (Updated in version 1.1)	Several customer complaints are received and may represent a pattern. Significant number of substantive issues. (Updated in version 1.1)
Access devices are not offered or are limited to ATM cards. (Regulation E)	Access devices such as ATM and debit cards are offered. Multiple channels may be available. (Regulation E)	Bank's ATM network may be extensive. Access devices such as ATM and debit cards are offered. Multiple channels may be available. (Regulation E)
Bank does not offer money market deposit accounts (MMDA) or negotiable order of withdrawal (NOW) accounts. (Regulation D)[61]	MMDA and/or NOW accounts may be offered as permitted by regulation. (Regulation D)	MMDA and/or NOW accounts are offered. NOW accounts may not be limited to consumers only. (Regulation D)
Bank does not provide disclosures electronically.	Bank provides both electronic and paper disclosures. Staff is knowledgeable of E-Sign Act,[62] and there is effective consumer opt-in as required by the act.	Bank provides disclosures electronically only. Staff has some knowledge of the E-Sign Act. Effective consumer opt-in, as required by the act, is inconsistent.

Quality of Consumer Deposit Regulations Risk Management Indicators

Examiners should use the following indicators when assessing quality of consumer deposit regulations risk management.

[61] Refer to 12 CFR 204, "Reserve Requirements of Depository Institutions (Regulation D)." (Footnote added in version 1.1)

[62] Refer to 15 USC 7001 et seq., "Electronic Signatures in Global and National Commerce." (Footnote added in version 1.1)

Quality of Consumer Deposit Regulations Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Management fully understands all aspects of deposit compliance risk and exhibits clear commitment to compliance. Importance of deposit compliance is emphasized and communicated throughout the organization.	Management reasonably understands key aspects of deposit compliance risk. Commitment to deposit compliance is reasonable and satisfactorily communicated.	Management may not fully understand some key aspects of deposit compliance risk. Commitment to deposit compliance may not be reasonable or satisfactorily communicated.	Management does not understand key aspects of deposit compliance risk. Commitment to deposit compliance is nonexistent or ineffectively communicated.
Authority and accountability for deposit compliance is clearly defined and enforced.	Authority and accountability for deposit compliance is defined, although some refinements are needed.	Authority and accountability for deposit compliance is not fully defined and needs improvement.	Management has not established accountability for deposit compliance performance.
Management anticipates and responds well to changes of a market, technological, or regulatory nature that affect deposit regulations compliance.	Management adequately responds to changes of a market, technological, or regulatory nature that affect deposit regulations compliance.	Management's response to changes of a market, technological, or regulatory nature that affect deposit regulations compliance needs improvement.	Management does not anticipate or take timely or appropriate actions in response to changes of a market, technological, or regulatory nature that affect deposit regulations compliance.
Deposit compliance considerations (APYs, periodic statements, deposit holds, MMDA withdrawals/transfers, etc.) are proactively incorporated into products and system development and modification processes, including changes made by third parties. (Regulations DD, E, CC, and D)	Deposit compliance is considered when developing products and systems. Issues are typically addressed before products and systems are fully implemented.	Deposit compliance is not consistently considered when developing products and systems, and issues may not be addressed before products and systems are fully implemented.	Deposit compliance considerations are not incorporated into product and systems development.
When deposit compliance deficiencies are identified, management promptly implements meaningful corrective action. These include responding to customer complaints and resolving electronic funds transfer errors.	Deposit compliance problems can be corrected in the normal course of business without a significant investment of money or management attention. Management is responsive when deposit issues are identified.	Deposit compliance errors are not consistently detected internally, corrective action may be ineffective, or management may be unresponsive.	Deposit compliance errors are not detected internally, corrective action is ineffective, or management is unresponsive.

Quality of Consumer Deposit Regulations Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Appropriate deposit compliance controls and systems (e.g., quality control functions, compliance reviews, compliance audits, self-assessments) are implemented to identify compliance problems and assess performance.	No shortcomings of significance are evident in deposit compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). The probability of serious future violations or noncompliance is within acceptable tolerance.	Some shortcomings are evident in deposit compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). The probability of serious future violations or noncompliance may not be within acceptable tolerance.	Likelihood of continued deposit compliance violations or noncompliance is high because a corrective action program does not exist, or extended time is needed to implement such a program.
Deposit compliance training programs are effective, and the necessary resources have been to appropriate personnel.	Management provides adequate resources and training, given the complexity of products and operations, for compliance with deposit regulations.	Management does not consistently provide adequate resources and training, given the complexity of products and operations, for compliance with deposit regulations.	Management has not provided adequate resources or training for compliance with deposit regulations.
Compliance risk management processes and information systems are sound, and the bank has a strong control culture that has proven effective for deposit compliance.	Compliance risk management processes and information systems are adequate to avoid significant or frequent violations or noncompliance with deposit regulations.	Compliance risk management processes and information systems may need improvement to avoid significant or frequent violations or noncompliance with deposit regulations.	Compliance risk management processes and information systems are deficient.

Other Consumer Protection Regulations Risk Indicators

The other consumer protection regulations risk indicators are used to assess a bank's quantity of risk and quality of risk management regarding applicable consumer protection laws and regulations that are not directly related to lending or deposit accounts.

Quantity of Other Consumer Protection Regulations Risk Indicators

Examiners should use the following indicators when assessing quantity of other consumer protection regulations risk.

Quantity of Other Consumer Protection Regulations Risk Indicators		
Low	**Moderate**	**High**
Bank does not share customer information with affiliates and non-affiliates outside of the regulatory exceptions contained in 12 CFR 1016 (Privacy)	Bank shares limited customer information with affiliates and non-affiliates.	Bank actively shares customer information with affiliates and non-affiliates.
Bank does not disclose information to nonaffiliated third parties outside the statutory exceptions, and an opt-out election is therefore not necessary. (Privacy)	Bank discloses information to nonaffiliated third parties outside the statutory exceptions. Consumers are provided a reasonably clear and conspicuous opt-out notice and a generally reasonable means to do so. Bank has devised a generally effective means to record, maintain, and effectuate opt-out election by consumers.	Bank discloses information to nonaffiliated third parties outside the statutory exceptions. Consumers are either not provided with an opt-out notice or it is not clear and conspicuous. It is difficult for consumers to submit the notice. Bank either has not devised a means to record, maintain, and effectuate opt-out election by consumers or it is not effective.
Bank has no relationships with nonaffiliated entities. (Privacy)	Bank has relationships with a limited number of nonaffiliated entities.	Bank has relationships with a large number of nonaffiliated entities.
Bank does not report credit information on its customers other than to a consumer-reporting agency. (Fair Credit Reporting Act)[63]	Bank provides credit information on its customers to their holding companies or affiliates as permitted by the law.	Bank routinely provides credit information on its customers to other creditors or correspondents to market new products.
Bank has not received requests from government agencies for information related to customers' financial records. (Right to Financial Privacy Act)	Bank has received limited requests from government agencies for customers' financial records.	Bank has received a significant number of requests from government agencies for customers' financial records.

[63] Refer to 15 USC 1681 et seq., "Credit Reporting Agencies," and 12 CFR 1022, "Fair Credit Reporting (Regulation V)." (Footnote added in version 1.1)

Quantity of Other Consumer Protection Regulations Risk Indicators		
Low	**Moderate**	**High**
Bank does not operate a website or online service directed to children younger than 13 or does not have actual knowledge that it is collecting or maintaining personal information from a child online. (COPPA).	Bank's website may collect information from children younger than 13 but does not have a Federal Trade Commission-approved program.	Bank's website collects information from children younger than 13. Bank participates in a Federal Trade Commission-approved, self-regulatory program, and independent review/audit has verified bank's compliance with the program.
Bank does not market products or services via email or telephone (CAN-SPAM,[64] TCPA).[65]	Bank may market products or services via email or telephone, but its program does not meet all requirements of CAN-SPAM or the TCPA.	Bank markets products or services via email or telephone. It does not have controls for, or a process to review, compliance with requirements of CAN-SPAM or the TCPA.
Bank does not regularly collect consumer debts for another person or institution or use any name other than its own when collecting consumer debts and is therefore not a "debt collector." (Fair Debt Collection Practices Act)	Bank occasionally acts as a "debt collector."	Bank frequently acts as a "debt collector."

Quality of Other Consumer Protection Regulations Risk Management Indicators

Examiners should use the following indicators when assessing quality of other consumer protection regulations risk management.

Quality of Other Consumer Protection Regulations Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Management has effective privacy and marketing policies that accurately reflect the operations of the bank. (Privacy, CAN-SPAM, TCPA)	Management has privacy and marketing policies that adequately reflect the operations of the bank.	Management has privacy and marketing policies that do not fully reflect the operations of the bank.	Management does not understand or has chosen to ignore key aspects of risk within the privacy regulation. Privacy and marketing policies are ineffective and do not reflect the operations of the bank.
Bank has implemented a comprehensive, board-approved written information security	Bank has implemented an adequate, board-approved written information security	Bank has implemented a board-approved written information security program that may not	Bank has not implemented a written information security program or does not

[64] Refer to 15 USC 7707 et seq., "Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003," and 16 CFR 316, "CAN-SPAM Rule." (Footnote added in version 1.1)

[65] TCPA is the Telephone Consumer Protection Act of 1991. Refer to 47 USC 227, "Restrictions on Use of Telephone Equipment." (Footnote added in version 1.1)

Quality of Other Consumer Protection Regulations Risk Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
program that conforms with section 501(b) of the Gramm–Leach–Bliley Act (GLBA). (Privacy)	program that generally conforms with section 501(b) of GLBA but could be enhanced.	fully conform to with section 501(b) of GLBA.	conform with section 501(b) of GLBA.
Compliance actively monitors to confirm that the bank does not report credit information on its customers other than to a consumer-reporting agency. (Fair Credit Reporting Act)	Compliance adequately monitors to confirm that the bank does not report credit information on its customers other than to a consumer-reporting agency.	Compliance needs to improve monitoring to confirm that the bank does not report credit information on its customers other than to a consumer-reporting agency.	Compliance does not monitor to confirm that the bank does not report credit information on its customers other than to a consumer-reporting agency.
Bank has an effective system to appropriately respond to requests for information related to customer's financial records from government agencies. (Right to Financial Privacy Act)	Bank has an adequate control system to appropriately respond to requests for information from government agencies. Control system may not be fully implemented.	Bank needs to improve its control system to appropriately respond to requests for information from government agencies.	Bank does not have a control system in place to appropriately respond to requests for information related to customers' financial records from government agencies.
Training related to privacy and marketing laws and regulations is effective, and resources have been provided to personnel.	Management provides adequate resources and training given the complexity of products and operations for compliance with privacy and marketing laws and regulations.	Management needs to improve resources and training given the complexity of products and operations for compliance with privacy and marketing laws and regulations.	Management has not provided resources or training for compliance with privacy and marketing laws and regulations.
Authority and accountability for privacy and marketing compliance is clearly defined and enforced.	Authority and accountability for privacy and marketing compliance are defined, although some enhancements may be needed.	Authority and accountability for privacy and marketing compliance may not be clearly defined and improvements are needed.	Management has not established or enforced accountability for privacy and marketing compliance performance.
Bank either has not received any customer complaints or, if it has, the complaint resolution process is timely and complete. (Updated in version 1.1)	Bank responds to customer complaints in a generally timely and complete manner. (Updated in version 1.1)	Bank does not consistently respond to customer complaints in a timely and complete manner. (Updated in version 1.1)	Bank either does not respond to customer complaints, or does so after an extended period of time. Responses are inadequate. (Updated in version 1.1)
Appropriate compliance controls and systems (e.g., quality control functions, compliance audits, and self-assessments) are implemented to identify compliance problems and assess performance.	No shortcomings of significance are evident in compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). Probability of serious future violations or noncompliance is within acceptable tolerance.	Some shortcomings are evident in compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). Probability of serious future violations may not be within acceptable tolerance.	Likelihood of continued compliance violations or noncompliance is high because a corrective action program does not exist, or extended time is needed to implement such a program.

Asset Management Risk Indicators

Quantity of Asset Management Risk Indicators

Examiners should use the following indicators when assessing quantity of asset management risk.

Quantity of Asset Management Risk Indicators		
Low	**Moderate**	**High**
Amount of capital allocated to asset management is low and insignificant in relation to total capital.	Substantial amount of capital is allocated to asset management but still not high in relation to total capital.	Amount of capital allocated to asset management is substantial and significant in relation to total capital.
Asset management revenue or operating profit is insignificant in relation to the bank's overall revenue or operating profit.	Asset management revenue or operating profit is an important contributor to the bank's total revenue or operating profit.	Asset management revenue or operating profit is a substantial contributor to the bank's total revenue or operating profit.
Asset management accounts administered and/or managed are mostly noncomplex and small in size.	Asset management accounts administered and/or managed may be complex and large in size.	Significant number of asset management accounts administered and/or managed are complex and large in size.
Asset management products and services are provided in a limited number of locations or branches in one state.	Asset management products and services are provided in locations or branches in more than one state.	Asset management products and services are provided in multiple locations or branches in multiple states.
Asset management account growth is low and stable, and usually below management expectations. New product volume is low.	Asset management account growth is significant and generally meets or exceeds management expectations. New product volume is high.	Asset management account growth is significantly above management expectations. New product volume is significant and complex.
Transaction volume of asset management accounts is not significant, and the probability of significant loss from errors, disruptions, or fraud is minimal.	Transaction volume of asset management accounts is substantial, but the probability of significant loss from errors, disruptions, or fraud is acceptable.	Transaction volume of asset management accounts is substantial, and the probability of significant loss from errors, disruptions, or fraud is high.
Compliance with applicable laws and regulations is good and the potential for noncompliance is minimal. Identified violations are quickly and effectively corrected.	Compliance with applicable laws and regulations is satisfactory, but compliance can be improved. Identified violations are normally corrected in a satisfactory manner.	Compliance with applicable laws and regulations is unsatisfactory and the potential for additional noncompliance is high. Identified violations are not corrected in a timely and effective manner.
Financial losses from asset management are low relative to allocated capital.	Financial losses from asset management are moderate relative to allocated capital.	Financial losses from asset management are high relative to allocated capital.
Volume and significance of litigation related to asset management is minimal.	Volume and significance of litigation related to asset management is satisfactory, but increasing.	Volume and significance of litigation related to asset management is high and increasing.

Quantity of Asset Management Risk Indicators		
Low	**Moderate**	**High**
Volume and significance of complaints by clients is minimal.	Volume and significance of complaints by clients is satisfactory but increasing.	Volume and significance of complaints by clients is high and increasing.
Compliance with internal bank asset management related policies and procedures is good and the potential for significant noncompliance is minimal.	Compliance with internal bank asset management related policies and procedures is satisfactory, but unauthorized policy exceptions exist and policy compliance can be improved.	Compliance with internal bank asset management related policies and procedures is unsatisfactory and potential for additional noncompliance is high.
Asset management related audit findings are usually good. The type and volume of audit exceptions are minor. Audit deficiencies are quickly and effectively corrected.	Asset management related audit typically identifies a moderate level of exceptions that require a higher level of management involvement. Audit deficiencies are normally corrected in a satisfactory manner.	Asset management related audit typically identifies a high level of exceptions that require a significant senior management involvement. Audit deficiencies are not corrected in a timely and effective manner.

Quality of Risk Management for Asset Management Indicators

Examiners should use the following indicators when assessing quality of risk management for asset management activities.

Quality of Risk Management for Asset Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
Strategic planning processes fully incorporate asset management. Asset management strategic planning and financial budgeting processes are sound.	Strategic planning processes include asset management. Asset management strategic planning and financial budgeting processes are adequate but could be enhanced.	Strategic planning processes include asset management. Asset management strategic planning and financial budgeting processes need improvement.	Strategic planning processes do not include asset management. Asset management financial budgeting processes are inadequate and ineffective.
Board has adopted asset management policies that are fully consistent with business strategies and risk appetite.	Board has adopted asset management policies that are generally consistent with business strategies and risk appetite.	Board has adopted asset management policies that are not sufficiently consistent with business strategies and risk appetite.	Board has adopted asset management policies that are inconsistent with business strategies and risk appetite.
Asset management is well organized with clear lines of authority and responsibility for monitoring adherence to policies, procedures, and controls.	Asset management is adequately organized. Lines of authority and responsibility have been established but could be enhanced.	Asset management organization needs improvement. Lines of authority and responsibility may not be clear.	Asset management is poorly organized. Clear lines of authority and responsibility have not been established.
Board has employed a strong asset management team. Management is competent, experienced, and knowledgeable of	Board has employed a satisfactory asset management team. Management is competent, experienced,	Board has employed an adequate asset management team. Management may need additional experience or	Board has employed an inadequate asset management team. Management is inexperienced and

Quality of Risk Management for Asset Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
business strategies, policies, procedures, and control systems.	and knowledgeable in most areas.	knowledge in some areas.	may not be competent. Inadequate knowledge of asset management business.
Processes effectively identify, approve, track, report, and correct significant asset management-related policy and control exceptions.	Processes generally identify, approve, track, report, and correct significant asset management-related policy and control exceptions. Processes could be enhanced.	Processes do not consistently identify, approve, track, report, and correct significant asset management related-policy and control exceptions.	Processes do not identify, approve, track, report, and correct significant asset management-related policy and control exceptions.
Staffing levels and expertise are strong for the size and complexity of the asset management business.	Staffing levels and expertise are adequate for the size and complexity of the asset management business.	Staffing levels and expertise need improvement given the size and complexity of the asset management business.	Staffing levels and expertise are inadequate for the size and complexity of the asset management business.
Personnel policies, practices, and training programs related to asset management are reasonable and sound.	Personnel policies, practices, and training programs related to asset management are satisfactory, with only minor enhancements needed.	Personnel policies, practices, and training programs related to asset management may need improvement in some areas.	Personnel policies, practices, and training programs related to asset management are deficient and ineffective.
Policies and controls to prevent and detect inappropriate conflicts of interest and self-dealing are comprehensive and effective.	Policies and controls to prevent and detect inappropriate conflicts of interest and self-dealing are adequate and generally effective.	Policies and controls to prevent and detect inappropriate conflicts of interest and self-dealing need improvement to be fully effective.	Policies and controls to prevent and detect inappropriate conflicts of interest and self-dealing are inadequate and ineffective.
Management and the board receive comprehensive information reports to manage asset management risk.	Management and the board receive adequate information reports. Content or timeliness could be enhanced.	Management and the board do not consistently receive adequate information reports. Content or timeliness needs to be improved.	Management and the board either do not receive information reports to manage asset management risk or the reports they receive have ineffective content and/or are not timely.
Management uses legal counsel appropriately and effectively.	Management uses legal counsel in an adequate and generally effective manner.	Management does not consistently use legal counsel effectively.	Management’s use of legal counsel is ineffective.
Risks from new asset management products and services, strategic initiatives, or acquisitions are well controlled and understood. Products and services are thoroughly researched, tested, and	Risks from new asset management products and services, strategic initiatives, or acquisitions are adequately controlled and understood. Products and services are researched, tested, and approved before	Risks from new asset management products and services, strategic initiatives, or acquisitions may not be adequately controlled and understood. Products and services may not be sufficiently researched,	Risks from new asset management products and services, strategic initiatives, or acquisitions are inadequately controlled and understood. Products and services are

Quality of Risk Management for Asset Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
approved before implementation.	implementation, but processes could be enhanced.	tested, and approved before implementation, and processes need to be improved.	inadequately researched, tested, and approved before implementation.
Asset management compliance program is comprehensive and effective.	Asset management compliance program is adequate and generally effective.	Asset management compliance program needs improvement to be effective.	Asset management compliance program is deficient and ineffective.
Account acceptance and administration processes are strong and effective.	Account acceptance and administration processes are adequate and generally effective.	Account acceptance and administration processes need improvement to be effective.	Account acceptance and administration processes are deficient and ineffective.
Processes to develop, approve, implement, and monitor client investment policies, including performance measurement, are comprehensive and effective.	Processes to develop, approve, implement, and monitor client investment policies, including performance measurement, are adequate and generally effective.	Processes to develop, approve, implement, and monitor client investment policies, including performance measurement, need improvement to be effective.	Processes to develop, approve, implement, and monitor client investment policies, including performance measurement, have significant deficiencies and are ineffective.
Processes to analyze, acquire, manage, and dispose of client portfolio assets are comprehensive and effective.	Processes to analyze, acquire, manage, and dispose of client portfolio assets are adequate and generally effective.	Processes to analyze, acquire, manage, and dispose of client portfolio assets need improvement to be effective.	Processes to analyze, acquire, manage, and dispose of client portfolio assets have significant deficiencies and are ineffective.
Policies and procedures for the selection and monitoring of third parties, including investment managers and advisors, are comprehensive and effective.	Policies and procedures for the selection and monitoring of third parties, including investment managers and advisors, are adequate and generally effective.	Policies and procedures for the selection and monitoring of third parties, including investment managers and advisors, need improvement to be effective.	Policies and procedures for the selection and monitoring of third parties, including investment managers and advisors, have significant deficiencies and are ineffective.
Management fully understands technology risks and has readily available expertise to evaluate technology-related issues.	Management generally understands technology risks and has reasonable access to expertise on technology-related issues.	Management may not fully understand all technology risks and may not have reasonable access to expertise on technology-related issues.	Management does not understand technology risks and does not have or use available expertise on technology-related issues.
Management effectively anticipates and responds to risks associated with operational changes, systems development, and emerging technologies.	Management adequately anticipates and responds to risks associated with operational changes, systems development, and emerging technologies.	Management does not consistently anticipate and respond to risks associated with operational changes, systems development, and emerging technologies.	Management does not anticipate and respond to risks associated with operational changes, systems development, and emerging technologies.
Management provides continuous and reliable	Management provides continuous and reliable	Management may not adequately provide	Management does not provide continuous

Quality of Risk Management for Asset Management Indicators			
Strong	**Satisfactory**	**Insufficient**	**Weak**
operating systems, including financial and operational services provided by third parties. Contingency planning is comprehensive and frequently tested.	operating systems, including financial and operational services provided by third parties, but occasional disruptions occur. Contingency planning is adequate but could be enhanced.	continuous and reliable operating systems, including financial and operational services provided by third parties, and occasional disruptions occur. Contingency planning needs improvement.	and reliable operating systems, including financial and operational services provided by third parties. Significant disruptions occur, and contingency planning is nonexistent or ineffective.
Asset management audit program is suitable and effective. Oversight by the board and management is strong.	Asset management audit program is satisfactory but could be enhanced. Oversight by the board and management is adequate.	Asset management audit program needs to be improved. Oversight by the board and management needs improvement.	Asset management audit program is significantly deficient. Oversight by the board and management is deficient and ineffective.

Community Bank Internal Controls and Audit Assessment Factors

Community Bank Internal Controls Assessment Factors

A system of internal controls includes the systems, policies, procedures, and processes effected by the board, bank management, and other personnel to safeguard bank assets, limit or control risks, and achieve the bank's objectives. (Updated in version 1.1)

Summary Conclusion

(Section updated in version 1.1)

Conclusions from the core assessment allow examiners to assess internal controls.

The overall system of internal control is:

☐ **Strong**	☐ **Satisfactory**	☐ **Insufficient**	☐ **Weak**

Examiners use the following definitions to assess internal controls. It is not necessary to meet every attribute to be accorded a specific assessment. These key attributes are normally present to distinguish between assessments, but examiners need to factor in the bank's size, the nature of its activities, and its risk profile to arrive at an overall assessment.

Strong

The board and senior management have established an organizational culture that provides for strong internal controls and appropriate standards and incentives for ethical and responsible behavior. The system of internal controls allows the bank to achieve objectives in operational effectiveness and efficiency and provides for reliable financial reporting, safeguarding of assets and information, and compliance with applicable laws and regulations. Controls are effective in limiting operational losses, and new controls are implemented in a timely manner in areas found to have deficiencies. The organization has an effective process in place to ensure that controls as described in its policy and procedures manuals are operating effectively, and these controls are periodically reviewed through a self-assessment and an independent evaluation. Follow-up is required when internal and external auditors and regulatory agencies recommend improvements to the system of internal controls, and that follow-up is timely and appropriate.

Satisfactory

The board and senior management have established an organizational culture that provides for adequate internal controls and appropriate standards and incentives for ethical and responsible behavior. The system of internal controls generally allows the bank to achieve objectives in operational effectiveness and efficiency and provides for reliable financial reporting, safeguarding of assets and information, and compliance with applicable laws and regulations. Controls are effective in limiting operational losses, and new controls are implemented in a timely manner in areas found to have deficiencies. The organization has an adequate process in place to ensure that controls as described in its policy and procedures manuals are applied. A periodic self-assessment or independent evaluation of internal controls may have minor deficiencies. The organization follows up when internal and external auditors and regulatory agencies recommend improvements to the system of internal controls.

Insufficient

The organization ascribes some importance to an adequate control environment, and the board supports that environment. The organization's culture generally provides for adequate internal controls and appropriate ethical and responsible behavior. The system of internal controls, however, may not provide for reliable financial reporting, safeguarding of assets and information, and compliance with applicable laws and regulations in all areas. Controls implemented may not fully remediate deficiencies found. The organization's process to ensure that controls as described in its policy and procedures manuals are applied may have weaknesses or may not have been fully implemented in all areas. A periodic self-assessment or independent evaluation of internal controls may have significant deficiencies in specific areas. The organization generally follows up when internal and external auditors and regulatory agencies recommend improvements to the system of internal controls, but actions taken may not be completed in a timely manner or may not be fully effective.

Weak

The organization does not ascribe to or otherwise sufficiently emphasize the importance of an adequate control environment, and the board provides marginal support and oversight for such an environment. The organization's culture does not consistently provide for adequate internal controls and appropriate and responsible behavior. The system of internal controls does not completely provide for the achievement of objectives in operational effectiveness and efficiency, reliable financial reporting, safeguarding of assets and information, and compliance with applicable laws and regulations. Controls are not readily implemented in areas found to have deficiencies. The organization has an inadequate process to ensure that controls as described in its policy and procedures manuals are applied as they are meant to be applied. A periodic self-assessment or independent evaluation of internal controls may be lacking or have significant deficiencies. The organization is not pro-active, and its follow-up on identified control weaknesses is inadequate or lacks senior management commitment.

Community Bank Audit Assessment Factors

(Updated in version 1.1)

Well-planned, properly structured auditing programs are essential to effective risk management and internal controls. Effective internal and external audit programs are also a critical defense against fraud and provide vital information to the board about the effectiveness of internal control systems.

For more information, refer to the “Internal and External Audits” booklet of the *Comptroller’s Handbook*.

Summary Conclusion

Conclusions from the core assessment allow examiners to assess the audit program.

The overall audit program is:

☐ **Strong**	☐ **Satisfactory**	☐ **Insufficient**	☐ **Weak**

Examiners use the following definitions to assess the audit program. It is not necessary to meet every attribute to be accorded a specific assessment. Examiners consider the key attributes in the audit core assessment when assessing the audit program. These key attributes are normally present to distinguish between assessments, but examiners need to factor in the bank’s size, the nature of its activities, and its risk profile to arrive at an overall assessment. Examiners should also consider whether the audit program includes appropriate risk-based coverage of consumer protection-related laws and regulations, the bank’s BSA/AML/OFAC program, and compliance risk management systems.

Strong

Overall, a **strong** audit program is assigned a high level of respect, credibility, and stature in the organization that is continually confirmed by management and board attitudes, actions, and support. Audit’s role is clearly spelled out and incorporated into overall risk management, new product and service deployment, changes in strategy, and organizational and structural changes. The OCC can fully rely on the work and conclusions of the audit function.

Board or Audit Committee Oversight

The board, or its committee assigned audit oversight responsibility, is proactive in dealing with management and risk management issues in a timely manner. Reports and information submitted to the board or committee are clear and understandable in their discussions of issues, emerging risks, corrective actions, testing, and resolution of outstanding items. The board or committee maintains dialogue with internal and external auditors, regulators, and management and involves all appropriate groups in discussions on new business ventures, the potential risks involved, and planned controls. The board or committee takes an active role in reviewing and approving overall annual audit plans, for internal audit and the external audit engagement, as well as in setting expectations for the roles of both internal and external auditors and evaluating their performance under the plan. The use of external auditors is clearly defined in engagement letters.

Audit Management and Processes

Internal audit management possesses industry expertise and knowledge to match the sophistication and complexity of the bank's risk profile and operations. Audit is independent in executing audit plans and audit programs and discussing issues with the board or audit committee and regulators. Audit scopes and report findings are supported by work papers. Internal auditors address control deficiencies in a timely manner and perform thorough follow-up testing to validate corrective measures are effective. Internal audit plans are completed with minimal carry-over or have appropriately supported amendments based on significant changes in the bank's risk profile.

The internal and external audit processes are fully effective. Any outsourced or co-sourced internal audit duties or assignments are effective and appropriately managed by the bank. Audit processes include indicators and descriptions of key risks and controls in place. MIS are timely, accurate, complete, and reliable.

Responsibilities between audit and other risk management oversight functions are well delineated. If appropriate, risk and frequency models are effectively used and accurately reflect the risk posed by the bank's activities. Overall audit planning is effective and timely in addressing audit needs for low- and moderate-risk areas. Audit scopes are flexible to the extent of addressing new business lines, products, and activities, and, if appropriate, merger/acquisition situations.

Audit Reporting

Internal audit reports clearly outline the causes of problems and specifically point out management issues when present. There are few differences between bank-assigned audit assessments and examiner assessments for internal controls. Internal audit ratings, if used, are well defined and are fully effective in identifying areas where control weaknesses exist. Work paper documentation effectively supports the findings presented in the reports and the audit ratings assigned.

Internal Audit Staffing

Audit staffing and experience fully complement the level of risk undertaken by the bank. Staff turnover is minimal, and vacancies are promptly addressed and have little or no effect on internal audit plans or processes. Recruitment and training processes are effective. The audit staff possesses a high level of knowledge of the areas audited.

Satisfactory

Overall, a **satisfactory** audit program attains an adequate level of respect and stature in the organization and is generally supported by the actions of management and board. Audit's role in overall risk management and its participation in new product and service deployment, changes in strategy, and organizational and structural changes may be limited but are conducted effectively.

Board or Audit Committee Oversight

The board or audit committee is effective in its oversight of the audit program. Reports and information presented to the committee provide sufficient information and discussion of significant audit and control issues. The committee holds senior managers accountable for issues in their respective business lines. The committee understands the overall audit plans of internal audit and the engagement of external auditors and the respective roles to be performed by both internal and external auditors. The use of external auditors is clearly defined in engagement letters.

Audit Management and Processes

Internal audit management generally possesses the knowledge and experience to manage adequate internal audit operations appropriate for the bank's size, activities, and risk profile. For small community banks, the lack of internal audit management independence is mitigated by effective internal controls. Internal audits and follow-up are timely, comprehensive, independent, and effective in assessing and monitoring controls. Audit programs, processes, and information systems are generally sound and complement the control and risk management environment. Audit policies are generally effective, adhered to, and appropriate for the bank's size, complexity, and risk profile. The bank adequately manages outsourced or co-sourced internal audit duties or assignments.

Audit Reporting

Internal audit reports are clear and concise, and accurately reflect reviews of the area and the root causes of issues. Bank-assigned internal audit ratings, if used, or assessments are adequately defined. Conclusion or assessment differences with examination findings may exist but do not compromise the overall audit program. Internal audit work papers and programs support findings and conclusions.

Internal Audit Staffing

Audit staff is generally competent and experienced. The audit staff may have experienced some turnover and vacancies, but not to the extent of compromising internal audit plans and processes. Staff training is adequate.

Insufficient

Overall, an **insufficient** audit program may not be fully integrated into all aspects of the organization. The audit program may not consistently have the full support of the board and management. Some weaknesses may be present concerning audit's role in overall risk management and its participation in new product and service deployment, changes in strategy, and organizational and structural changes.

Board or Audit Committee Oversight

The board or audit committee is generally effective in its oversight of the audit program, but improvements are needed. Reports and information presented to the committee do not consistently provide sufficient information and likely require additional discussion of significant audit and control issues. The board or audit committee may not always hold senior management accountable for issues in its respective business line. The committee is involved in setting the overall audit plans and determining the respective roles of the internal and external auditors but may need to take a more active role in this process. The use of external auditors may not be clearly defined in engagement letters.

Audit Management and Processes

Internal audit management has a basic level of knowledge and experience, but it may be limited given the bank's size, activities, and risk profile, and as a result, weaknesses exist in internal audit management and processes. For small community banks, the lack of internal audit management independence may not be fully mitigated by effective internal controls. Audit policies exist and are generally effective, but they may not always be adhered to or may require enhancements or updating. Audit programs, processes, reports, and information systems are generally effective in addressing only significant control or risk issues. The bank may not adequately manage outsourced or co-sourced internal audit duties or assignments.

Audit Reporting

Internal audit reports, while accurate, do not consistently provide clear and concise reviews of the area and likely do not consistently identify the root causes of issues. Bank-assigned internal audit ratings, if used, or assessments may not be clearly defined. Conclusion or assessment differences with supervisory activity findings may exist but should not be significant. Internal audit work papers and programs generally support conclusions but may not be well organized or may require enhancement to better document and support individual findings.

Internal Audit Staffing

Audit staff is generally competent but may require additional experience and/or training given the bank's size, activities, and risk profile. The audit staff may have experienced some turnover and vacancies, and this may have temporarily compromised internal audit plans and processes. Staff training may require additional enhancement.

Weak

Overall, a **weak** audit program is one that is not an integral part of the organization, and the OCC cannot rely on the audit function's work or conclusions. The audit program does not have the full support of the board and management. Audit's role is unclear and not used in overall risk management, new product and service deployment, changes in strategy, and organizational and structural changes.

Board or Audit Committee Oversight

The board or audit committee is not effective in its oversight of the audit program. Reports and information submitted to the board or committee are insufficient or not fully understood. The board or committee fails to follow up on control and risk weaknesses noted by audit or to hold senior managers accountable for issues in their respective business lines. The board or committee has a passive role in the overall audit plan or selection of the external audit engagement and is not involved in determining the respective roles of the internal and external auditors. Engagement letters describing the work to be performed by the external auditors are nonexistent, incomplete, or not understood.

Audit Management and Processes

Weaknesses exist in internal audit management and processes, such as lack of competence or independence or inadequate scope of review, that are not mitigated by strong internal controls. Audit policies may exist but need significant enhancements in light of the bank's size, complexity, and risk profile. Audit programs, processes, reports, and information systems are generally ineffective in addressing significant control or risk issues. Outsourced or co-sourced internal audit duties or assignments are ineffective or not appropriately managed by the bank.

Audit Reporting

Internal audit rating or assessment definitions are loosely defined or nonexistent. Audit reports are unclear and do not reflect accurate conclusions or fully identify the root causes of concerns. Significant conclusion or assessment differences exist with examination findings. Internal audit program work papers, in many cases, are insufficient or do not support findings and conclusions.

Internal Audit Staffing

Audit staff is inexperienced or lacks adequate knowledge. The internal audit function is understaffed or suffers from high turnover significantly affecting internal audit plans and processes. Management has failed to maintain the staff levels needed to fully support the internal audit function. Staff training is inadequate.

Appendixes

Appendix A: Standard Request Letter

(Appendix updated in version 1.1)

This appendix is provided as a guide and should be modified as needed depending on the scope of the supervisory activity and the risk profile of the bank. The EIC should indicate which items need to be provided before the start of the supervisory activity and which will be reviewed during the on-site portion of the supervisory activity. If activities are being conducted throughout the supervisory cycle, examiners should only request the information they need to complete the current activity. The EIC is responsible for getting the general information and maintaining it in Examiner View to avoid duplicate requests to the bank.

During examination planning, the EIC should discuss obtaining the request letter information in a digital format with bank management. The following paragraph should be included in the request letter:

In order for us to prepare effectively for this supervisory activity, please provide the information listed in the attachment to this request letter in digital format and send to the designated EIC via OCC secure mail or large file transfer tool, which can be accessed by going to www.banknet.gov. When this is not possible, we request the data be faxed to a designated number at our office. For larger pieces of hard copy information and for security purposes, we request that you provide the information by mail using a "tracking" service. Please indicate whether hard copy information needs to be returned.

In addition, the request letter should include the following statement with regard to the consumer compliance portion of the examination (select the appropriate version of the text for a national bank or an FSA):

<u>Use for national banks:</u> *The consumer compliance examination is being conducted under the authority of 12 USC 481. However, it also constitutes an investigation within the meaning of section 3413(h)(1)(A) of the Right to Financial Privacy Act. Therefore, in accordance with section 3403(b) of the Act, the undersigned hereby certifies that the OCC has complied with the Right to Financial Privacy Act, 12 USC 3401, et seq. Section 3417(c) of the Act provides that good faith reliance upon this certification relieves your bank and its employees and agents of possible liability to the bank's customers in connection with the disclosure of the requested information.*

<u>Use for FSAs:</u> *The consumer compliance examination is being conducted under the authority of 12 USC 1463 and 1464. However, it also constitutes an investigation within the meaning of section 3413(h)(1)(A) of the Right to Financial Privacy Act. Therefore, in accordance with section 3403(b) of the Act, the undersigned hereby certifies that the OCC has complied with the Right to Financial Privacy Act, 12 USC 3401, et seq. Section 3417(c) of the Act provides that good faith reliance upon this certification relieves your bank and its employees and*

agents of possible liability to the bank's customers in connection with the disclosure of the requested information.

Management and Supervision

If uploading this information via the OCC's Large File Transfer, please select the "Other Safety and Soundness" folder where prompted.

1. The most recent board packet. Information included in the packet that is requested in this letter need not be duplicated.

2. Current organizational chart.

3. If changes have occurred since the last examination, a list of directors and executive management and their backgrounds, including work experience, length of service with the bank, etc. Also, a list of committees, including current membership.

4. If changes have occurred since the last examination, a list of related organizations (e.g., parent holding company, affiliates, and operating subsidiaries).

5. Brief description of new, expanded, or modified products, services, lines of business, delivery channels, or changes in the bank's market area.

6. List of third-party relationships with an indication of mission-critical third parties. Please include the following for each third-party relationship:

    - Name of servicer.
    - Contact name and phone number.
    - Brief explanation of the product(s) or service(s) provided.
    - Note of affiliate relationships with the bank or relationships with bank insiders.
    - For third-party loan originators, please indicate any changes since the prior examination.

    For example, services provided may include the servicing of loans sold in whole or in part to other entities, including the service provider. OCC examiners use this list to request trial balances or other pertinent information not otherwise requested in this letter.

7. Minutes of board and major committee meetings (e.g., Audit, Risk, Loan, Asset/Liability Management, Compliance, Fiduciary, or Technology Steering Committee) since our last examination.

8. A brief summary of corrective action taken to address MRAs and violations identified in the last examination report. Management need not provide information that has been previously provided to the OCC (e.g., during the OCC's periodic monitoring).

Audit

If uploading this information via the OCC’s Large File Transfer, please select the “Audit ERM” folder where prompted.

9. Most recent external audit and consultant reports, management letters, engagement letters, and management’s responses to findings (including audits of outside service providers, if applicable).

10. Internal audit schedule, including compliance and other separate audits, for the current year. Please note those audits that have been completed and their summary ratings, as well as those that are in process.

11. Most recent internal audit reports, including compliance and other separate audits, as well as management’s responses. Include (prior year) audit reports covering loan administration, funds management and investment activities, risk-based capital computations, BSA, information processing, and audit areas that were assigned a less than satisfactory rating.

12. A copy of risk assessments performed by management or an outside party.

Asset Quality

If uploading this information via the OCC’s Large File Transfer, please select the “Commercial Credit” folder where prompted.

13. Loan trial balance using the “Interagency Loan Data Request” format (refer to OCC news release 2013-52, “Increase in Required Electronic Loan Data Fields”), including applicable code descriptions. Please populate all key fields used in underwriting decisions.

14. List of watch, problem, past-due, and nonaccrual loans.

15. Most recent concentrations of credit reports and the results of portfolio stress testing.

16. Most recent policy, underwriting, collateral, and documentation exception reports.

17. List of insider credits (to directors, executive officers, and principal shareholders) and their related interests. The list should include terms (rates, collateral, structure, etc.). Management need not provide this information if it is captured in the loan trial balance data provided.

18. List of loan participations purchased and sold, whole loans purchased and sold, and securitization activity since the last examination.

19. List of overdrafts.

20. Most recent analysis of ALLL.

21. List of OREO, repossessed assets, classified investments, and cash items.

22. Latest loan review report, including responses from management or the board.

23. Bank's loan policy, including a list of changes since the last examination.

Financial Performance

If uploading this information via the OCC's Large File Transfer, please select the "Other Safety and Soundness" folder where prompted.

24. Most recent ALCO package.

25. Most recent reports used to monitor and manage IRR (e.g., gap planning, simulation models, and duration analysis).

26. Most recent liquidity reports (e.g., sources and uses).

27. List of investment securities purchased and sold for (current year) and (prior year). Please include amount, seller/buyer, and date of each transaction.

28. Most current balance sheet and income statement.

29. Most recent strategic plan, budget, variance reports, etc.

30. For national banks: Securities acquired based on "reliable estimates" authority in 12 CFR 1.3(i).

31. Securities acquired using the bank's lending authority.

32. Prepurchase analysis for all securities purchased since the last examination.

33. Summary of the primary assumptions used in the IRR measurement process and the source.

34. Current CFP.

35. Investment portfolio summary trial, including credit ratings.

36. List of board-approved securities dealers.

37. List of shareholders and ownership.

38. Most recent annual and quarterly shareholders' reports.

39. List of pending litigation, including a description of circumstances behind the litigation.

40. Details regarding the bank's blanket bond and other major insurance policies (including data processing-related coverage). Provide name of insurer, amount of coverage and deductible, and maturity. Also, please indicate the date of last board review and whether the bank intends to maintain the same coverage upon maturity.

41. Summary of payments to the holding company and affiliates.

42. Bank work papers for the most recent call report submitted.

IT

If uploading this information via the OCC's Large File Transfer, please select the "Bank Technology" folder where prompted.

43. List of in-house computer systems and networks. Include equipment vendor, type/version of system, operating system, number of terminals, and major applications accessed/processed. Provide schematics for networks (including local or wide area networks).

44. List of major software applications used by the bank. Include developer (in-house or third-party), individual/company responsible for maintenance, and computer system(s) where application is used. Include PC-based applications or spreadsheets that support the bank's risk-management processes (for example, internally developed gap report).

45. As applicable, contracts, financial analyses, and performance monitoring reports for third-party IT service providers.

46. Meeting minutes from IT steering committee (or similar group) since the last examination.

47. Bank and servicer plans for disaster recovery and corporate-wide business recovery, including report from most recent disaster recovery test.

48. Reports used to monitor computer activity, network performance, system capacity, security violations, and network intrusion attempts.

49. Bank policies and procedures relating to information processing or information security.

Asset Management

If uploading this information via the OCC's Large File Transfer, please select the "Asset Management" folder where prompted.

50. Asset management organizational chart and résumés of senior asset management officers hired since the last examination.

51. Bank policies and procedures relating to asset management activities.

52. Most recent management reports, including those used to monitor new and closed accounts, account investment reviews, overdrafts, financial results, etc.; exceptions; and compliance/risk information related to asset management.

53. Information on investment activities, including most recent analysis of investment performance, approved securities lists, arrangements with mutual funds, and approved brokers/dealers.

54. Information on asset management operations, including a user access report for the trust accounting system. Please make available the most recent reconcilements of general ledger, cash/demand deposit account and suspense/house accounts, and securities held at depositories.

55. Asset master list reflecting CUSIP (if applicable), description, number of units, book value, and market value for each asset. Asset master list should include unique assets such as real estate, closely held securities, and other nonmarketable assets.

56. Most recent asset management trial balance. Please include account name, account number, account type, the bank's investment authority, and market value for each account. Also identify accounts opened within the past 12 months.

Retail Sales of Nondeposit Investment Products

If uploading this information via the OCC's Large File Transfer, please select the "Asset Management" folder where prompted.

57. Information on retail sales activities, including the bank's program management statement, agreements with third parties providing retail sales services, reports used to monitor activities, employee referral programs, and complaints.

Insurance Activities

If uploading this information via the OCC's Large File Transfer, please select the "Asset Management" folder where prompted.

58. Description of the bank's insurance activities, planned changes, and client complaint information.

Consumer Compliance

If uploading this information via the OCC's Large File Transfer, please select the "Compliance" folder where prompted.

59. List of changes to the bank's compliance policies, procedures, and compliance review process since the last examination.

60. Changes in third-party relationships, contracts, or activities.

61. List of real estate secured loans originated in special flood hazard areas since the last examination.

62. List of customer complaints received since the last examination with brief descriptions.

63. Description of the bank's complaint resolution processes.

64. Copies of (1) fair lending self-assessments; (2) written analyses of the bank's home mortgage lending; and (3) information regarding credit scoring model validations and compliance with Regulation B.

65. Description of the bank's training programs and criteria for ensuring that employees receive job-appropriate compliance training.

BSA/AML Compliance

If uploading this information via the OCC's Large File Transfer, please select the "BSA" folder where prompted.

66. Board-approved BSA/AML compliance program, including compliance with 12 CFR 21.21.

67. List of products, services, customers, and geographies with a high risk for money laundering.

68. Provide an overview of your key internal controls and management information reports to detect suspicious cash activity, wire transfer activity, monetary instrument sales, and transactions involving high-risk jurisdictions.

69. List of nonresident alien accounts.

Appendix B: Abbreviations

(Appendix updated in version 1.1)

ADC	assistant deputy comptroller
AFS	available-for-sale
ALCO	asset-liability committee
ALLL	allowance for loan and lease losses
AML	anti-money laundering
APR	annual percentage rate
APY	annual percentage yield
ASC	Accounting Standards Codification
ATM	automated teller machine
BOLI	bank-owned life insurance
BSA	Bank Secrecy Act
CAMELS	capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to market risk
CAN-SPAM	Controlling the Assault of Non-Solicited Pornography and Marketing Act
CFP	contingency funding plan
CFR	Code of Federal Regulations
CFPB	Consumer Financial Protection Bureau
CIF	collective investment fund
CMP	civil money penalty
CMS	compliance management system
CMT	constant maturity Treasury
COFI	cost-of-funds index
COPPA	Children's Online Privacy Protection Act
CRA	Community Reinvestment Act
CSV	cash surrender value
CTR	currency transaction report
DTI	debt to income
EAR	earnings at risk
EFTA	Electronic Fund Transfer Act
EIC	examiner-in-charge
ERISA	Employee Retirement Income Security Act
EVE	economic value of equity
FDIC	Federal Deposit Insurance Corporation
FDPA	Flood Disaster Protection Act
FFIEC	Federal Financial Institutions Examination Council
FHHLD	Fair Housing Home Loan Data
FinCEN	Financial Crimes Enforcement Network
FINRA	Financial Industry Regulatory Authority
FSA	federal savings association
GLBA	Gramm–Leach–Bliley Act
HIDTA	high-intensity drug trafficking area
HIFCA	high-intensity financial crime area

HMDA	Home Mortgage Disclosure Act
HPA	Homeowners Protection Act
HTM	held-to-maturity
IRR	interest rate risk
IRS	Internal Revenue Service
IT	information technology
ITC	information technology, trust, and consumer compliance
ITCC	information technology, trust, consumer compliance, and Community Reinvestment Act
Libor	London Interbank Offered Rate
LTV	loan to value
MAPR	military annual percentage rate
MCBS	Midsize and Community Bank Supervision
MIS	management information systems
MLA	Military Lending Act
MMDA	money market deposit account
MRA	matter requiring attention
NIM	net interest margin
NOW	negotiable order of withdrawal
OCC	Office of the Comptroller of the Currency
OFAC	Office of Foreign Assets Control
OREO	other real estate owned
OTS	Office of Thrift Supervision
PPM	Policies and Procedures Manual
PTA	payable through accounts
RAS	risk assessment system
RESPA	Real Estate Settlement Procedures Act
RNDIP	retail nondeposit investment product
ROE	report of examination
SCRA	Servicemembers Civil Relief Act
SEC	U.S. Securities and Exchange Commission
SOC	service organization control
SVP	stable value protection
TCPA	Telephone Consumer Protection Act
TILA	Truth in Lending Act
TISA	Truth in Savings Act
UBPR	Uniform Bank Performance Report
UDAP	unfair or deceptive acts and practices
UDAAP	unfair, deceptive, or abusive acts and practices
UFIRS	Uniform Financial Institutions Rating System
UITRS	Uniform Interagency Trust Rating System
URSIT	Uniform Rating System for Information Technology
USC	U.S. Code

References

(Section updated in version 1.1)

This section includes a list of items referenced throughout this booklet. References are applicable to both national banks and FSAs unless otherwise noted.

Laws

10 USC 987, "Terms of Consumer Credit Extended to Members and Dependents: Limitations"
12 USC 4b, "Deputy Comptroller for the Supervision and Examination of Federal Savings Associations" (applies to the OCC)
12 USC 61, "Shareholders' Voting Rights; Cumulative and Distributive Voting; Preferred Stock; Trust Shares; Proxies, Liability Restrictions; Percentage Requirement Exclusion of Trust Shares" (national banks)
12 USC 161, "Reports to Comptroller of the Currency" (national banks)
12 USC 371c, "Banking Affiliates"
12 USC 371c-1, "Restrictions On Transactions With Affiliates"
12 USC 481, "Appointment of Examiners; Examination of Member Banks, State Banks, and Trust Companies; Reports" (national banks)
12 USC 1463, "Supervision of Savings Associations" (FSAs)
12 USC 1464, "Federal Savings Associations" (FSAs)
12 USC 1464(v), "Reports of Condition" (FSAs)
12 USC 1467(h), "Additional Information" (FSAs)
12 USC 1468, "Transactions With Affiliates (FSAs)
12 USC 1468b, "Powers of Examiners" (FSAs)
12 USC 1813(v), "Violation"
12 USC 1818, "Termination of Status as Insured Depository Institution"
12 USC 1818(i), "Jurisdiction and Enforcement; Penalty"
12 USC 1818(s), "Compliance With Monetary Transaction Recordkeeping and Report Requirements"
12 USC 1820(d), "Annual On-Site Examinations of All Insured Depository Institutions Required"
12 USC 1820(i), "Flood Insurance Compliance by Insured Depository Institutions"
12 USC 1831i, "Agency Disapproval of Directors and Senior Executive Officers of Insured Depository Institutions or Depository Institution Holding Companies"
12 USC 2601 et seq., "Real Estate Settlement Procedures"
12 USC 2801 et seq., "Home Mortgage Disclosure"
12 USC 3401 et seq., "Right to Financial Privacy"
12 USC 4001 et seq., "Expedited Funds Availability"
12 USC 4301 et seq., "Truth in Savings"
12 USC 4901 et seq., "Homeowners Protection"
15 USC 78q-1(c), "Registration of Transfer Agents"
15 USC 78bb(e), "Exchange, Broker, and Dealer Commissions; Brokerage and Research Services"

15 USC 1601 et seq., “Consumer Credit Cost Disclosure”
15 USC 1681 et seq., “Credit Reporting Agencies”
15 USC 1691 et seq., “Equal Credit Opportunity”
15 USC 1692 et seq., “Debt Collection Practices”
15 USC 1693 et seq., “Electronic Fund Transfers”
15 USC 6501 et seq., “Children’s On-Line Privacy Protection”
15 USC 6801 et seq., “Disclosure of Nonpublic Personal Information”
15 USC 7001 et seq., “Electronic Signatures in Global and National Commerce”
15 USC 7707 et seq., “Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003”
29 USC 1001 et seq., “Employee Retirement Income Security Program”
42 USC 3601 et seq., “Fair Housing”
42 USC 4003(a)(10), “Regulated Lending Institution”
42 USC 4012a(f), “Civil Money Penalties for Failure to Require Flood Insurance or to Notify”
47 USC 227, “Restrictions on Use of Telephone Equipment”
50 USC 3901 et seq., “Servicemembers Civil Relief”
Internal Revenue Code section 408
Internal Revenue Code section 4975

Regulations

12 CFR 1, “Investment Securities” (national banks)
12 CFR 3, “Capital Adequacy Standards”
12 CFR 4, “Organization and Functions, Availability and Release of Information, Contracting Outreach Program, Post-Employment Restrictions for Senior Examiners”
12 CFR 4.6, “Frequency of Examination of National Banks and Federal Savings Associations”
12 CFR 5.51, “Changes in Directors and Senior Executive Officers of a National Bank or Federal Savings Association”
12 CFR 6, “Prompt Corrective Action”
12 CFR 9, “Fiduciary Activities of National Banks” (national banks*)
12 CFR 11, “Securities Exchange Act Disclosure Rules”
12 CFR 12, “Recordkeeping and Confirmation Requirements for Securities Transactions” (national banks)
12 CFR 14, “Consumer Protection in Sales of Insurance”
12 CFR 21, subpart A, “Minimum Security Devices and Procedures” (national banks)
12 CFR 21.21, “Procedures for Monitoring Bank Secrecy Act Compliance”
12 CFR 22, “Loans in Areas Having Special Flood Hazards”
12 CFR 30, appendix A, “Interagency Guidelines Establishing Standards for Safety and Soundness”
12 CFR 30, appendix B, “Interagency Guidelines Establishing Information Security Standards”
12 CFR 32.7, “Residential Real Estate Loans, Small Business Loans, and Small Farm Loans (“Supplemental Lending Limits Program”)
12 CFR 34, subpart C, “Appraisals”

12 CFR 150, "Fiduciary Powers of Federal Savings Associations" (FSAs)
12 CFR 151, "Recordkeeping and Confirmation Requirements for Securities Transactions" (FSAs)
12 CFR 160, "Lending and Investment" (FSAs)
12 CFR 168, "Security Procedures" (FSAs)
12 CFR 204, "Reserve Requirements of Depository Institutions (Regulation D)"
12 CFR 218, "Exceptions for Banks From the Definition of Broker in the Securities Exchange Act of 1934 (Regulation R)"
12 CFR 223, "Transactions Between Member Banks and Their Affiliates (Regulation W)"
12 CFR 229, "Availability of Funds and Collection of Checks (Regulation CC)"
12 CFR 363, "Annual Independent Audits and Reporting Requirements"
12 CFR 1002, "Equal Credit Opportunity Act (Regulation B)"
12 CFR 1003, "Home Mortgage Disclosure (Regulation C)"
12 CFR 1005, "Electronic Fund Transfers (Regulation E)"
12 CFR 1016, "Privacy of Consumer Financial Information (Regulation P)"
12 CFR 1022, "Fair Credit Reporting (Regulation V)"
12 CFR 1024, "Real Estate Settlement Procedures Act (Regulation X)"
12 CFR 1026, "Truth in Lending (Regulation Z)"
12 CFR 1030, "Truth In Savings (Regulation DD)"
16 CFR 316, "CAN-SPAM Rule"
17 CFR 240, "General Rules and Regulations, Securities Exchange Act of 1934"
17 CFR 247, "Regulation R—Exemptions and Definitions Related to the Exceptions for Banks From the Definition of Broker"

* 12 CFR 9.18 is applicable to FSAs under 12 CFR 150.260(b).

Comptroller's Handbook

Examination Process

"Bank Supervision Process"
"Large Bank Supervision"

Safety and Soundness Series

"Accounts Receivable and Inventory Financing" (national banks)
"Asset-Based Lending"
"Bank Dealer Activities" (national banks)
"Capital and Dividends"
"Cash Accounts" (national banks)
"Commercial Loans" (national banks)
"Commercial Real Estate Lending"
"Concentrations of Credit"
"Corporate and Risk Governance"
"Country Risk Management"
"Credit Card Lending"
"Deposit-Related Credit"
"Due From Banks"

“Emerging Market Country Products and Trading Activities” (national banks)
“Floor Plan Lending”
“Foreign Exchange” (national banks)
“Futures Commission Merchant Activities” (national banks)
“Insider Activities”
“Installment Lending”
“Interest Rate Risk”
“Internal Control” (national banks)
“Internal Control Questionnaires/Verification Procedures”
“Internal and External Audits”
“Lease Financing”
“Leveraged Lending” (national banks)
“Liquidity”
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OTS Examination Handbook (FSAs)

Section 201, “Overview: Lending Operations and Portfolio Risk Management”
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OCC Issuances

Banking Circular 216, “Securities Denominated in Foreign Currencies” (national banks)
Banking Circular 277, “Risk Management of Financial Derivatives” (national banks)
OCC Bulletin 1994-31, “Risk Management of Financial Derivatives Q&A’s” (national banks)
OCC Bulletin 1996-43, “Credit Derivatives: Guidelines for National Banks” (national banks)
OCC Bulletin 1998-20, “Investment Securities: Policy Statement”
OCC Bulletin 1999-2, “Risk Management of Financial Derivatives and Bank Trading Activities—Supplemental Guidance”
OCC Bulletin 2000-20, “Uniform Retail Credit Classification and Account Management Policy: Policy Implementation”
OCC Bulletin 2001-6, “Subprime Lending: Expanded Guidance for Subprime Lending Programs”
OCC Bulletin 2003-9, “Mortgage Banking: Interagency Advisory on Mortgage Banking”
OCC Bulletin 2003-12, “Interagency Policy Statement on Internal Audit and Internal Audit Outsourcing”
OCC Bulletin 2003-36, “Liquidity Risk Management: Interagency Advisory on the Use of the Federal Reserve’s Primary Credit Program in Effective Liquidity Management”
OCC Bulletin 2004-29, “Embedded Options and Long-Term Interest Rate Risk: Interest Rate Risk”
OCC Bulletin 2004-56, “Bank Owned Life Insurance: Interagency Statement on the Purchase and Risk Management of Life Insurance”
OCC Bulletin 2005-9, “Overdraft Protection Programs: Interagency Guidance”

OCC Bulletin 2005-13, "Response Programs for Unauthorized Access to Customer Information and Customer Notice: Final Guidance: Interagency Guidance"
OCC Bulletin 2005-35, "Authentication in an Internet Banking Environment: Interagency Guidance"
OCC Bulletin 2006-24, "Interagency Agreement on ERISA Referrals: Information Sharing Between the FFIEC Agencies and the DOL"
OCC Bulletin 2006-35, "Authentication in an Internet Banking Environment: Frequently Asked Questions"
OCC Bulletin 2006-41, "Nontraditional Mortgage Products: Guidance on Nontraditional Mortgage Product Risks"
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OCC Bulletin 2007-26, "Subprime Mortgage Lending: Statement on Subprime Mortgage Lending"
OCC Bulletin 2007-36, "Bank Secrecy Act/Anti-Money Laundering: BSA Enforcement Policy"
OCC Bulletin 2009-15, "Investment Securities: Risk Management and Lessons Learned" (national banks)
OCC Bulletin 2010-1, "Interagency Advisory on Interest Rate Risk Management"
OCC Bulletin 2010-13, "Final Policy Statement: Interagency Policy Statement on Funding and Liquidity Risk Management"
OCC Bulletin 2010-24, "Incentive Compensation: Interagency Guidance on Sound Incentive Compensation Policies"
OCC Bulletin 2010-42, "Sound Practices for Appraisals and Evaluations: Interagency Appraisal and Evaluation Guidelines"
OCC Bulletin 2010-15, "Overdraft Protection: Opt-In Requirements and Related Marketing Issues"
OCC Bulletin 2011-12, "Sound Practices for Model Risk Management: Supervisory Guidance on Model Risk Management"
OCC Bulletin 2011-26, "Authentication in an Internet Banking Environment: Supplement"
OCC Bulletin 2012-5, "FAQs on 2010 Interagency Advisory on Interest Rate Risk Management"
OCC Bulletin 2012-6, "Interagency Guidance on ALLL Estimation Practices for Junior Liens: Guidance on Junior Liens"
OCC Bulletin 2012-18, "Alternatives to the Use of External Credit Ratings in the Regulations of the OCC: Final Rules and Guidance"
OCC Bulletin 2012-30, "BSA/AML Compliance Examinations: Consideration of Findings in Uniform Rating and Risk Assessment Systems"
OCC Bulletin 2012-33, "Community Bank Stress Testing: Supervisory Guidance"
OCC Bulletin 2013-28, "Classification of Securities: Interagency Guidance"
OCC Bulletin 2013-29, "Third-Party Relationships: Risk Management Guidance"
OCC Bulletin 2014-8, "End-User Derivatives and Trading Activities: Comptroller's Handbook Supplemental Examination Procedures"
OCC Bulletin 2014-35, "Mutual Federal Savings Associations: Characteristics and Supervisory Considerations"

OCC Bulletin 2016-6, "Bank Secrecy Act/Anti-Money Laundering: Process for Administrative Enforcement Actions Based on Noncompliance With BSA Compliance Program Requirements or Repeat or Uncorrected BSA Compliance Problems"
OCC Bulletin 2017-7, "Third-Party Relationships: Supplemental Examination Procedures"
OCC Bulletin 2017-21, "Third-Party Relationships: Frequently Asked Questions to Supplement OCC Bulletin 2013-29"
OCC Bulletin 2017-43, "New, Modified, or Expanded Bank Products and Services: Risk Management Principles"
OCC Bulletin 2018-41, "OCC Enforcement Actions: OCC Enforcement Action Policies and Procedures Manual"
OCC Bulletin 2019-42, "Flood Disaster Protection Act: Revised Interagency Examination Procedures"

OTS Issuances (FSAs)

Thrift Bulletin 73a, "Investing in Complex Securities"

Other

Accounting Standards Codification 310-10, "Receivables"
Accounting Standards Codification 320, "Investments—Debt and Equity Securities"
Accounting Standards Codification 450-20, "Loss Contingencies"
Accounting Standards Codification 825, "Financial Instruments"
FFIEC Bank Secrecy Act/Anti-Money Laundering Examination Manual
FFIEC Information Technology Examination Handbook

Table of Updates Since Publication

Refer to the "Foreword" booklet of the *Comptroller's Handbook* for more information regarding the OCC's process for updating and revising *Comptroller's Handbook* booklets.

Version 1.0: Published June 28, 2018			
Version number	**Date**	**Reason**	**Affected pages**
1.1	September 30, 2019	Updated to reflect changes in the OCC's organizational structure	2–3, 168–169, 172, 179
		Updated asset size threshold for eligibility for the expanded supervisory cycle; removed content regarding the Economic Growth, Regulatory Relief, and Consumer Protection Act (Pub. L. 115-174) in relation to the supervisory cycle	7
		Edited for clarity	12, 18, 19, 20, 22, 30–31, 50–51, 55, 65–66, 68–69, 70–73, 76, 78, 81, 86–89, 93–94, 99–100,106, 110, 124,132, 137, 140, 146, 148, 156, 159, 163–164, 166–168, 179, 205, 229, 234, 253, 247
		Added detail to "Risk Assessment System" section for consistency with "Bank Supervision Process" booklet of the *Comptroller's Handbook*	13
		Eliminated unnecessary duplication of content from "Bank Supervision Process" booklet	20
		Revisions for consistency with OCC's updated enforcement action policies	36–39
		Clarified applicability to national banks or FSAs	50, 55, 71, 73–74, 77, 89, 119, 147, 152, 155, 184, 247–248
		Added references	51, 77, 89, 99, 107, 110, 118–120, 124–125, 132, 146, 148, 155, 164, 168–172, 224, 229, 232–233
		Combined two examination procedures from the conclusions sections for efficiency	62, 68, 82, 91, 97, 108, 115, 125, 138, 157, 161, 175
		Updates from publication of the "Capital and Dividends" booklet of the *Comptroller's Handbook*, including • Change in booklet title from "Capital Accounts and Dividends" • Rescission of OCC Bulletin 2012-16 and replacement with "Capital Planning" section of the "Capital and Dividends" booklet Refer to OCC Bulletin 2018-20, "Capital and Dividends: Revised Comptroller's Handbook Booklet and Rescissions," for	64, 67

		more information regarding the revised "Capital and Dividends" booklet.	
		Generalized language regarding capital computations to not mention specific ratios	64
		Changes to the OCC's credit underwriting assessment	73–74, 77, 80, 82–84
		Consistency with OCC policies	76
		Updated reference to be more specific	80
		Consistency with the updated ROE policy in the "Bank Supervision Process" booklet of the *Comptroller's Handbook*	80, 82
		Clarifications regarding sound risk management, supervisory guidance, or legal requirements	88, 148
		Combined examination procedures regarding CFPs under one objective for efficiency and to reduce redundancy	103, 106–107
		Eliminated redundant examination procedure	NA (would be on page 104)
		Updated request letter appendix to reflect that the OCC's standard process is obtaining information digitally, and to reflect changes in the LFT folder structure for community banks	247–253
		Updated for consistency with interagency guidance	106–107
		Consistency with the "Corporate and Risk Governance" booklet of the *Comptroller's Handbook*	104–105, 113, 133, 137, 182, 240, 252
		Consistency with OCC Bulletin 2009-15 and Thrift Bulletin 73a	110–111
		Revised to more fully reflect the definition of price risk from the "Bank Supervision Process" booklet	124
		Removed reference to the Volcker rule given the scope of the new rule (refer to 12 CFR 44)	124
		Split one examination procedure into two for clarity	131
		Consistency with OCC Bulletin 2017-43	140
		Corrected citation	146, 157, 178, 219
		Revised to include both bank holding companies and savings and loan holding companies	148
		Clarified BSA and OFAC examination information for consistency with the "Bank Supervision Process" booklet. Streamlined BSA objectives and procedures to reduce redundancy with *FFIEC BSA/AML Examination Manual*	160–161

		Changed Bureau of Consumer Financial Protection (BCFP) to Consumer Financial Protection Bureau (CFPB)	164–167, 169
		Reflected rescission of “Flood Disaster Protection Act” booklet of the *Comptroller’s Handbook* and replacement with the “Interagency Flood Disaster Protection Act Examination Procedures” (Refer to OCC Bulletin 2019-42)	170
		Revised for consistency with other booklets in the *Examination Process* series of the *Comptroller’s Handbook*	204, 240, 242
		Updated terminology “internal controls” for consistency with other *Comptroller’s Handbook* booklets	240–242
		Updated “Abbreviations” section for consistency with the content of the booklet	254–255
		Updated “References” section for consistency with the content of the booklet	256–262