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## CHAPTER: Administration

### SECTION: Examination Strategy, Scoping, and Management

### Section 060

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This Handbook Section provides guidance to you as the examiner. We refer to “you” in a general sense. Regional directors may assign responsibilities to certain other positions as appropriate.

This section provides guidance in five areas:

- Examination strategy (includes scheduling).
- Scoping examinations.
- Managing examinations.
- Off-site examination procedures.
- Joint examinations.

#### EXAMINATION STRATEGY

Concentration on improving examination efficiency and a risk-focused regulatory approach are critical strategies to ensuring a sound thrift industry. These strategies will help you assess the overall safety and soundness of an institution in a timely manner and ensure the accuracy of its composite and component ratings. As a regional office, you are responsible for developing appropriate management tools and performance standards to affirm that our examination strategy is consistently met. An important aspect of this strategy is the scheduling of examinations.

#### Scheduling Examinations

You must schedule full-scope (type 10), on-site examinations of insured depository institutions once during a 12-month cycle or once during an 18-month cycle. Supplemental examinations are necessary under certain conditions.

The Office of Thrift Supervision (OTS) measures the 12-month and 18-month cycles from the “close date” of the last examination to the “start date” of the next examination. The “close date” is the date the Report of Examination (ROE) is transmitted to the institution.

Regional offices may accept full-scope, on-site examinations conducted by the regulatory authorities of state depository institutions on an alternating basis instead of an OTS examination, if such ex-

aminations meet the requirements and objectives of OTS’s examination strategy.

#### *12-month cycle*

You must conduct a full-scope (type 10), on-site examination of the institution once during each 12-month period unless the institution meets the 18-month cycle requirements below.

By conducting examinations annually you increase your chances of discovering problems and resolving them early. Regional offices may conduct full-scope, on-site examinations more often than prescribed by statute.

All de novo institutions are subject to the 12-month examination cycle. The 12-month examination cycle should continue until management has demonstrated its ability to operate an institution in a safe and sound manner.

#### *18-month cycle*

An 18-month examination interval applies to insured institutions of \$250 million or less that meet all of the criteria of a “well-run” institution (12 CFR § 563.171):

- The most recent examination received a composite CAMELS rating of 1 or 2.
- The most recent examination received a Management component rating of 1 or 2.
- The institution is well-capitalized as defined under Section 38 of the Federal Deposit Insurance Act (FDIA) and 12 CFR §565.4.
- The institution is not currently subject to a formal enforcement proceeding or order by the OTS or the FDIC.
- The institution has not been acquired (change in control) during the 12-month period since completion of the last full-scope examination.

Vary from the 18-month examination schedule in the event of an enforcement action, an acquisition or change in control; or a change in asset size, PCA rating, CAMELS rating, or management component rating. If a triggering event occurs in any of the following timeframes at an institution that otherwise meets all of the criteria for an 18-month examination interval, you must conduct a full-scope examination within the appropriate interval:

- Within 9 months of the “close” date of the prior full-scope examination, start the next examination no later than 12 months from the close of the last full-scope examination.
- Between 9 and 12 months since the close of the last full-scope examination, start the next examination within 90 days.
- Twelve or more months since the close of the last full-scope examination, start the next examination within 90 days, but no later than 18 months from the close of the last full-scope examination.

Conversely, if an institution under a 12-month examination interval later becomes eligible for an expanded interval, the interval can be expanded to 18 months immediately.

#### *Supplemental Examinations*

More frequent or supplemental examinations may be necessary for the following institutions:

- De novo or newly insured institutions.
- Institutions that have had a change in management, control, or operations.
- Institutions under an enforcement agreement.
- Institutions whose conditions undergo a significant change.

Use special limited examinations (type 40) for supplemental reviews focusing on high-risk areas. Special limited examinations or other abbreviated

examination programs do not satisfy the 12/18 month requirement.

To determine if an institution needs a supplemental on-site examination, focus on the following factors:

- Changes in key financial ratios and indicators.
- Changes in business activity and strategy, such as a change in loan product lines, the investment portfolio, or the deposit structure.
- Deterioration in asset quality indicators such as non-performing assets.
- Compliance with prior enforcement actions.
- Negative earnings, unfavorable earnings trends, or dependence on nonoperating income.
- The levels and composition of capital, as well as trends in capital formation and accumulation.
- An excessive rate of growth or a level of growth that exceeds capital levels or regulatory or supervisory directives.
- Other information such as the independent audit report, news articles, supervisory correspondence, and information obtained from examinations of other institutions.

#### **SCOPING YOUR EXAMINATION**

Scoping an examination means you determine the specific examination procedures to use and the depth of review. Scoping may occur on site or off site before the examination, when it begins, or both.

To help OTS meet its strategy of an on-site presence in each institution every 12 or 18 months, place a special emphasis on risk analysis and prioritization. That is, vary the depth of review in each area according to an institution’s size, activities, and condition. Do less review in those areas where no significant present or potential risks ex-

ist and more review where major risks are present or possible.

Consider all handbook programs and questionnaires when setting the initial depth of examination review. Use only programs and questionnaires appropriate to the scope and examination. In some circumstances, you will not need all or even a majority of the programs. (See “Selecting Examination Programs and Procedures” discussed later in this section and Thrift Activities Handbook Section 011, Program Use.)

### **Preliminary Scoping of Examinations**

The preliminary scope may provide information needed to determine staff expertise requirements, the examination start date and duration, and strategies for conducting the examination.

Preliminary scoping may be done off site or on site. Items that may be reviewed off site include the following:

- The Regulatory Plan (see Thrift Activities Regulatory Handbook Section 050) for the institution.
- Prior thrift, holding company, and service corporation examination reports, work papers, and recommendations.
- Preliminary Examination Response Kit (PERK) documents completed by institution management prior to the start of the examination.
- Documentation on supervisory and enforcement actions.
- Results of off-site monitoring.
- Correspondence and internal memoranda involving the institution.
- Economic information about the institution’s market area(s).
- News articles.

Ensure that the scope does two things:

- Provides for a sufficient review of high-risk areas.
- Includes clear, specific guidelines on the depth of review needed in each area.

Major areas of risk do not necessarily mean problems; some risk is part of conducting any profitable institution. Include procedures that enable you to determine if the institution’s level and management of risk is unsafe and unsound. Also concentrate on changes in operations or management because these can pose a significant risk.

### **Ongoing Scoping of Examinations**

Whatever the size or condition of the institution, you will be more productive by using a well-defined scope. Avoid beginning with a broad scope and then trying to narrow it during the examination. Instead, focus first on areas of major risk and then expand the scope as you uncover or suspect significant problems or changes. Also expand the scope if you can assign ratings only by doing more procedures. Determining the depth of review (Level II and Level III procedures) within specific programs may require a preliminary analysis (Level I procedures). For more information about the three levels of review, see Section 011 of this Handbook, Program Use.

The ongoing determination of scope, particularly the depth of review within each program, requires the involvement of each member of the examination team:

- The Examiner in Charge (EIC): Ensure that the team is aware of the procedures needed to efficiently meet the scope. Discuss possible changes to the scope with your team throughout the examination.

Discuss any significant changes in the scope, projected staffing needs, or completion date with your managing supervisor as soon as you anticipate these changes. These discussions are

important because any changes will affect how your regional office plans its regulatory activities.

- The regional director or designee: Approve expansions of scope that will cause the examination to extend beyond the original time frame.
- Safety and soundness examiners: Communicate any significant changes to the scope and the reasons for them with examiners involved in holding company, consumer compliance, trust, and information systems (IS) examinations. Share significant findings and conclusions to avoid duplicating efforts.
- Regulators when FDIC is involved: Maintain close communication with FDIC regulatory authorities and appropriate state regulatory authorities.

When you start an on-site examination, review additional information that may affect the scope as soon as possible. Examples of scoping materials commonly reviewed on site include the following:

- PERK documents available at examination commencement.
- Minutes from the meetings of the board of directors, board committees, and management committees.
- Board reports and management reports.
- Internal audit reports.
- Internal Asset Review (IAR) reports.
- General ledger and subsidiary ledgers.
- Business plan.
- Operating budget.
- Any new contracts (e.g., employment, information systems).

- Leases.
- Loan registers.

### Additional Scoping Considerations

As soon as practical, before or at the beginning of the examination, the EIC must meet with the CEO to discuss items of interest or concern that could affect the scope. At this meeting, you should clarify administrative details.

It is helpful to prepare for the meeting with the CEO in advance so that you cover all items of interest efficiently. Topics that could affect the scope of this discussion include the following:

- Changes in control.
- Changes in management.
- Actions taken to correct deficiencies mentioned in prior examination reports and audit reports.
- Operating performance in comparison with the budget.
- Significant changes in operations or strategies.
- Any significant concerns expressed by management.
- Economic and competitive conditions in the market area.

The EIC might also discuss with the CEO, or with a designated institution representative, the following administrative details:

- Time limits for receiving requested information.
- The availability of the examiners to answer questions from the staff preparing requested information.

- Names of key contact people, facilities and parking availability, hours for work, use of equipment, etc.
- The expected duration of the examination, any planned interruptions (these should be kept to a minimum), and names of assisting examiners.
- A meeting with the independent auditor and review of independent audit work papers, in accordance with regional policy, if applicable.
- Regular meetings with the CEO to discuss the progress of the examination and to address any other issues of concern to the CEO or the EIC.
- An examination exit meeting with the institution's senior management to discuss examination findings, the examiner's overall conclusions, and recommendations (see Thrift Activities Regulatory Handbook Section 070, Overall Conclusions).

### **Preliminary Examination Response Kit**

Several documents comprise the Preliminary Examination Response Kit (PERK). The regulator selects certain documents and sends them to the institution for completion by institution management prior to the examination. The preparation and availability of this information before the beginning of the examination, assists OTS and the institution by determining examination scope and increasing the efficiency of the on-site examination.

#### *General Instructions*

Prepare the PERK by selecting various documents and information requests specific to the institution from the list on the Summary Schedule (PERK 001). You may access the PERK electronically from your regional office M: drive. This enables you to revise and print the individual documents needed for the examination of a particular institution.

You should tailor the summary schedule to the institution and type of examination. Request the minimum information needed to conduct a risk-focused examination based on the examination scope. This approach will increase the efficiency of the on-site examination and reduce the burden on savings associations, particularly for highly rated, well-managed institutions engaging in traditional activities.

List items needed for both phases of a concurrent examination, for example, concurrent safety and soundness and compliance examinations, as an information request in only one schedule – either the safety and soundness examination summary schedule or the compliance examination summary schedule.

To meet the OTS customer service plan standards, send the PERK to an institution four weeks prior to the examination start date. Contact the institution and inform management of any delays so that they can plan for a shorter turnaround. If you are performing off-site examination procedures, consider advancing the request date beyond the four weeks prior to the examination start date.

The EIC or designee: At the beginning of the examination, request the completed PERK from institution management. Be aware of information that management may have sent to the regional office prior to examination commencement.

Encourage institution management to submit the requested information on internally generated reports, such as computer printouts or software spreadsheets if these reports will facilitate the completion of the examination.

At the conclusion of the examination, complete a summary schedule for the PERK at the next examination. Update it when necessary to facilitate the scoping and planning process for the next examination.

The examiner: Review management's responses and discuss them in greater detail with management including any unclear answers or areas that may affect the scope of the examination. Ensure that the appropriate dates are entered on the first

page of each document and that the “Institution Name” and “Docket Number” are indicated on each document and any attachments.

PERK Letter (PERK 000) – Prepare the PERK Letter on OTS regional/area office letterhead in the same general format exhibited in the sample letter. You may modify the PERK letter for use with safety and soundness, compliance, information systems, trust, special limited examinations, or concurrent examinations of any combination. Insert the appropriate paragraph as provided in the examples or create a paragraph accordingly. You may identify in the letter items needed for both phases of a concurrent examination, such as concurrent safety and soundness and compliance examinations. The institution need only provide one copy.

The PERK letter must include all of the following information:

- A start date for the on-site examination.
- The examination as of date.
- The number of on-site staff and an estimation of the amount of time required to conduct the examination.
- A contact person’s name and phone number, usually the OTS official who signs the PERK letter and expects to field questions from the institution, e.g., the EIC.

Summary Schedule (PERK 001) – The summary schedule lists (1) the PERK documents enclosed in the package to the institution and (2) suggested CAMELS-related requests that should be tailored to the scope of the examination. You may add additional requests and delete unnecessary or irrelevant requests. You should make a determination as to the items necessary to complete an on-site examination of the institution, and provide dates and dollar limits where appropriate. Each request should be indicated by an “A” (completion required 10 days in advance of the examination), “X” (provide at examination commencement), or “R” (make available for on-site review). In a concurrent examination, the safety

and soundness and compliance EICs should coordinate to ensure that items needed for both examinations are listed in either the safety and soundness summary schedule or the compliance examination summary schedule.

Institution management should complete summary schedule requests and provide the information to the EIC prior to or at the commencement of the examination as indicated (“A,” “X,” or “R”). The examiners may also use the summary schedule as a checklist to keep track of the documents as institution management provides them.

*“Core” PERK*

Include the following documents in the PERK that is sent to the institution.

Management Questionnaire (PERK 002) – Prior to sending the PERK to the institution, enter the previous examination date and the examination commencement date at the top of the questionnaire.

You should carefully review written explanations for completeness and accuracy, and initiate further discussion with the managing officer, if necessary. If the response to No. 14.a. or 14.b. indicates a reportable event or violation of the applicable regulation, you must notify the FDIC regional office.

Schedule of Directors, Senior Executive Officers, and Attorneys (PERK 003) – The institution may complete the compensation schedule in the format exhibited in the PERK or any format currently in use by the institution that contains substantially equivalent information. Directors, senior executive officers, and designated attorneys are to be listed on the compensation schedule. “Senior executive officers” are those responsible for the management function of the institution. See RB 27a and 12 CFR § 563.555 for pertinent definitions.

Internal Control Procedural Questionnaire (PERK 004) – Each section of the questionnaire should be completed by institution personnel familiar with that section; for instance, the Vice-President

of Lending might complete the Lending section. The EIC, or designee, should review the entire questionnaire and sign in the spaces provided. Note that the appropriate response may not always be in the affirmative, in which case the institution should provide an adequate written explanation.

Information Systems (IS) Questionnaire for Insured Institutions (PERK 005) – The IS Questionnaire should be sent out on every annual safety and soundness examination and completed by institution personnel. The institution should forward a copy of the completed questionnaire to the IS examination manager at the regional office. You should review the questionnaire and investigate inappropriate responses. Note that the appropriate response may not always be in the affirmative.

Electronic Loan Data (ELD) Request – The ELD Request is a new method for reviewing and analyzing loan portfolios. It is a voluntary submission by institution management of certain loan information in an electronic format, such as a personal computer diskette. If you request this schedule, you must ensure that duplicative information requested in the summary schedule is deleted from the request. The ELD Request will formally be included in the PERK when it is approved.

### *Compliance Examinations*

Include the following documents in the PERK when a compliance examination and a safety and soundness examination are conducted concurrently. The regional office may (1) determine that a compliance examination will be conducted separately from the safety and soundness examination or (2) consider requests by the institution to conduct non-concurrent examinations.

Compliance Examination Summary Schedule (PERK 006) – The Compliance Examination Summary Schedule is a list of standard requests that should be tailored to the scope of the examination, i.e., you may add additional requests and delete unnecessary requests. Coordinate with the safety and soundness EIC to ensure that items

needed for both the safety and soundness and the compliance examinations are listed on either PERK 001 or PERK 007. Information requested on the Compliance Examination Summary Schedule should be provided to the EIC prior to or at the commencement of the examination.

Fair Lending Questionnaire (PERK 007) – The managing officer should provide answers to the questionnaire and attach additional pages if space provided is inadequate.

Community Reinvestment Act Information (PERK 008) – Responses to requests for CRA information should be as specific as possible and signed by both the institution's managing officer and CRA officer. If the institution is not involved in a particular activity, management should explain why they chose not to participate in a program addressing the specific assessment factor.

CRA Optional Information - Small Institutions (PERK 015) – This outline guides an institution by identifying the types of supplementary information that may provide examiners with a better understanding of the institution's performance. Response to this request is voluntary.

CRA Public File Summary (PERK 016) – This document summarizes the information from the CRA Public File that the OTS uses to evaluate CRA performance in both small and large institutions.

### *Supplemental Schedules*

You may include in the PERK the applicable documents listed below if the particular area is to be examined in conjunction with the safety and soundness examination.

Schedule for Retail Nondeposit Investment Products (PERK 009) – Request completion of this schedule by any savings association engaged in the retail sale of nondeposit investment products such as stocks, bonds, mutual funds, or annuities.

Subordinate Organization Questionnaire (PERK 010) – The institution should complete this ques-

tionnaire for each subordinate organization that significantly affects, or has the potential to significantly affect the institution's operations, unless noted otherwise. Subsidiaries that have an insignificant effect on the institution should be listed separately with an explanation as to why they are considered insignificant. The Subordinate Organization Questionnaire should be completed by those who have direct knowledge or can obtain it by appropriate inquiry. If the institution has no investment in subordinate organizations, it should so state in answer to No. 1. Separate questionnaires should be used for each subordinate organization, including second tier corporations and other sublevels.

Information Systems (IS) Information Request Schedule for In-House Institutions and Service Bureaus (PERK 011) – This schedule should be used for examinations of independent service bureaus and institutions with an in-house data center. The schedule of information requests should be provided to the EIC prior to or at the commencement of the IS examination.

Trust Examination Summary Schedule (PERK 012) – The Trust Examination Summary Schedule of information should be made available to the EIC prior to or at the commencement of the trust examination. Management should provide a brief explanation, or the name of an individual to contact, for any information they do not provide.

Mortgage Banking Questionnaire (PERK 013) – Completion of this questionnaire should be included in the PERK if the institution or any subsidiaries are engaged in mortgage banking during the examination period.

Schedule of Stockholders (PERK 014) – This schedule should be completed to determine the stock activity that has taken place between examinations.

### **Selecting Examination Programs and Procedures**

You should consider all programs and questionnaires within the scope of the examination. Use programs and questionnaires deemed appropriate,

but only to the extent necessary to address the scope and support the examination conclusions. In some circumstances, not all or not even a majority of the procedures will be needed.

For example, if your review of the policies, structure, administration, and results of the institution's internal asset review program reveals that the program is sufficient and the results are accurate, you may place a greater reliance on the institution's internal review. The risk that the institution is not adequately reviewing and classifying its assets would be low, so more detailed examination procedures would generally not be necessary.

When using this risk-focused examination approach, use sound professional judgment to ensure that the depth of review is sufficient to accurately assess the institution's condition, but is not excessive. For further information regarding the examination program and the three levels of review, refer to Section 011 of this Handbook, Program Use.

### **Work Paper Documentation**

Examination work papers should include a title or well-marked description of the work paper purpose, the scope for the particular area of review, the sampling criteria used, the procedures performed, and the preparer's initials. Documented procedures support the analysis and help maintain the integrity of the work paper.

You are required to support all the applicable elements reviewed under each CAMELS component either in the work papers or in a conclusion documented on the appropriate program. In addition, the conclusion for each work paper or area of review should summarize the examination findings, support the composite rating (in addition to the component rating), and indicate if any corrective or enforcement action is necessary.

However, you should avoid excessive documentation and include only information that is relevant or may require follow-up. Time spent recording extraneous information would be better spent examining high-risk areas. To facilitate any

follow-up review that may be necessary, you should also document the name and title of persons or a description of the records from which information was obtained. Schedules prepared by the institution should be clearly marked as such. The EIC or designee is required to review and initial all work papers, indicating agreement with the conclusions reached and ensuring that assistants have complied with the applicable documentation requirements. The TFR, UTPR, and other multi-page printed documents need only be initialed and dated on the first page. The EIC should ensure that all comments, charts, and appendices have been carefully checked by exam staff. At a minimum, the EIC's supervisor will review the work papers prepared by the EIC and the supporting documentation for the report comments.

### **Continuing Examination File and the General File**

#### *Continuing Examination File*

Include the following items, only if applicable to the particular institution being examined, in the Continuing Examination File (CEF), or file them with the applicable examination programs and carry them forward from examination to examination until no longer applicable. Maintenance of these documents preserves examination continuity and reduces excessive requests for information during examinations.

- Management and Director Committees and Members (PERK)
- Organizational Chart (PERK)
- Officer Resumes (PERK)
- Directors' and Officers' Home Addresses (PERK)
- Enforcement Documents
- Schedule of Branch Offices and LPOs
- Copy of Charter and Bylaws
- Copy of Conditions for Insurance (in force)
- Summary of Leases
- Holding Company/Affiliates Corporate Structure (PERK)
- Internal Audit Program (PERK)
- Stockholders' Schedule (PERK)
- Proxy Statement

- Approved Appraisers and Qualifications (PERK)
- Employment Contracts (PERK)

If an institution policy must be included as part of work paper support, file it in the appropriate CAMELS section of the work papers. Similarly, include the business plan and budget requirements in the Management/Administration work paper file.

#### *General File*

The general file contains the administrative information related to the examination, and is organized to correspond with the administrative section of the Handbook.

Include the following items in the general file:

- Exception Sheets
- Examination Strategy, Scoping, and Management Program
- PERK Summary Schedule (for next exam)
- Regulatory Plan
- Pre-Assignment Analysis
- Overall Conclusions Program
- EDS Part III Interim Report
- Recent Correspondence
- Newspaper Clippings

You should use exception sheets to record all specific regulatory and policy violations that are not specifically discussed in the ROE. Either the managing officer or the appropriate department head must provide a disposition for each problem noted and initial the exception sheet. Provide a copy of all exception sheets to the managing officer.

### **EXAMINATION MANAGEMENT**

Managing examinations is as important as scoping them. Effective management of the examination expedites and enhances the examination process by ensuring that objectives are met efficiently. The level and sophistication of management methods and procedures will vary depending on the activities to be performed and the size and nature of the institution.

**EIC Responsibilities**

The EIC carries the primary responsibility for managing the examination. Key elements the EIC should consider:

- The examination objectives: The EIC must ensure that the assistants understand the objectives of the examination and for their assigned programs. Objectives should be specific as to results desired.
  - The examination procedures contained in the individual programs are designed to be comprehensive. So, select only the appropriate procedures within each program. Assistants should notify the EIC as questions occur regarding scope or depth of review.
- Organization: This involves scheduling meetings with institution personnel; arranging appropriate workspace for regulators; prioritizing and scheduling work flow; communicating examination status; preparing the examination report; and preparing, filing, indexing, and reviewing work papers.
- Assignments and job monitoring: The EIC must determine the expertise necessary to perform certain aspects of the examination and make assignments accordingly. When warranted, assign major areas to individual assistants. Depending on the size of the job, delegate certain management responsibilities to assistants for efficiency and to improve upon administrative and management skills of assistants. Also consider training and development needs when making examination assignments.
  - Whenever possible, assign assistants to program areas that they can complete, including report pages and comments, before leaving the assignment. This allows for efficiency and accountability and provides necessary on-the-job training.
  - Monitor assistants' performance throughout the examination to ensure that objectives are being met according to schedule and to prevent minor problems from growing. Early identification of work-related problems also allows the assistants the opportunity to correct mistakes and to immediately improve upon skills.
- Budgeting and monitoring overall time: Consider the time budget when assigning tasks. A useful tool for improved personnel planning is a time and planning summary that is organized according to the sections contained in this Handbook. It specifies the areas for which procedures are planned and provides for a comparison of actual and budgeted hours. Add, as needed, any activities not included on the time sheet.
  - Assign priorities to the critical categories and determine optimal timing of simultaneous activities. Ordinarily this can be accomplished by assigning categories of related programs to one assistant who subsequently may supervise others. If time allows, it is also most efficient to have one assistant complete interrelated programs to avoid duplication of effort.
  - To minimize costs and disruption for the institution, it is important that the examination be conducted as quickly as practical. A stable crew with minimal interruptions of staff time allows for continuity and efficiency. It is the EIC's responsibility to discuss any planning problems with a supervisor. If institution management is concerned about scheduling, include this matter in your discussion.
  - Monitoring the progress of the examination allows for early adjustments to the scope, staffing, and completion date, as necessary, for the examination. The EIC is responsible for notifying a supervisor as soon as adjustments to scope are a consideration.

- On-the-job training and evaluation of assistants: Assistants may need guidance, depending on their experience and ability. The EIC should encourage questions and ensure that someone is available to provide guidance. Depending on the size of the job, the EIC should be familiar with the work performed by the assistant(s) so that you can make fair and constructive evaluations of the work performed.
- Ensuring that PERK information is received and distributed: The PERK is sent to the institution prior to the beginning of the examination. The EIC should set up controls to ensure that all information requested is received as early as possible. The EIC should also list any other items needed and submit the list to the contact person as early as possible to allow time for preparation by institution personnel. Encourage institution personnel to ask questions if instructions for preparation of requested information are unclear.
- Serving as the primary communications link: The EIC is the focal point for communications on significant matters. Assistants, institution personnel, and regional office staff must all know how to communicate information and when to share information. During examinations it is important that answers to significant items be given by only one responsible individual. The EIC should coordinate this in case questions arise.
- Ensuring a cooperative and positive working environment: Conduct examinations with as little disruption, conflict, and confusion as possible. A positive work environment fosters the productivity of the team members. Disagreements will occur at times, but avoid an antagonistic role. Allow for regular meetings with management to discuss findings and questions, and avoid monopolizing the time of the staff as much as possible. A professional and considerate approach usually results in cooperation from the institution staff.

- Determining that the examination meets the overall examination objectives: At the conclusion of the examination, the EIC should ensure that the examination meets the objectives and that examiners followed appropriate procedures for all examination functions.

### **Off-Site Examination Procedures**

On-site examinations are essential to OTS's mission; however, some examination procedures may be conducted off site as proficiently as they can be conducted on site. Given the overall health of the industry and the experience level of the examination staff, the OTS may be able to fulfill its examination responsibilities at many institutions and limit on-site examination time.

Performing examination procedures off site is optional. Regional directors or their designee should determine whether off-site examinations are feasible and develop appropriate policies and procedures.

An off-site examination does not replace an on-site examination. In simple terms, more procedures may be performed off site at the beginning and end of an examination. Some of the advantages of performing procedures off site may include reduction in travel expenses and a reduction in the disruption to normal thrift operations attendant with even the best-run examinations.

### *Institution Selection Criteria and Examination Procedures*

You should determine whether off-site examination procedures may be used in an institution based on certain criteria, including the institution's CAMELS rating, prior history, complexity of operations, reliability of data, and other factors. Typically, small, highly rated institutions would be the most likely candidates for these procedures. You should be able to demonstrate that a tangible benefit can be gained from using off-site examination procedures.

The exact combination of on-site and off-site work is a function of relevant factors unique to the institution and the examination crew. Flexibil-

ity is retained through the absence of any firm guidelines such as asset size, rating, or location where an off-site examination may or may not be conducted. Open lines of communication with institution personnel are essential at all examinations, but extra steps may have to be taken to keep those lines open during off-site portions of the examination. Advise thrift management of the start and completion of off-site work. Finally, exercise judgment so that work that is best performed on site is performed on site.

#### *PERK*

You may revise the PERK letter to alert institution management that some of the examination work will be conducted off site.

As discussed in greater detail in this section, you may request PERK information from institution management in several ways:

- Complete the information prior to the start of the examination.
- Provide the information at examination commencement.
- Make the information available for on-site review.

Unless it is practical to retrieve items from the institution, at least some items should be requested in advance for delivery to the field office or other appropriate location. If you select this option, the PERK should go out a few days earlier than recommended in the normal customer service standards.

Do not require thrifts to photocopy and ship materials to examiners if it creates rather than reduces regulatory burden. Regulatory staff will have to gauge the resources and attitudes of each thrift examined using off-site examination procedures. Again, keep open the lines of communication with management.

#### *Examination Data System I & II*

Examination Data System (EDS) I and II should continue to reflect the actual start and completion dates of examination work performed on site. The dates used for EDS I and II should correspond with the dates disclosed in the cover page of the examination report.

#### *Scoping*

Scoping may be done off site and on site. See the discussion presented earlier in this Section on Examination Scoping.

#### *Examination "Entrance" Meeting*

At the initiation of the examination, hold a meeting with management. Discuss examination objectives, examiner assignments, and any other relative administrative issues. This meeting can be held by telephone, or in person if distance permits. In addition to an entrance meeting, the EIC should conduct weekly meetings (by telephone if off site) with the appropriate institution personnel to discuss current findings, as required by the OTS Customer Service Plan.

#### *Suggested Off-Site Examination Procedures*

Other than asset review and TFR verification, many of the examination procedures could potentially be completed off site, as long as the appropriate information is obtained. The following is a partial list of examination procedures that could be considered for off-site completion. Again, flexibility is the operative word. If the procedures listed below or any other procedures can be efficiently performed in whole or in part off site, consider doing them off site during the time frame assigned to an off-site office.

#### Capital

- Review SEC filings and pertinent correspondence.
- Evaluate adequacy of and trends in capital.
- Evaluate management reports and the business plan to determine adequacy of capital

planning, earnings retention, and dividend policy.

- Outline and draft comment.

### Asset Quality

- Review applicable policies, as deemed necessary (loan, investment, appraisal, etc.).
- Identify asset review samples.
- Review internal loan review procedures and resulting reports.
- Review asset quality trends to determine any potential areas of concern. Stratify loan data in pivot tables to identify concentrations, sources of delinquencies (loan type, loan age, loan office), etc.
- Evaluate the adequacy of loss allowances.
- Review regulatory limitations.

### Management

- Review business/strategic plan.
- Review employment contracts.
- Review completed management questionnaire.
- Review internal/external audit reports.
- Review electronic data processing agreements.

### Earnings

- Review financial reports.
- Identify earnings components, identify trends, and assess results.
- Review budget and the planning/monitoring processes.
- Outline or draft comment.

### Liquidity

- Review applicable policies and procedures.
- Outline or draft comment.

### Sensitivity to Market Risk

- Review applicable policies and procedures.
- Review IRR modeling and assess the institution's exposure position.
- Determine overall funds management strategies.

### Administrative

- Construct work paper files.
- Prepare/finish ROE.

### **Examination Conclusion**

At the conclusion of the examination, review the examination report and update the regulatory plan. Also ensure that the institution takes prompt corrective action for any problems found during the examination and closely monitor the institution's condition for any recurrence of these or new problems.

OTS regional staff must send the report of examination to 1- and 2-rated institutions within 30 days and to 3-, 4-, and 5-rated institutions within 45 days from completion of on-site examination activities.

Refer to Thrift Activities Regulatory Handbook Section 070, Overall Conclusions, and Section 320, Meetings with the Board of Directors, for other appropriate examination closing procedures.

### **OTS/FDIC Joint Examinations Process**

The OTS and FDIC regional staffs should meet regularly to review the examination schedule. The FDIC should indicate those examinations in which they desire joint participation. All FDIC savings association examination activities will be performed on a joint basis unless compelling reasons dictate otherwise.

For joint examinations, the FDIC and OTS should jointly scope the examination at the EIC level or at the respective regional office level. Disagreements over scope should default to the broader alternative. When examinations of savings association affiliates are considered necessary, the EIC should decide how to conduct the examinations.

For non-joint examinations, the OTS should determine the scope and provide the FDIC a copy of the proposed final report and allow a ten-day period for review and comment prior to the OTS transmission to the institution.

OTS is responsible for specialty examinations.

Nothing in the joint OTS/FDIC agreement should alter the normal examination and supervisory cooperation with state authorities.

*Report of Examination*

Joint examinations will represent a division of responsibilities among the joint staff; the OTS and FDIC should each provide an EIC, who will share responsibility for managing the examination and will be responsible for resolving interagency differences during the examination process. EICs of both agencies should coordinate and communicate during the examination to assure examination objectives are achieved with a minimum of redundancy.

The FDIC's ROE will be for internal purposes only, although they will provide a copy to the OTS. If the FDIC Board authorizes an enforcement action, however, the FDIC would then transmit its examination report to the institution. As the OTS and FDIC regional staffs prepare the concurrent reports, they should attempt to resolve all significant differences of opinion concerning the thrift's overall condition and the enforcement or corrective action needed.

The OTS view will prevail concerning non-substantive differences in examination interpretations, conclusions, and report comments. Substantive differences in examination conclusions that could lead to an enforcement action by the FDIC if not pursued by OTS, and that the EIC cannot resolve, should be referred to the OTS and FDIC regional offices for resolution at the time such differences are identified. The regional offices must resolve such differences within ten working days. If they cannot resolve such differences following full review and communication between the regional offices within ten working days, the regional offices refer the matter to the FDIC Director of Supervision and OTS Deputy Director. It is expected that they will resolve such differences within ten working days. If the differences remain unresolved, the FDIC should so notify OTS of the differences and that they will

seek corrective action authorization from the FDIC Board.

Prepare the OTS examination report using GAAP as the appropriate accounting treatment for financial accounting information. Use OTS regulations, policies, and directives in reaching examination conclusions.

The OTS and FDIC should routinely copy one another on institution-related correspondence. The OTS provides the FDIC with copies of examination-related correspondence.

Examination work papers, loan line sheets, report pages, and findings should be shared, but retained by the OTS following completion of the examination, with interim examination access provided to the FDIC upon request.

*Board of Directors Meeting*

The OTS and FDIC should jointly participate in examination-related meetings with management and directors during and at the conclusion of joint examinations.

The FDIC should communicate all actions taken by the FDIC Board to the institution after notification to the OTS.

*Enforcement Actions*

The OTS regional director should endeavor to advise the FDIC regional director of, and solicit written input on, all proposed OTS enforcement actions. The FDIC will have ten working days to respond. The OTS regional director should provide the FDIC regional director with a copy of the final enforcement document within five working days of execution. The OTS regional director should also provide a written explanation of the reasons why OTS did not take any of the FDIC-recommended actions.

Likewise, the FDIC regional director should endeavor to advise the OTS regional director of, and solicit written input on, all proposed FDIC enforcement actions. The OTS will have ten working days to respond. The FDIC regional di-

rector should provide the OTS regional director with a copy of the final recommendation to Washington. The FDIC regional director should also provide a written explanation of the reasons why the FDIC did not take any of the OTS-recommended actions.

Regional staff should resolve significant differences concerning corrective and enforcement actions. If regional staff cannot resolve a significant issue, they should submit the issue to the FDIC Director of Supervision and the OTS Deputy Director. It is expected that they will resolve such differences within fifteen working days. If the differences are irresolvable, the FDIC can recommend backup action to the FDIC Board. The FDIC should not direct corrective action until the FDIC Board authorizes such action.

#### *Divestiture Plans/Brokered Deposit Waivers*

The FDIC regional director should advise the OTS regional director of its intent to approve or deny, or otherwise exercise its independent authority with respect to a divestiture plan or brokered deposit waiver, prior to communication with the thrift institution.

The FDIC should coordinate its efforts with the OTS to ensure that such actions are consistent with OTS-approved capital plans, as long as conditions at the savings association have not changed to any material extent (in the opinion of FDIC).

#### *Capital Plans*

The OTS addresses inadequate capital in savings associations as required by 12 CFR Parts 565 and 567, or through the impositions of an individual minimum capital requirement, or through other enforcement action.

The OTS regional director should provide copies of capital plans, revisions and modifications, requests for additional information, and proposed actions to the FDIC regional director for review and comment. Unless the FDIC regional director submits to the OTS regional director a written objection to the capital plan within thirty working

days, the FDIC will normally not take backup enforcement action or action on divestiture plans that are contrary to the action taken by the OTS in approving a capital plan.

The FDIC regional director and the OTS regional director should resolve any differences with respect to capital plans. The regional directors should refer significant issues they cannot resolve to the OTS Deputy Director and the FDIC Director of Supervision. If such issues remain unresolved, the OTS may then approve the capital plan, but the FDIC may pursue backup enforcement action to resolve its concerns.

### **REFERENCES**

#### **Code of Federal Regulations (12 CFR)**

§ 563.171 Frequency of Examinations

#### **Office of Thrift Supervision Bulletins**

TB 68 Supervisory Review, Appeal and Reconsideration Process and Ombudsman Matters

#### **Closely Related Thrift Activities Regulatory Handbook Sections**

Section 010	Handbook Use
Section 011	Program Use
Section 040	EDS/ROE
Section 045	Regulatory Action Data System (RAD)
Section 050	Regulatory Plan
Section 070	Overall Conclusions
Section 071	CAMELS Ratings

#### **OTS Report of Examination Instructions Manual for Safety and Soundness Examinations**

#### **FFIEC Guidelines for Relying on State Examinations (June 27, 1995)**