

# Chapter 22

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## EXAMINATION EVALUATION AND REVIEW POLICY

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## Chapter 22

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# EXAMINATION EVALUATION AND REVIEW POLICY

### **Examination Evaluation and Review Objectives**

- Communicate consistent feedback regarding the overall quality of examiner work in a timely manner
- Measure the quality and effectiveness of NCUA's examination and supervision program by assessing the quality of examiner problem identification, recommendations for resolution and risk mitigation, and effectiveness of communication with officials
- Provide feedback for improving the examination and supervision program to management and the examiner

### **Associated Risks**

Although the associated risks in this chapter do not apply to the examination evaluations and reviews, the quality of the examination report can cause risk to the National Credit Union Share Insurance Fund (NCUSIF.)

### **Overview**

For purposes of staff development and quality control, NCUA evaluates and reviews examination reports. The process occurs at two levels:

- Supervisory examiners in the field evaluate all of the examiners' work as part of the examiner's development and overall appraisal; and
- Division of supervision (DOS) analysts perform a quality control function, and as such, limit their review to the written reports.

Supervisory examiners have responsibility for developing staff and ensuring the effectiveness of the examination and supervision program. To meet these responsibilities, they encourage the district examiners to perform high quality examinations and supervision. The Supervisory Examiner (SE) Evaluation commends the examiners for high quality work, provides guidance to examiners, and informs examiners of needed improvements in their work.

DOS analysts review reports to identify existing or emerging trends, common or frequently occurring findings, and systemic risk factors. DOS can further observe trends within the credit unions (e.g., increases in member business loans, decreases in net worth) and trends in the examination process (e.g., decrease in consumer compliance reviews, misinterpretation of ALLL criteria.)

After DOS identifies and analyzes region- or area-wide findings, trends, and risks, they communicate resulting information as appropriate. Sharing of this information in a timely manner will enable NCUA to determine the extent of the situation under review, monitor it for further developments, and take action when necessary.

The “Selecting Reports for Evaluation and Review” section of this chapter sets forth the national standard minimum criteria for reports requiring an SE Evaluation or a DOS Review. The regional office may adopt additional criteria thereby increasing reports they review to further assure quality control or to meet other regional objectives.

**Minimum Standards**

All regions adhere to the following minimum standards for evaluations and reviews, presented in priority order. Regions may add standards according to their needs.

**Supervisory Examiner Evaluations**

SE Evaluations serve as the basis for annual performance appraisals and staff development. These evaluations should determine the following:

- Examiners receive consistent, prompt feedback regarding the quality of their work, including the strengths, weaknesses, and suggestions for improving performance;
- Examiners prepare an appropriate and effective scope and report that adequately addresses risk, identifies problems, and makes sound recommendations to resolve major problems within acceptable time frames;
- Examiners have written a report that stands alone and documents a complete administrative record of the examination contact; and

- Examiners minimize NCUSIF losses through adequate identification and resolution of problems.

**DOS  
Reviews**

DOS Reviews focus on quality control and should address whether the report:

- Addresses risk through an appropriate and effective scope;
- Focuses on results and includes plans for correcting problems promptly;
- Addresses negative trends and includes sound recommendations to resolve major problems within acceptable time frames;
- Complies with uniform examination, insurance review, and supervision standards;
- Presents a stand-alone document of the examination contact; and
- Provides a complete administrative record of the examination contact.

**Selecting  
Reports for  
Evaluation and  
Review**

Supervisory examiners select at least five reports each year from each examiner for formal evaluation. They should make every effort to select the reports evenly throughout the year. When reviewing a report that addresses a specific risk area well, the supervisory examiner may determine that other examiners could benefit from the information presented and methods outlined in the report. They may choose to share this information for continuing staff development.

DOS, at a minimum, reviews reports meeting the following criteria:

- All credit unions coded CAMEL 4 or 5 with assets greater than \$100,000;
- All credit unions coded CAMEL 3 with assets greater than \$50 million;

- All credit unions coded CAMEL 3 for longer than 36 months and with assets greater than \$5 million;
- All credit unions with assets greater than \$250 million; and
- A selected sample of examinations and supervision contacts determined by the regional director.

NCUA's reviews of federally insured state-chartered credit unions (FISCUs) include at a minimum:

- Insurance reviews performed independently by NCUA, including supervision contacts designated by the regional director, using the above criteria; and
- Joint NCUA insurance review and state supervisory authority (SSA) examination reports, including supervision contact reviews designated by the regional director, using the above criteria.

**Independent Review and Feedback**

The supervisory examiner and DOS will conduct the evaluation and review processes independently. Both supervisory examiners and DOS will complete and disseminate their evaluations and reviews within 30 days of the report upload. Regional policy determines whether the region will release DOS Reviews to examiners.

Each region will develop its own policy to identify and resolve material differences between DOS Reviews and SE Evaluations.

**DOS Review**

The DOS Review will address the following:

1. Risk Identification;
2. Scope Development;
3. Proper Solutions;
4. Continuing Supervision/Examination Plans; and
5. Comments.

Appendix 22A contains a sample form for a DOS Review. This form contains the minimum elements regional office staff must include in

their reviews. In addition to these required elements, each regional director has the discretion to add other elements to these standard criteria and use whatever format best fulfills regional needs.

**Risk  
Identification**

Risk identification is the recognition of significant problems through the collection, analysis, and verification of data. The Scope Workbook and report will address and document material risks. The DOS review will determine whether the report:

- Properly assessed and appropriately rated risks (low, moderate, or high) from the seven major risk areas (strategic, interest rate, credit, liquidity, transaction, compliance, and reputation) and reasonably determined the direction of the risks (increasing, decreasing, or unchanged);
- Identified and discussed areas with high or increasing risk (moderate or high risk rating) including (1) the underlying cause; (2) the problem's severity, duration, and effect on the credit union's financial condition; and (3) deficiencies in policies, processes, personnel, and control systems (refer to the Risk-Focused Program chapter);
- Identified and discussed material negative financial trends (e.g., key ratios, loan analysis, liquidity and funds management, shares and deposits, capital evaluation, etc.);
- Supported conclusions using the Total Analysis Process (TAP) considering both quantitative and qualitative data;
- Stated clearly that credit union officials acknowledged or refused to acknowledge the existence of risks, problems, and weaknesses; and
- Supported CAMEL ratings consistent with risk ratings and in accordance with current NCUA guidance.

**Scope  
Development**

Scope development involves the process of evaluating the potential for loss, and building examination procedures to review risk areas.

Examiners require proficiency in developing the scope when performing a risk-focused examination. Regional office staff assesses whether the Scope Workbook:

- Contained a preliminary risk assessment using historical examination information, current financial data, 5300 data (risk management reports and Financial Performance Reports [FPRs]), and local economic factors;
- Included modifications to the preliminary scope based on examination analysis, unforeseen issues, and emerging problems; and
- Documented sufficient examination procedures used to evaluate the risk areas using *process* (e.g., review of policies and procedures) and *transactional* procedures to ensure high-risk areas received in-depth review and low-risk areas only a limited review.

**Proper  
Solutions**

The report's effectiveness depends on the development and communication of proper resolutions for the risks and problems identified both during the scope development and the examination. The analyst will evaluate the recommendations for problem resolution, timeliness, and effectiveness. The DOS Review will include an analysis of whether:

- The Overview:
  - Summarizes the risk profile, conditions, problems, and probable effect of problems on operations and financial condition; and
  - Documents the plan for handling severe or persistent problems clearly and provides information to officials concerning consequences of inadequate action if management does not correct noted problems by the next contact;
- The Document of Resolution:
  - Contains reasonable, effective, and timely corrective action plans.

**Continuing Supervision/ Examination Plans** Regional analysts will determine whether the Scope Workbook focuses on continuing supervision and/or monitoring the financial condition of the credit union and existing and potential material risks.

**Comments** Regional office staff will use the Comments section of the DOS Review for items that do not fall under the other criteria as explained above.

**SE Evaluation** The SE Evaluation will address the following:

1. Risk Identification;
2. Scope Development/Resource Allocation;
3. Proper Solutions;
4. Form;
5. Continuing Supervision/Examination Plans; and
6. Comments.

Appendix 22A contains a sample form for an SE Evaluation. This form contains the minimum elements supervisory examiners must include in their evaluations. Each regional director has the discretion to add to these standard criteria and use whatever format best fulfills regional needs.

**Risk Identification** Risk identification involves comparing the scope to the examiner's analysis in the narrative sections of the report. The supervisory examiner determines whether the examiner:

- Properly identified, assessed, and rated risks (low, moderate, or high) from the seven major risk areas (strategic, interest rate, credit, liquidity, transaction, compliance, and reputation) and reasonably determined the direction of the risks (increasing, decreasing, or unchanged) using appropriate workpapers;
- Used the Total Analysis Process (TAP) to consider both quantitative and qualitative data, weigh relative importance of data, check accuracy, and reach and support valid conclusions;



- Adequately discussed major areas of risk (moderate or high risk rating) including (1) the underlying cause; (2) the problem's severity, duration, and effect on the credit union's financial condition; and (3) material deficiencies in policies, processes, personnel, and control systems (refer to the Risk-Focused Program and Report Writing chapters);
- Stated that credit union officials acknowledge or refuse to acknowledge the existence of risks, problems, and weaknesses;
- Assigned CAMEL ratings consistent with risk ratings and in accordance with current NCUA guidance.

**Scope  
Development and  
Resource  
Allocation**

The SE Evaluation will address the appropriateness of the scope and assess the examination process for the efficient use of resources. When evaluating scope development, the supervisory examiner considers whether the examiner:

- Performed and documented a preliminary risk assessment using historical examination information, current financial data, 5300 data (risk management reports and Financial Performance Reports [FPRs]), and local economic factors;
- Documented modifications to the preliminary scope based on examination analysis, unforeseen issues, and emerging problems; and
- Documented sufficient examination procedures used to evaluate the risk areas using *process* (e.g., review of policies and procedures) and *transactional* procedures to ensure high-risk areas received in-depth review and low-risk areas only a limited review.

When evaluating resource allocation, the supervisory examiner considers whether the examiner:

- Allocated resources appropriate to the risk posed by the credit union and consistent with the report's findings and recommendations;

- Used subject matter examiners (SMEs) to review complex areas with a significant degree of risk; and
- Documented material changes to the anticipated examination and supervision hours.

**Proper Solutions**

The examination's effectiveness depends on the development and communication of proper solutions for the risks and problems identified during the examination. The supervisory examiner will evaluate the timeliness and effectiveness of the solutions. The supervisory examiner will determine whether the report:

- Is clearly written for the credit union officials;
- Contains reasonable, effective corrective action plans;
- Assigns responsibility and deadlines for action and defines benchmarks, as necessary, to attain agreed-upon goals;
- Provides a realistic plan that will assist officials in resolving the problems, if followed; and
- Includes other information such as agreements reached during discussions with officials and other items as required by regional management.

The supervisory examiner will evaluate the examiner's interaction with management and officials at the joint conference or other exit meeting, if attended by the supervisory examiner.

**Report Form**

Form includes the clear and professional presentation of facts and solutions to credit union officials. The supervisory examiner determines whether the report exhibits the following:

- Complete, concise, and well-organized discussion and conclusions;
- Correct grammar, spelling, and punctuation; and
- Appropriate enhancements such as bolding, underlining, white space, graphics, and lists for presenting information.

**Continuing Supervision/ Examination Plans**

The supervisory examiner's evaluation will assess the examiner's recommendations for ongoing supervision and future examination plans. Plans should provide for timely and appropriate supervision to ensure prompt resolution of problems and implementation of adequate measures to control risk. The supervisory examiner will evaluate continuing supervision and examination plans to ensure they:

- Focus on material risk-related areas;
- Monitor the condition of the credit union efficiently and effectively (may include informal discussions with management and onsite contacts targeting specific areas of risk);
- Address future plans regarding any outstanding administrative action (Discretionary Supervisory Actions, Letters of Understanding and Agreement, Preliminary Warning Letters, Cease and Desist Orders, Net Worth Restoration Plans, etc.);
- Project resources needs for future contacts (hours and examiners needed, including a specialist or subject matter examiner (SME)) consistent with the report's findings and recommendations.

**Comments**

The supervisory examiner will use the Comments section of the SE Evaluation form for items that do not fall under the other criteria, as explained above.

**SE Evaluation Summary**

Narrative comments clearly document the supervisory examiner's evaluation of an examination report. Supervisory examiners will not rate a report using the terminology "exceeds standards," "meets standards," "minimally meets standards," or "does not meet standards." These terms have specific meanings for the year-end appraisal process; supervisory examiners should limit the use of these terms to that purpose only.

If a supervisory examiner notes material deficiencies with an examination report, the supervisory examiner discusses these with the examiner, who then signs the evaluation form and returns it to the supervisory examiner.

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If the supervisory examiner notes no material deficiencies, discussion of the report occurs at the option of the supervisory examiner or examiner. The examiner's signature on the evaluation form is optional at the supervisory examiner's discretion.

The supervisory examiner will submit evaluations to the regional office in accordance with regional policy.

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# DOS REVIEW AND SE EVALUATION FORMS - APPENDIX 22A

## DOS Review

## Sample DOS Review Form

Examiner:		SE:	
CU #:		CU Name:	
CAMEL:		Assets:	
Effective Date:		Reviewer:	
Date Completed:		Hours to Complete Exam:	
Date Received:			
Date Reviewed:		Contact Type:	

### CATEGORIES OF RISK:

Risk Category	Examiner Assessment	Risk Category	Examiner Assessment
Credit		Interest Rate	
Liquidity		Transaction	
Compliance		Strategic	
Reputation			

RISK IDENTIFICATION

SCOPE DEVELOPMENT

PROPER SOLUTIONS

CONTINUING SUPERVISION/EXAMINATION PLANS

COMMENTS

**SE Evaluation**

**Sample SE Evaluation Form**

CU Name:		Examiner:	
CU#:		SE:	
Assets:		Date Exam Completed:	
CAMEL Comp:		Date Report Received:	
Days Exam Open:		Date Report Appraised:	
Effective Date:		Budget Hrs:	
Hours Charged:		Contact Type:	

**CATEGORIES OF RISK:**

Risk Category	Examiner Assessment	Risk Category	Examiner Assessment
Credit		Interest Rate	
Liquidity		Transaction	
Compliance		Strategic	
Reputation			

RISK IDENTIFICATION: \_\_\_\_\_

SCOPE DEVELOPMENT/RESOURCE ALLOCATION: \_\_\_\_\_

PROPER SOLUTIONS: \_\_\_\_\_

FORM: \_\_\_\_\_

CONTINUING SUPERVISION/EXAMINATION PLANS: \_\_\_\_\_

COMMENTS: \_\_\_\_\_  
\_\_\_\_\_

Supervisory Examiner: \_\_\_\_\_ Date: \_\_\_\_\_

I have reviewed this evaluation and discussed its contents with my Supervisor.

Examiner's Signature: \_\_\_\_\_ Date: \_\_\_\_\_

(Optional at the SE's discretion unless the evaluation noted material deficiencies.)

Examiner's Comments: (Affix additional pages if necessary)

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# STATE CREDIT UNION REPORT REVIEWS - APPENDIX 22B

## **State Credit Union Report Reviews**

NCUA examiners review state examination reports to determine the risk state-chartered credit unions pose to the National Credit Union Share Insurance Fund (NCUSIF.) Because economic conditions or circumstances may vary from one region to another, the regional directors may require that examiners expand the procedures outlined in this appendix and provide additional documentation.

At a minimum, the NCUA examiner-reviewer (reviewer), after analyzing the state supervisory authority's (SSA) examination report, scope workbook, and any other pertinent information, assesses the operational and financial condition of the credit union. In addition, the reviewer determines if the SSA followed up on problems from the prior examination, identified material risk areas during the current examination, addressed weaknesses, and reached agreement with the officials to resolve the problems and appropriately manage the risk.

Examiners and regional staff must treat information obtained from the state examination report reviews as confidential. The region may distribute the information to the SSA according to the agreements between the regional director and each SSA.

## **Assigning FISCUs to Examiner Districts**

Supervisory examiners normally assign district responsibility, including state examination report reviews for federally insured state-chartered credit unions (FISCUs) to examiners based on factors such as their experience level, technical ability, and areas of expertise. The supervisory examiner also considers the credit union's asset size, complexity, quality of operations, and geographical location.

Supervisory examiners monitor the state examination report reviews to ensure that reviewers promptly complete high-quality state examination report reviews that are both accurate in content and appropriate in their recommendations.

While it is the mission of NCUA, as the insurer, to ascertain the safe and sound operation of FISCUs, examiners must remember that

primary responsibility for the supervision of state-chartered credit unions rests with the SSA. NCUA examiners should demonstrate a courteous, professional, and cooperative attitude in all communications (including state report reviews) and contacts with the SSAs and their staff members.

**Processing and Reviewing State Examination Reports and Scope Workbooks**

Upon receipt of the report and scope workbook, reviewers will:

- Review the state examination report, scope workbook, financial performance, and any other information pertinent to the credit union (e.g., risk reports, Consolidated Balance Sheet, Financial Performance Reports);
- Complete the Examiner Contact Information and upload it to the host system within regional time frames;
- Complete a state examination report review within the scope workbook and any other work papers required by the regional director; and
- Upload the scope workbook within regional time frames.

**State Examination Review Scope Workbook**

Examiners will use the Code 26 function within the scope workbook to document their analysis of state examinations and the review process. The scope workbook contains instructions for specific steps on completing and uploading the Code 26 scope workbook.

Reviewing the state examination report and scope workbook should enable the reviewer to answer the following questions:

- Did the SSA examination report identify material risk areas?
- Did the SSA examination report offer appropriate solutions to reduce unacceptable risks?
- Was the scope of the examination appropriate given the risk profile of the credit union?
- Did the examination report provide adequate documentation supporting the work performed and the conclusions drawn?



- Are the supervision plans outlined by the SSA adequate given the credit union's risk profile?

If the NCUA and state CAMEL composite ratings differ, the reviewer must present the specific facts, ratios, and justifications to support the basis for the NCUA examiner's position. The reviewer, while supporting the NCUA CAMEL rating, should avoid subjective comments critical of, or antagonistic to, the state examination program, the state regulator, or the state examiner. Examiners will inform their supervisory examiners when assigning a composite CAMEL rating different from the state's rating when the variance in the composite ratings will necessitate an onsite contact. NCUA may use the support presented by the reviewer to enhance NCUA's position to the SSA in those instances where the supervisory examiner finds it necessary to schedule a joint contact.

# State Examination Report Review Summary

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<b>Ins. #:</b>	<b>CU Name:</b>
<b>State:</b>	<b>Exam Effective Date:</b>
<b>State Examiner (EIC):</b>	<b>Exam Assets:</b>
<b>Date SSA Report Received from RO:</b>	<b>NCUA Ex.-Reviewer:</b>
<b>Date NCUA Review Mailed to RO:</b>	<b>Exam Contact Type:</b>

Through the review of the state examination report, the examiner should determine the credit union's financial and operational condition and provide sufficient quantitative and qualitative data to substantiate the analysis and assignment of the CAMEL component and composite ratings. Current and past trends, effectiveness of problem resolution from prior examinations, agreements with officials to correct problems, and results of previous supervision contacts should be addressed in this review. Examiners should base the extent of the narrative on the risk, size and complexity of the credit union and severity of the problems noted.

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**COMPOSITE CODE:**                      **NCUA CODE** \_\_\_\_\_ **STATE CODE** \_\_\_\_\_

**CAPITAL ADEQUACY:**                      **NCUA CODE** \_\_\_\_\_ **STATE CODE** \_\_\_\_\_  
 (Discussion should include past, future, and current aspects of capital.)

**ASSET QUALITY:**                      **NCUA CODE** \_\_\_\_\_ **STATE CODE** \_\_\_\_\_  
 (Discussion should include loan programs, quality of lending, appropriateness of investments, fixed assets, etc.)

**MANAGEMENT:**                      **NCUA CODE** \_\_\_\_\_ **STATE CODE** \_\_\_\_\_  
 (Discussion should include supervisory committee audit and verification, policies and procedures, record keeping, problem resolution, etc.)

**EARNINGS:**                      **NCUA CODE** \_\_\_\_\_ **STATE CODE** \_\_\_\_\_  
 (Discussion should include the various components of the income statement (e.g., gross income, operating expenses, and the cost of funds.)

**LIQUIDITY MANAGEMENT:** **NCUA CODE** \_\_\_\_\_ **STATE CODE** \_\_\_\_\_  
 (Discussion should address the adequacy of liquidity and appropriateness of the ALM policy.)

**Attachment 22.1**

**EXAMINER'S GUIDE**

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**INSURABILITY REQUIREMENTS:** (Does the report provide adequate information to assess compliance with part 741 of the NCUA Rules and Regulations, including the Requirement for Insurance, and with applicable federal consumer regulations?)

**APPROPRIATENESS OF SSA PROBLEM RESOLUTIONS AND FOLLOW-UP PLANS:** (Does the report provide documents of resolution and examiner's findings and are they appropriate and adequate? List any supervision plans the SSA has provided in the report. (Please indicate if none are provided.))

**NCUA EXAMINER RECOMMENDATIONS:** (Are offsite supervision and monitoring plans or formal onsite supervision plans appropriate given the condition of the FISCU?)

**OTHER ITEMS:**

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**REGIONAL OFFICE COMMENTS:**

The information contained on this form is based on our review of the state examination report.

**Attachment 22.1**

22 B-10