# Report on Underwriting Practices

Federal Deposit Insurance Corporation
Donna Tanoue, Chairman

## OCTOBER 1999 THROUGH MARCH 2000

### HIGHLIGHTS

- The potential risk associated with institutions' current underwriting practices for new lending remained low during the six months ending March 31, 2000—3 percent were reported as having "high" risk, down from 4 percent previously.
- The potential credit risk of institutions' overall loan portfolios also remained low during the six months ending March 31, 2000—3 percent were reported as having "high" risk, down from 4 percent previously.
- Examiners reported continued problems with agricultural loan "carryover debt" (loans not paid off at the end of the growing season) during the six months ending March 31, 2000, but among a lower proportion of banks than during the six months ending September 30, 1999.
- Examiners also reported slight increases in the frequency of two risky underwriting practices in construction lending during the six months ending March 31, 2000, compared with the six months ending September 30, 1999. Counterbalancing these concerns, however, were examiners' reports of generally stable, and often declining, frequencies of specific risky underwriting practices across the **major loan categories**.

## *INTRODUCTION*

At the end of each FDIC-supervised bank examination, the examiner-in-charge responds to a questionnaire on the bank's underwriting practices. This *Report on Underwriting Practices* covers the responses submitted during the six months beginning October 1, 1999, and ending March 31, 2000. The number of responses received during this six months was 1,158—which represents approximately 20 percent of the number and 24 percent of the assets of all FDIC-supervised banks. The results reported here refer to weighted responses and are *estimates* of the underwriting practices of all FDIC-supervised banks. An explanation of the use of weights appears in "Purpose and Design of the Report." All weighted responses appear in the table at the end of this *Report*.

## *GENERAL UNDERWRITING TRENDS*

During the six months ending March 31, 2000, examiners indicated that 90 percent of FDIC-supervised banks showed no material change in underwriting practices since the previous examination. The proportion of banks that had loosened their underwriting practices since the previous examination was larger than the proportion that had tightened them (6 percent and 4 percent).

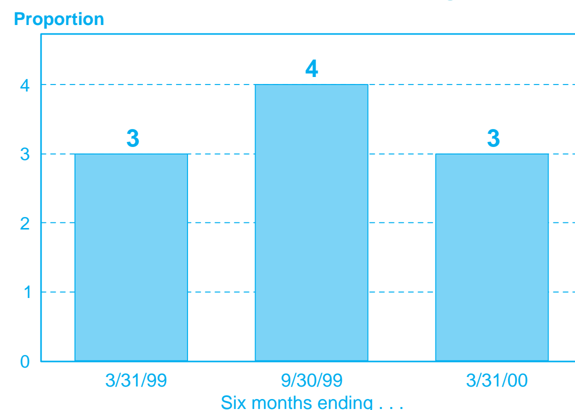
Examiners indicated that the main reasons for the loosening of underwriting practices were competition and/or a drive to meet growth goals; the reasons for the tightening were a need to respond to regulatory observations and/or a change in management.

Examiners also reported that the potential risk associated with institutions' current underwriting practices decreased slightly during the six months ending March 31, 2000, compared with the six months ending September 30, 1999. For example, the proportion of banks with "high" risk associated with institutions' current underwriting practices fell to 3 percent from the previous 4 percent.

Furthermore, the proportion of banks with an absolute level of "high" potential credit in their loan portfolios also dropped—to 3 percent from 4 percent.

The most noteworthy changes for FDIC-supervised banks during the six months ending March 31, 2000, compared with the previous six months ending September 30, 1999, were a decrease in the proportion of banks with "high" risk associated with loan growth and/or with significant changes in lending activities since the previous examination and a decrease in the risk associated with loan administration.

**Proportion of FDIC-Supervised Banks with "High" Risk Associated with Current Underwriting Practices**

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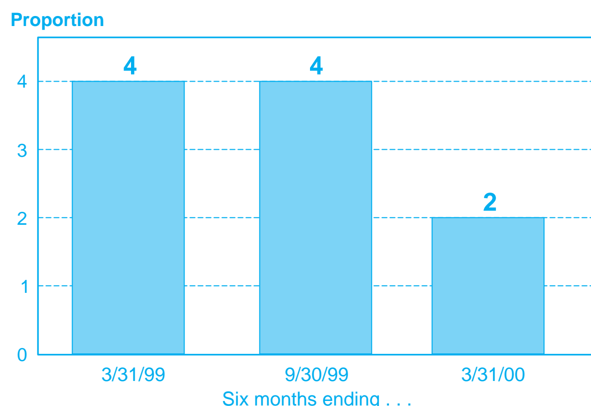
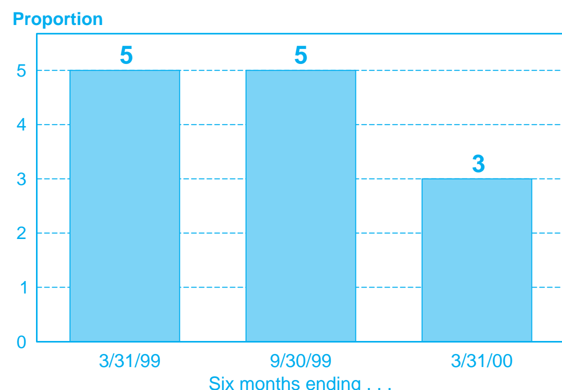



Also noteworthy was the declining proportion of FDIC-supervised banks that engaged in out-of-area financing either "frequently enough to warrant notice" or "commonly or as standard procedure": the proportion decreased to 12 percent from 13 percent. The proportion that failed to adjust loan pricing on different-quality loans to reflect differences in risk either "frequently enough to warrant notice" or "commonly or as standard procedure" also decreased—to 12 percent from 14 percent. The proportion of banks making loans in amounts that resulted in—or contributed to—concentrations of credit to one borrower or industry either "frequently enough to warrant notice" or "commonly or as standard procedure" remained unchanged—21 percent.

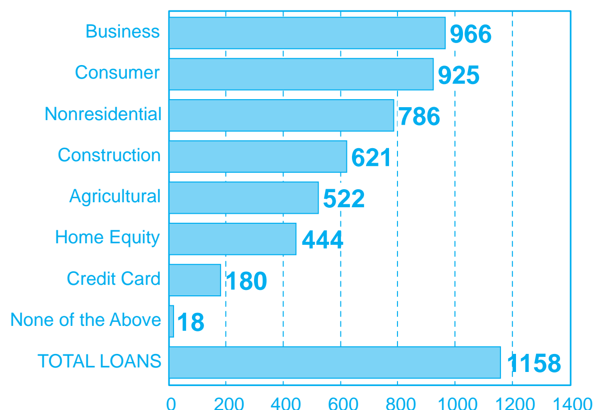
Of the 1,158 banks examined, 215 used a credit scoring model for credit decisions; the model was used most frequently (101 banks) for consumer installment lending.




## *INDIVIDUAL LOAN CATEGORIES*

During the six months ending March 31, 2000, 966 of the 1,158 banks examined were active business lenders; 925 were actively making consumer loans (excluding credit cards); and 786 were actively making commercial (nonresidential) real estate loans. Eighteen banks were not active in any of the major loan categories covered. The numbers for all of the major loan categories are shown in the accompanying chart.

Examiners are also asked to report additional loan categories (those not listed in the chart) in which the institution may be active.[1] Only 223 banks examined had activity in additional loan categories, with the largest number (108) having dealer paper loans.

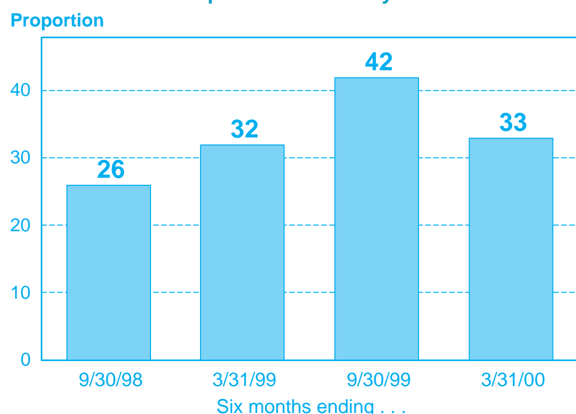



During the six months ending March 31, 2000, examiners reported slight increases in the frequency of two risky underwriting practices in construction lending, compared with the six months ending September 30, 1999. Examiners also reported continued problems with agricultural loan "carryover debt" (loans not paid off at the end of the growing season), but among a lower proportion of banks than during the six months ending September 30, 1999. Some examiners noted that government farm support programs were contributing heavily to farm income. For all loan categories, some examiners expressed concern about the lack of proper loan documentation and improper monitoring of loans. Counterbalancing these concerns, however, were examiners' reports of generally stable, and often declining, frequencies of specific risky underwriting practices across the **major loan categories**.

### *Agricultural Loans*

For FDIC-supervised banks active in agricultural lending, examiners reported a decrease in the proportion having a "moderate" or a "sharp" increase in the bank's level of carryover debt—the first drop in the proportion since the six months ending March 31, 1998. In both 1998 and 1999, Congress passed legislation specifically directed to address low commodity prices and weather problems affecting selected commodities. In 1999, total direct government payments added approximately $22.7 billion in assistance to the agricultural sector. According to the U.S. Department of Agriculture, the direct payments received by farmers in 1999 topped the previous record set in 1987, both in nominal and real terms.

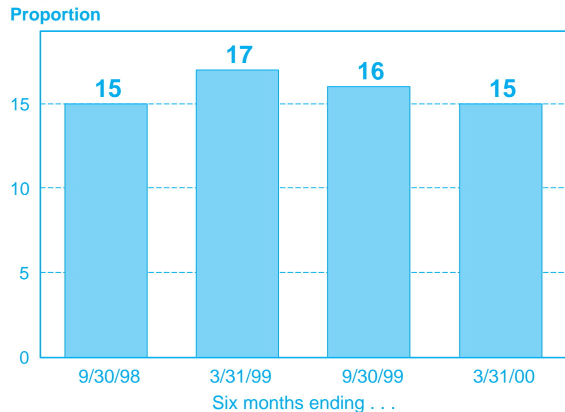
[1] The section "Purpose and Design of the Report" lists additional loan categories.




In general, examiners noted little change in the frequency of risky practices for agricultural lending at FDIC-supervised banks that were actively making agricultural loans. For example, 14 percent made agricultural loans on the basis of land values that cannot be supported by farm operations either "frequently enough to warrant notice" or "commonly or as standard procedure" (unchanged from previously). Forty-six percent had portfolios tied to crops affected by the Federal Agricultural Improvement and Reform Act of 1996[2] either "frequently enough to warrant notice" or "commonly or as standard procedure" (up slightly from 45 percent previously). And 14 percent made agricultural loans on the basis of unrealistic cash flow projections either "frequently enough to warrant notice" or "commonly or as standard procedure" (down from 16 percent previously).

## *Business Loans*

The frequency of specific risky underwriting practices in business lending changed only slightly compared with the six months ending September 30, 1999. The proportion of FDIC-supervised banks making business loans




[2] In contrast to previous law, which allowed traditional subsidies tied to prices and limits on production, this law allowed declining payments to farmers until the year 2002 for certain crops.

that did so without a clear and reasonably predictable repayment source either "frequently enough to warrant notice" or "commonly or as standard procedure" decreased slightly (to 15 percent from 16 percent).

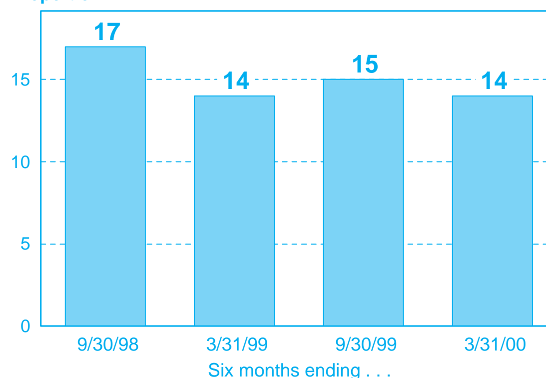
Also down slightly (to 20 percent from 21 percent) was the proportion of banks making business loans that failed to monitor the collateral pledged on asset-based loans either "frequently enough to warrant notice" or "commonly or as standard procedure."

The proportion that made business loans to borrowers who lacked documented financial strength to support such lending either "frequently enough to warrant notice" or "commonly or as standard procedure" remained the same, 20 percent.

## *Consumer Loans (Excluding Credit Card Lending)*

For FDIC-supervised banks active in consumer lending (excluding credit card loans), the frequency of specific risky underwriting practices changed only slightly during the six months ending March 31, 2000, compared with the six months ending September 30, 1999. Fourteen percent made "secured" consumer loans without adequate collateral protection either "frequently enough to warrant notice" or "commonly or as standard procedure" (down slightly, from 15 percent previously).

Seventeen percent made loans to borrowers who lack a demonstrable ability to repay either "frequently enough to warrant notice" or "commonly or as standard procedure" (unchanged from previously).

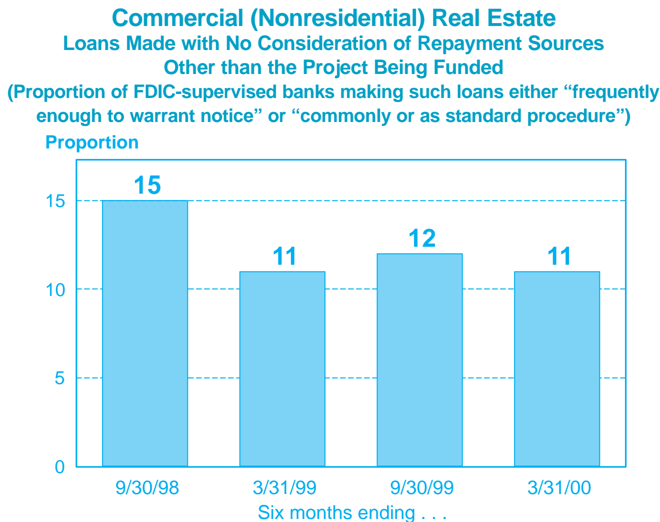



## *Commercial (Nonresidential) Real Estate Loans*

The frequency of specific risky underwriting practices was slightly lower compared with the six months ending September 30, 1999. Of the FDIC-supervised banks actively making commercial (nonresidential) real estate loans, 11 percent made such loans without considering sources of repayment other than the project being funded either "frequently enough to warrant notice" or "commonly or as standard procedure" (down slightly, from 12 percent previously).

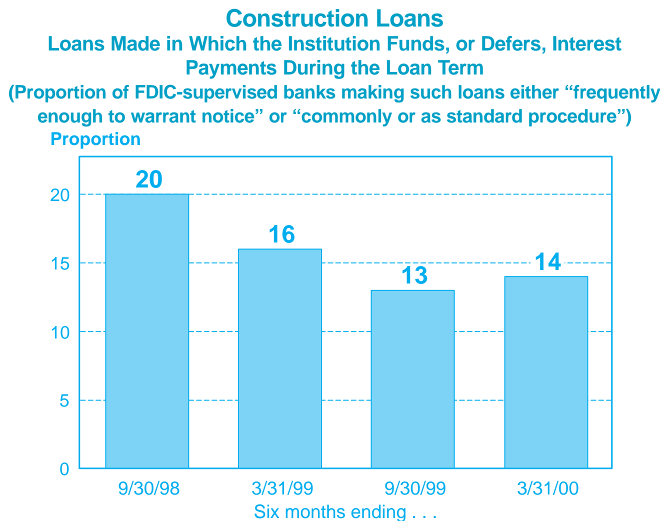
Seventeen percent made short-term loans with minimal amortization and large balloon payments either "fre-

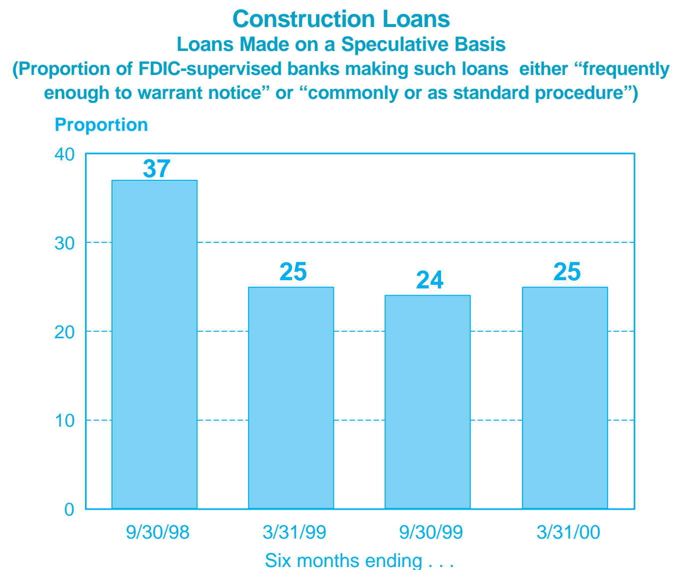
quently enough to warrant notice" or "commonly or as standard procedure" (down slightly, from 18 percent previously). And 7 percent made interest-only, extended-amortization, or negative-amortization permanent commercial real estate loans either "frequently enough to warrant notice" or "commonly or as standard procedure" (unchanged from previously).




## *Construction Loans*

The frequency of specific risky underwriting practices in construction lending increased slightly compared with the six months ending September 30, 1999, for two specific risky underwriting practices. One of the practices was funding, or deferring, interest payments during the loan term. The proportion of banks doing so "commonly or as standard procedure" rose to 6 percent from 3 percent previously. Although this practice is not unusual in construction lending, an increase in the frequency of banks making such loans "commonly or as standard procedure" indicates that this practice should be watched. When the proportion of banks doing so "frequently enough to warrant notice" was added in, however, the combined proportion increased only slightly, to 14 percent from 13 percent previously.



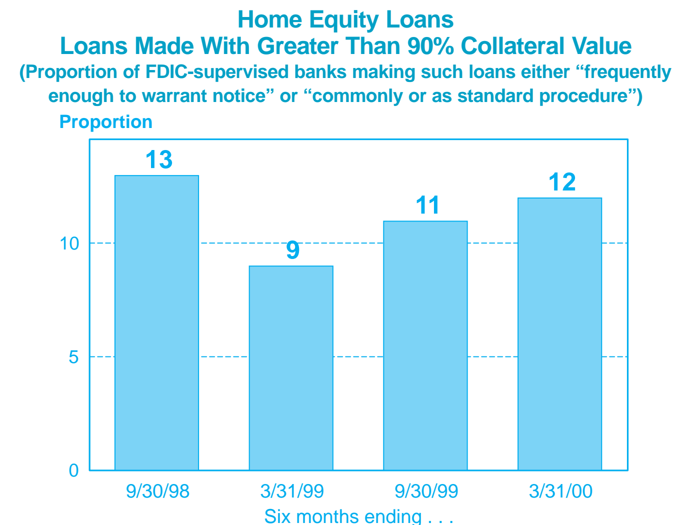




The other practice that increased in frequency was the proportion of banks making speculative construction loans (that is, projects unaccompanied by refinancing commitments). The proportion of banks doing so either "frequently enough to warrant notice" or "commonly or as standard procedure" rose to 25 percent from 24 percent.

## *Home Equity Loans*

Of FDIC-supervised banks active in home equity lending, a slightly larger proportion were making home equity loans that pushed mortgage indebtedness above 90 percent of collateral value. Specifically, 12 percent were making such loans either "frequently enough to warrant notice" or "commonly or as standard procedure" during the six months ending March 30, 2000, compared with 11 percent during the six months ending September 30, 1999.

One percent of banks qualified borrowers for home equity credit on the basis of initially discounted loan (teaser) rates either "frequently enough to warrant notice" or "commonly or as standard procedure" (down slightly from 2 percent previously).



## *Credit Card Loans*

Few FDIC-supervised banks were making new credit card loans. Only 1 percent of banks active in new credit card lending had "high" risk in current underwriting practices for new credit card loans (down from 3 percent previously). And only 1 percent had "high" risk associated with the bank's credit card portfolio (down from 3 percent previously).

## *Purpose and Design of the Report*

In early 1995, the FDIC began to require that a supplementary examination questionnaire on current underwriting practices at FDIC-supervised banks be filled out at the end of each FDIC-supervised bank examination. The questionnaire focuses on three topics: material changes in underwriting practices for new loans, the overall degree of risk in underwriting practices for new loans, and the frequency of specific risks in underwriting practices within major categories of loans (business, consumer, commercial [nonresidential] real estate, agricultural, construction, home equity, and credit card loans). Examiners are also asked to report whether the institution is active in additional loan categories (unguaranteed portions of Small Business Administration [SBA] loans, subprime loans [automobiles, mortgages], dealer paper loans, low- /no-document business loans, high loan-to-value ratio home equity loans [up to 125%], or any category of loan not mentioned). The systematic collection and analysis of questionnaire responses provides an early-warning mechanism for identifying potential lending problems.

Examiners evaluate underwriting practices in terms of FDIC supervisory practices. **Until October 1, 1998**, examiners were asked to rate the risk associated with a bank's underwriting practices in relative terms: "above average," "average," or "below average." **Beginning October 1, 1998**, examiners began rating the risk associated with a bank's underwriting practices in absolute terms: "low," "medium," or "high."[3] New questions about underwriting practices were also added to the questionnaire. Examiners continue to classify the frequency of specific risky underwriting practices as "never or infrequently," "frequently enough to warrant notice," or, if the risky practice is used more often, "commonly or as standard procedure."[4]

The questionnaire is completed at the end of each bank examination the FDIC conducts. Which banks are included during a reporting period, therefore, depends on how the FDIC schedules bank examinations. Examination schedules are heavily influenced by the financial condition of a bank, with the examinations generally becoming more frequent the poorer a bank's financial condition. In addition, the FDIC shares examination authority of state-chartered nonmember banks (those that are not members of the Federal Reserve System) with state bank regulators. To avoid excessive regulatory burden, the FDIC generally alternates examinations with state regulators, and the latter do not fill out questionnaires. Finally, examination schedules are affected by the availability of examination staff. For these reasons the group of banks included in any given report is not randomly selected and therefore may not be representative of the population of FDIC-supervised banks.

To address the potential bias that examination scheduling might introduce into the report's results, we statistically weight the responses. The weights are designed to make questionnaire responses in the aggregate more reflective of the population of FDIC-supervised banks. Simply put, when we compute aggregate questionnaire responses, we give greater weight to FDIC-supervised banks that are "underrepresented" in the questionnaire (when compared with the population of FDIC-supervised banks) and less weight to "overrepresented" groups.[5] Although these weightings cannot remove all potential bias, they do allow for more meaningful comparisons of results over time. Nevertheless, we adv1ise readers to interpret trends cautiously, for two reasons: (1) the lack of random selection of banks for examination, as noted above, and (2) the small number of responses for some loan categories.

Throughout this report, the proportions presented refer to these weighted responses and are estimates of the underwriting practices of all FDIC-supervised banks in the region. In addition, the data used to weight responses in this report are subject to slight revisions, so some of the weighted proportions might be revised in subsequent reports. We expect no substantive changes, however.

[3] **Low:** The level of risk imposed on the institution does not warrant notice by bank supervisors even when factors that might offset the risk are ignored. **Medium:** The level of risk should be brought to the attention of bank supervisors. There may or may not be factors that offset the risk imposed on the institution; however, the level of risk raises concerns when considered apart from these offsetting factors. **High:** The level of risk is high and therefore should be brought to the immediate attention of bank supervisors. There may or may not be factors that offset the risk imposed on the institution; however, the level of risk is high when viewed in isolation.

[4] **Never or infrequently:** The institution does not engage in the practice, or does so only to an extent that does not warrant notice by bank supervisors. **Frequently enough to warrant notice:** The institution engages in the practice often enough for it to be brought to the attention of bank supervisors. There may or may not be factors that offset the risks the practice imposes on the institution. **Commonly or as standard procedure:** The practice is either common or standard at the institution and therefore should be brought to the attention of bank supervisors. There may or may not be factors that offset the risks the practice imposes on the institution.

[5] Anyone who wishes more information about the weights should contact Virginia Olin, DRS, 202/898-8711.

## RESULTS FROM THE REPORT ON UNDERWRITING PRACTICES

### Percent of Respondents

| | | (Weighted) Six-Month Period Ending: 3/98 | 9/98 | 3/99 | 9/99 | 3/00 |
|---|---|---|---|---|---|---|
| **GENERAL UNDERWRITING PRACTICES** | | | | | | |
| **Have the institution's underwriting practices materially changed since the last examination:** | Yes | 10.7% | 11.7% | 9.3% | 10.6% | 9.7% |
| | No | 89.3 | 88.3 | 90.7 | 89.4 | 90.3 |
| **If practices have materially changed, are they:**[1] | Substantially tighter | NA | NA | 0.9 | 1.1 | 1.1 |
| | Moderately tighter | 4.4 | 5.4 | 4.3 | 4.1 | 3.1 |
| | Moderately looser | 6.4 | 6.3 | 3.1 | 4.3 | 4.4 |
| | Substantially looser | NA | NA | 1.0 | 1.1 | 1.1 |
| **How would you characterize the risk associated with loan growth and/or significant changes in lending activities since the last examination:** | Low | NA | NA | 55.1 | 54.3 | 55.4 |
| | Medium | NA | NA | 28.8 | 28.9 | 28.6 |
| | High | NA | NA | 3.9 | 4.1 | 2.3 |
| | Insignificant | NA | NA | 12.2 | 12.7 | 13.8 |
| **RISK IN CURRENT PRACTICES** | | | | | | |
| **How would you characterize the potential risk associated with the institution's current UW practices:** | Low | NA | NA | 65.0 | 66.4 | 67.7 |
| | Medium | NA | NA | 31.8 | 29.9 | 29.7 |
| | High | NA | NA | 3.3 | 3.7 | 2.7 |
| **How would you characterize the potential credit risk of the institution's overall loan portfolio:** | Low | NA | NA | 66.5 | 66.7 | 68.3 |
| | Medium | NA | NA | 30.4 | 29.0 | 29.0 |
| | High | NA | NA | 3.1 | 4.3 | 2.7 |
| **How would you characterize the potential risk in underwriting practices associated with loan participations purchased by the institution:** | Low | NA | NA | 79.7 | 77.4 | 78.5 |
| | Medium | NA | NA | 19.4 | 21.0 | 20.2 |
| | High | NA | NA | 0.8 | 1.6 | 1.3 |
| **To what extent has recent lending been made in amounts that resulted in—or contributed to—concentrations of credit to one borrower or industry:** | Never or infrequently | 79.1 | 77.7 | 80.0 | 78.6 | 79.5 |
| | Frequently enough to warrant notice | 13.9 | 14.5 | 12.9 | 13.9 | 14.1 |
| | Commonly or standard procedure | 7.0 | 7.8 | 7.1 | 7.5 | 6.4 |
| **To what extent is the institution currently engaged in out-of-area financing:** | Never or infrequently | NA | NA | 89.2 | 87.1 | 88.2 |
| | Frequently enough to warrant notice | NA | NA | 8.3 | 9.8 | 9.5 |
| | Commonly or standard procedure | NA | NA | 2.5 | 3.1 | 2.4 |
| **How would you characterize the risk associated with loan administration:** | Low | NA | NA | 64.5 | 63.1 | 65.5 |
| | Medium | NA | NA | 30.8 | 31.6 | 31.1 |
| | High | NA | NA | 4.7 | 5.3 | 3.4 |
| **To what degree does the institution fail to adjust its loan pricing on different quality loans to reflect differences in risk:** | Never or infrequently | 72.1 | 73.0 | 89.4 | 86.2 | 87.7 |
| | Frequently enough to warrant notice | 23.4 | 22.3 | 8.0 | 11.4 | 10.5 |
| | Commonly or standard procedure | 4.6 | 4.7 | 2.6 | 2.5 | 1.8 |
| **To what extent does the institution fail to require a material principal reduction before renewing term loans:** | Never or infrequently | 63.1 | 62.5 | 76.2 | 75.7 | 76.8 |
| | Frequently enough to warrant notice | 31.3 | 32.7 | 20.2 | 20.9 | 20.8 |
| | Commonly or standard procedure | 5.6 | 4.8 | 3.6 | 3.4 | 2.5 |
| **To what extent do the institution's written lending policies differ from actual practices:** | Never or infrequently | 72.5 | 71.5 | 79.8 | 77.5 | 78.2 |
| | Frequently enough to warrant notice | 23.1 | 22.7 | 17.1 | 19.4 | 19.0 |
| | Commonly or standard procedure | 4.4 | 5.8 | 3.1 | 3.1 | 2.9 |
| **BUSINESS LOANS** | | | | | | |
| **To what extent does the institution make business loans without a clear and reasonably predictable repayment source:** | Never or infrequently | 82.6 | 85.2 | 82.9 | 84.1 | 85.1 |
| | Frequently enough to warrant notice | 15.6 | 12.6 | 13.8 | 13.8 | 13.5 |
| | Commonly or standard procedure | 1.8 | 2.3 | 3.3 | 2.0 | 1.4 |
| **To what extent does the institution make business loans to borrowers who lack documented financial strength to support such lending:** | Never or infrequently | 76.7 | 78.6 | 81.0 | 80.4 | 79.9 |
| | Frequently enough to warrant notice | 20.6 | 18.9 | 16.6 | 17.8 | 18.5 |
| | Commonly or standard procedure | 2.7 | 2.5 | 2.3 | 1.8 | 1.6 |
| **With respect to asset-based business loans, to what extent does the institution fail to monitor collateral:** | Never or infrequently | 79.0 | 83.6 | 77.7 | 78.6 | 80.6 |
| | Frequently enough to warrant notice | 18.0 | 14.4 | 19.5 | 19.0 | 17.3 |
| | Commonly or standard procedure | 3.0 | 2.0 | 2.7 | 2.4 | 2.2 |
| **CONSTRUCTION LOANS** | | | | | | |
| **To what extent is the institution funding construction projects on a speculative basis (i.e., without meaningful pre-sale, pre-lease or take-out commitments):** | Never or infrequently | 62.2 | 63.2 | 75.2 | 76.1 | 75.3 |
| | Frequently enough to warrant notice | 30.6 | 29.7 | 19.4 | 20.1 | 20.4 |
| | Commonly or standard procedure | 7.2 | 7.2 | 5.4 | 3.9 | 4.4 |
| **To what extent are construction loans made without consideration of repayment sources other than the project being funded:** | Never or infrequently | 76.4 | 74.3 | 87.3 | 88.1 | 88.1 |
| | Frequently enough to warrant notice | 18.7 | 22.6 | 11.6 | 10.5 | 10.5 |
| | Commonly or standard procedure | 5.0 | 3.1 | 1.1 | 1.5 | 1.4 |
| **When alternative repayment sources are required, to what extent does the institution fail to take appropriate steps to verify the quality of these sources:** | Never or infrequently | 79.1 | 83.6 | 88.0 | 87.9 | 87.7 |
| | Frequently enough to warrant notice | 16.7 | 14.1 | 11.3 | 9.5 | 11.1 |
| | Commonly or standard procedure | 4.1 | 2.2 | 0.8 | 2.5 | 1.1 |
| **To what extent does the institution fail to use realistic appraisal values relative to the current economic environment and/or to the performance observed on similar credits:** | Never or infrequently | 86.0 | 86.0 | 89.8 | 87.9 | 89.5 |
| | Frequently enough to warrant notice | 12.2 | 11.8 | 9.9 | 11.2 | 9.6 |
| | Commonly or standard procedure | 1.8 | 2.2 | 0.3 | 0.9 | 0.9 |
| **To what extent does the institution fund, or defer, interest payments during the term of its commercial construction loans:** | Never or infrequently | 80.3 | 79.8 | 83.9 | 87.1 | 86.0 |
| | Frequently enough to warrant notice | 13.9 | 14.4 | 10.0 | 9.7 | 7.9 |
| | Commonly or standard procedure | 5.8 | 5.9 | 5.9 | 3.2 | 6.1 |

[1] Prior to October 1, 1998, responses were either "tighter" or "looser."

## RESULTS FROM THE REPORT ON UNDERWRITING PRACTICES

**Percent of Respondents**

| | | Weighted Six-Month Period Ending: | | | | |
|---|---|---|---|---|---|---|
| | | 3/98 | 9/98 | 3/99 | 9/99 | 3/00 |
| **CONSTRUCTION LOANS *(cont.)*** | | | | | | |
| **To what extent does the institution fund 100% of the cost of construction and land, with no cash equity on the part of the borrower/developer:** | Never or infrequently | NA | NA | 88.4% | 88.8% | 88.8% |
| | Frequently enough to warrant notice | NA | NA | 9.7 | 10.8 | 9.7 |
| | Commonly or standard procedure | NA | NA | 1.9 | 0.4 | 1.6 |
| **NONRESIDENTIAL LOANS** | | | | | | |
| **To what extent are commercial real estate loans made without consideration of repayment sources other than the project being funded:** | Never or infrequently | 86.1 | 85.1 | 88.9 | 87.7 | 88.7 |
| | Frequently enough to warrant notice | 12.5 | 12.3 | 8.9 | 10.5 | 10.2 |
| | Commonly or standard procedure | 1.4 | 2.6 | 2.2 | 1.8 | 1.1 |
| **To what extent does the institution make interest-only, extended amortization, or negative amortization permanent commercial real estate loans:** | Never or infrequently | 93.0 | 92.8 | 93.4 | 93.4 | 92.7 |
| | Frequently enough to warrant notice | 6.3 | 7.2 | 6.5 | 5.9 | 6.9 |
| | Commonly or standard procedure | 0.7 | 0.0 | 0.1 | 0.7 | 0.5 |
| **To what extent does the institution make short-term commercial real estate loans ("Mini-perms") with minimal amortization terms and large "balloon" payments at maturity:** | Never or infrequently | 80.6 | 84.7 | 83.9 | 81.8 | 83.1 |
| | Frequently enough to warrant notice | 15.0 | 12.7 | 12.9 | 15.3 | 13.8 |
| | Commonly or standard procedure | 4.4 | 2.7 | 3.2 | 2.9 | 3.1 |
| **To what extent does the institution fail to use realistic appraisal values relative to the current economic environment and/or to the performance observed on similar credits:** | Never or infrequently | 90.0 | 89.6 | 92.1 | 90.1 | 91.4 |
| | Frequently enough to warrant notice | 9.2 | 9.9 | 7.7 | 9.5 | 8.2 |
| | Commonly or standard procedure | 0.8 | 0.6 | 0.1 | 0.4 | 0.4 |
| **HOME EQUITY LOANS** | | | | | | |
| **To what extent does the institution make home equity loans that push mortgage indebtedness above 90 percent of collateral value:** | Never or infrequently | 88.1 | 86.8 | 91.0 | 89.3 | 88.3 |
| | Frequently enough to warrant notice | 9.9 | 11.5 | 5.5 | 9.3 | 9.2 |
| | Commonly or standard procedure | 2.0 | 1.7 | 3.5 | 1.4 | 2.5 |
| **To what extent does the institution qualify borrowers for home equity credit based on initially-discounted loan rates:** | Never or infrequently | 99.0 | 98.3 | 98.0 | 98.1 | 99.0 |
| | Frequently enough to warrant notice | 1.0 | 1.7 | 1.8 | 1.3 | 0.4 |
| | Commonly or standard procedure | 0.0 | 0.0 | 0.2 | 0.5 | 0.6 |
| **AGRICULTURAL LOANS** | | | | | | |
| **To what extent does the institution make agricultural loans on the basis of land values that cannot be supported by farm operations:** | Never or infrequently | NA | NA | 87.8 | 86.0 | 85.8 |
| | Frequently enough to warrant notice | NA | NA | 10.6 | 11.9 | 13.1 |
| | Commonly or standard procedure | NA | NA | 1.7 | 2.1 | 1.2 |
| **To what extent is the institution's agricultural loan portfolio tied to major crops affected by the phase out of farm subsidies:** | Never or infrequently | 59.2 | 51.2 | 58.6 | 55.0 | 54.5 |
| | Frequently enough to warrant notice | 27.1 | 27.7 | 23.0 | 22.8 | 24.8 |
| | Commonly or standard procedure | 13.7 | 21.1 | 18.4 | 22.2 | 20.7 |
| **To what extent are agricultural loans being made based on unrealistic cash flow projections:** | Never or infrequently | 88.1 | 84.3 | 85.7 | 84.5 | 86.3 |
| | Frequently enough to warrant notice | 9.4 | 12.6 | 13.0 | 14.3 | 12.2 |
| | Commonly or standard procedure | 2.5 | 3.1 | 1.3 | 1.2 | 1.5 |
| **How would you characterize the change in the level of the institution's agricultural related carryover debt since the last examination:** | Sharp decline | 2.4 | 0.8 | 1.6 | 2.0 | 3.1 |
| | Moderate decline | 25.5 | 17.6 | 9.6 | 7.0 | 11.3 |
| | No change | 60.5 | 55.8 | 56.4 | 48.7 | 52.7 |
| | Moderate increase | 10.4 | 23.5 | 29.0 | 37.2 | 31.0 |
| | Sharp increase | 1.2 | 2.4 | 3.4 | 5.1 | 2.0 |
| **CONSUMER LOANS** | | | | | | |
| **To what extent does the institution make "secured" consumer loans without adequate collateral protection:** | Never or infrequently | 83.0 | 82.6 | 86.5 | 85.0 | 85.7 |
| | Frequently enough to warrant notice | 14.2 | 13.5 | 10.9 | 13.1 | 12.1 |
| | Commonly or standard procedure | 2.8 | 3.9 | 2.6 | 1.9 | 2.2 |
| **To what extent does the institution make consumer loans to borrowers who lack demonstrable ability to repay:** | Never or infrequently | 78.9 | 79.5 | 83.7 | 83.3 | 83.1 |
| | Frequently enough to warrant notice | 18.0 | 16.0 | 13.9 | 14.7 | 14.4 |
| | Commonly or standard procedure | 3.1 | 4.5 | 2.5 | 2.0 | 2.5 |
| **CREDIT CARD LOANS** | | | | | | |
| **Have the institution's underwriting practices for new credit card loans materially changed since the last examination:** | Yes | 15.7 | 10.9 | 9.2 | 6.4 | 2.1 |
| | No | 84.3 | 89.1 | 90.9 | 93.6 | 97.9 |
| **Are underwriting practices for new credit cards:[1]** | Substantially tighter | NA | NA | 1.3 | 0.8 | 0.7 |
| | Moderately tighter | 13.7 | 9.4 | 7.2 | 3.3 | 0.5 |
| | Moderately looser | 2.0 | 1.5 | 0.0 | 1.5 | 0.9 |
| | Substantially looser | NA | NA | 0.7 | 0.9 | 0.0 |
| **How would you characterize the level of risk associated with the institution's current underwriting practices for new credit card loans:** | Low | NA | NA | 74.4 | 72.6 | 80.2 |
| | Medium | NA | NA | 24.7 | 24.2 | 18.5 |
| | High | NA | NA | 0.9 | 3.2 | 1.4 |
| **How would you characterize the level of risk associated with the institution's credit card portfolio:** | Low | NA | NA | 76.5 | 74.4 | 79.6 |
| | Medium | NA | NA | 23.5 | 22.5 | 19.6 |
| | High | NA | NA | 0.0 | 3.1 | 0.9 |
| **For credit card loans in the institution's portfolio with risk characterized as high, to what degree does the institution fail to adjust its loan pricing to account for this risk:** | Never or infrequently | NA | NA | 0.0 | 84.3 | 100.0 |
| | Frequently enough to warrant notice | NA | NA | 0.0 | 15.6 | 0.0 |
| | Commonly or standard procedure | NA | NA | 0.0 | 0.0 | 0.0 |

[1] Prior to October 1, 1998, responses were either "tighter" or "looser."

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## Characteristics of Banks Examined in the *Report on Underwriting Practices*

- Coverage: 1,158 FDIC-supervised banks.
- Period: Reports filed between October 1, 1999, and March 31, 2000.
- Charter types: 100 percent of the examined banks during this period were state-chartered commercial banks.
- Size distribution of banks: assets of $1 billion or greater, 4 percent; assets between $300 million and $1 billion, 8 percent; assets between $25 million and $300 million, 74 percent; assets less than $25 million, 14 percent.

## The Report on Underwriting Practices Seeks

- To identify (1) material changes in underwriting practices, (2) overall risk in new lending practices, and (3) specific risks in underwriting practices for major loan categories.
- To track emerging issues in underwriting practices of new loans.
- To provide an early-warning mechanism for identifying potential problems.