

## Handbook and Program Use

The Examination Handbook is a new Handbook that integrates safety and soundness (S&S) and compliance guidance. This Handbook replaces the Thrift Activities and Compliance Activities Handbooks. We retained the general layout of the handbooks with a chapter for each CAMELS component and a chapter for Compliance and the Community Reinvestment Act (CRA).

The Examination Handbook is a guide for the examination of savings associations regulated by the Office of Thrift Supervision (OTS). Specifically, the Handbook aids OTS regulatory staff and the savings and loan industry in the regulatory process. The Handbook provides uniform standards for planning and conducting examinations and addressing supervisory issues. It also serves as a reference tool, training aid, and guide to national policies and procedures.

The Handbook illustrates and describes, for examiners and the thrift industry, certain standards of conduct and prudent operation that OTS views as important to the safe and sound operation of savings associations. These standards should be consistent with the respective fiduciary duties of those individuals associated with them.

This Handbook Section explains how to use the Handbook and the programs in the examination process. It describes the organization of the Handbook chapters and sections, and sets forth objectives and procedures common to all phases of the examination.

### REGULATORY PROCESS

The regulatory process allows you to meet the following objectives:

- Assess an association's degree of safety and soundness.
- Assess the adequacy of the association's compliance management program.
- Assess how well an association manages compliance with consumer protection and public interest-related laws and regulations (Compliance).
- Evaluate an association's condition.
- Identify the association's strengths.
- Identify existing regulatory violations.

- Identify potential problems.
- Prevent the development or continuation of unsafe operating practices.
- Report findings.
- Inform directors of association strengths and weaknesses.
- Facilitate corrective action where needed.

Proactive regulatory supervision should evaluate future needs and potential risks to ensure the success of the thrift system in the long term. This Handbook provides a framework for the successful completion of that process.

The Handbook encourages independent reasoning, objectivity, efficiency, and professionalism in the examination process.

The Handbook encourages independent reasoning, objectivity, efficiency, and professionalism in the examination process. To promote consistency among the OTS regional offices, the Handbook sets forth national minimum standards for examination objectives and procedures. While this process promotes standardization of the examination process, we encourage you to modify programs to fit the association's specific needs.

We are designing the Examination Handbook to cover S&S, compliance, and CRA for both new and experienced examiners. Background information, applicable references, and expanded procedures within the text serve to help in the learning process.

You should supplement your use of the Handbook and associated programs with your education, experience, and judgment. We will periodically update the Handbook and issue individual sections as necessary. Separate manuals are available for Compliance Self-Assessment, Holding Companies, Trust and Asset Management Activities, Information Technology (IT), and Applications Processing. These Handbooks are available via the OTS website.

## HANDBOOK ORGANIZATION

The Examination Handbook will contain a table of contents, one chapter for each CAMELS element, a chapter on other activities, and a chapter for Compliance and CRA. A brief discussion of the Handbook's organization appears below.

### Table of Contents

The table of contents lists each Handbook chapter, section number and title, and, if applicable, programs, questionnaires, and appendices.

## 000 Administration

This chapter gives a general overview of the administration and coordination of the regulatory process. It includes instructions on determining the scope of an examination, monitoring the regulatory profile process, assigning component and composite CAMELS ratings, and Compliance and CRA ratings, and devising an examination strategy.

## 100 Capital Adequacy

This chapter provides useful information for assessing whether an association's capital position is sufficient, given the risk level, to ensure ongoing viability. Discussions of minimum regulatory capital requirements, prompt corrective action (PCA) categories, and stock ownership and control help you determine the adequacy and composition of an association's capital.

## 200 Asset Quality

This chapter addresses the following two issues:

- The determination of risks related to the association's assets.
- The association's management, administration, and evaluation of the quality of these assets.

It also provides guidance in assessing credit risk and reviewing asset portfolios (including loans, investments, and other assets). This chapter focuses on three areas:

- The quality of loan underwriting and portfolio management.
- Affirmation of classified asset levels.
- Adequacy of valuation allowances.

There are also sections discussing real estate appraisals, loan sampling, the Qualified Thrift Lender Test, and margin securities.

## 300 Management

This chapter provides guidance in evaluating the capability of executive management and the board of directors. It covers objectives, procedures, and references for examining compliance management, internal controls, internal and independent audits, fraud and insider abuse, and transactions with affiliates and insiders.

### 400 Earnings

This chapter will assist in analyzing an association's financial condition. It covers objectives, procedures, and references for examining the association's financial record keeping and reporting methods and operations analysis. The chapter also discusses present value analysis.

### 500 Liquidity

This chapter provides assistance in assessing liquidity and the funding risk confronting an association. It includes material on funds management, liquidity management, and investment activities. The chapter also discusses the Government Securities Act, Payments Systems Risk, and Regulation D.

### 600 Sensitivity to Market Risk

This chapter provides assistance in assessing the market risk confronting an association. It includes guidance on managing interest rate risk and hedging.

### 700 Other Activities

This chapter addresses review of the thrift's or subordinate organization's activities in insurance, real estate development, and networking arrangements.

This chapter also provides guidance in the evaluation of risk that operating subsidiaries, service corporations, and lower-tier entities (such as joint ventures or limited partnerships) pose to the association and thereby the insurance fund.

### 1000 Compliance

The Compliance chapter covers the new Compliance Oversight Examination Program (COEP); fair lending laws and regulations such as the Equal Credit Opportunity Act and the Fair Housing Act; the consumer protection laws and regulations such as the Truth in Lending Act, Real Estate Settlement Procedures Act, and the Electronic Funds Transfer Act; the laws and regulations such as the Bank Secrecy Act, the Bank Protection Act, and the Community Reinvestment Act and regulations.

#### *FFIEC-Approved Procedures*

In many instances, you will notice that the Federal Financial Institution Examination Council (FFIEC) logo and approval appears at the bottom of the first page of a Compliance section addressing a law or regulation. This indicates that the entire section, including the examination objectives and procedures, has been approved for use by all the agencies represented on the FFIEC (the Federal Reserve Board, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, OTS, and the National Credit Union Administration).

## SECTION ORGANIZATION

Each handbook chapter contains several sections of examination material subdivided into different areas of review. For example, Chapter 300 contains a section for each area of review under Management.

Each handbook section has a unique three- or four-digit number that allows for easy identification and referencing of materials. For example, under Management Chapter 300, the number 310 references the section on Oversight by the Board. The program, questionnaire, and any work papers have the same 310 reference number. Handbook page numbers follow the same sequence; hence, the introduction for Oversight by the Board of Directors, Section 310, is handbook page number 310.1.

Each handbook section has a unique three- or four-digit number that allows for easy identification and referencing of materials.

Each handbook section contains a discussion of the subject area, regulatory references, a program that includes examination objectives and procedures, related questionnaires, and appendices, if applicable. The discussion below covers each of these areas. We also provide a list of common objectives and procedures that may prove valuable during the examination, even though they may not appear in every program.

## Subject Narrative

The narrative of each handbook section provides the specific guidance for a particular topic. It provides basic information such as OTS policy, a historical perspective, and subject overview. The narrative highlights significant regulatory concerns such as the nature and intent of enforcement actions that may be applicable to the review area. Subheadings appear where appropriate.

## References

Pertinent legislative and regulatory citations appear in the reference section, following the narrative. References to other relevant OTS guidance may appear where appropriate, including: various bulletins, agency instruction and class manuals, industry sources, and accounting pronouncements.

The reference list is comprehensive, providing resources beyond those needed on a day-to-day basis. When examining a state-chartered thrift, you should also refer to state regulations per regional office policy.

## Programs

The examination program serves as a guide for the orderly completion of an examination. Programs include objectives for the review of a subject and a series of procedures for completing those objectives. Examination programs also help determine the examination scope and organization, serve as documentation, and help establish conclusions and recommendations. Once completed, the program becomes part of the foundation for an effective quality review process.

We provide a detailed discussion of programs later in this Section.

## Questionnaires

Questionnaires appear at the end of some handbook sections. They are also available on the OTS Intranet.

### *General Questionnaires*

General questionnaires reflect standards for safe and sound operating procedures and may be useful for evaluating an association's operations. They include questions on internal controls that you must answer for purposes of objectivity. These questionnaires also assist in organization, act as memory joggers, and facilitate the review process.

It is not necessary to complete all questionnaires. You should complete only those pertaining to the examination scope and objectives.

### *Internal Control Questionnaire and Funds Transfer Questionnaire*

These questionnaires appear in the Preliminary Examination Response Kit (PERK) and copies are included as appendices in Examination Handbook Section 340, Internal Control. The Internal Control Questionnaire contains questions about the association's internal control system. The Funds Transfer Questionnaire contains questions regarding the association's internal controls for funds transfers. The association should complete these questionnaires before the examination and it is your responsibility to verify the answers once you are onsite.

## Appendices

Some handbook sections include appendices. Appendices present additional sources of information applicable to the particular handbook section and may include forms, guidelines, or Q's and A's.

## EXAMINATION PROGRAMS

As mentioned earlier in this Section, examination programs serve as guides for the orderly completion of an examination via a set of objectives and procedures.

### Examination Objectives

This segment of the program helps you identify goals in reviewing a subject area. Each corresponding program, if applicable, lists objectives for easy reference.

Certain objectives are germane to the overall examination process and to virtually every examination section. You may wish to review these common objectives during an examination, as they may not appear in other handbook sections.

*Common Objectives*

- Document the effectiveness of an association's operations.
- Determine compliance with laws and regulations.
- Determine the adequacy of and adherence to association policies and procedures.
- Assess management's expertise and ability to manage the association's affairs.
- Assess the oversight and ensure that management and the board are receiving complete and accurate reports.
- Verify that an acceptable system of records and internal controls is in place.
- Assess the effect of anticipated internal and external changes on the association.
- Assess the association's ability to meet its future needs (for instance, fund growth, provide capital, absorb losses).
- Identify any actual or potential undue risk to the association.
- Report examination findings, presenting analysis and conclusions regarding the association's overall condition, trends, and prospects for future viability.
- Report concerns of material risk and initiate corrective action when needed.

**Examination Procedures**

Examination procedures appear in a top-down fashion in three categories – Levels I, II, and III. Each category represents a different level or depth of review. The top-down approach begins with a review of policies, procedures, and internal controls while focusing on the safety and soundness of the association (Level I). With this approach, you can expeditiously assess the degree of risk in each area of a particular association's operations early in the examination. You can also better determine the depth of review and the procedures (Levels II and III) needed.

The programs serve as guides and reminders throughout the examination process. For those with less experience, the programs are especially useful guides for effectively completing the assigned examination phase. For those with more experience, the programs tend to be reminders of review areas during each phase of an examination.

Not all programs will apply to an association. Further, of those that apply, you most likely will not need to complete all the procedures. The examination scope should help determine the level of review and procedures you need to conduct in each area. See [Examination Handbook Section 060, Examination Scheduling, Scoping, and Management](#). When selecting programs and procedures for review, you must

use a risk-focused examination approach. A risk-focused approach allows you to accomplish the following tasks:

When selecting programs and procedures  
for review, you must use a  
risk-focused examination approach.

- Highlight the concerns in the scope and any other problems found during the review.
- Assess the safety and soundness of the association.
- Update and support the CAMELS composite and component ratings.
- Assess the association's compliance management program.
- Update and support the Compliance rating.

Use sound professional judgment to ensure that the depth of review is sufficient to accurately assess the association's condition, but is not excessive. The following discussion focuses on general procedures, the three levels of procedures, and the national policy guidelines for their use.

### *General Procedures*

Although examination subject areas differ greatly, certain procedures are applicable to any phase of an examination. A list of procedures that is common to the overall examination process and to virtually every examination section appears below. You may wish to review this list when completing an area of review, as the procedures may not appear in other handbook sections or programs.

Gather data:

- Review previous Report of Examination (ROE), PERK documents, exceptions, and work papers.
- Review internal and external audit reports and related management letters.
- Review current year's scope, supervisory correspondence, and interagency data.
- Consider regulatory policy associated with area of review.
- Set forth special considerations pertinent to the areas of examination.
- Obtain association's management reports and written policies and procedures.



Set scope (see also [Examination Handbook Section 060](#)):

- Establish a clear understanding of examination objectives.
- Determine whether management corrected any deficiencies mentioned in the previous ROE, audit reports, and supervisory correspondence.
- Perform analytical review procedures on financial data:
  - Identify new or unusual transactions requiring modified examination procedures.
  - Indicate areas of greatest concern.
- Consider risk-focused or tailored examination procedures.
- Tailor examination program to meet individual needs.
- Consult with other examiners; take the nature of their initial findings into account in determining the procedures to perform.
- Determine if expanded procedures are necessary.
- Develop additional procedures not covered in the Handbook, if necessary.
- Perform only those procedures necessary to achieve program objectives.

Perform procedures:

- Interview association personnel.
- Evaluate policies and procedures.
- Spot check the reliability and accuracy of reports.
- Test the association's procedures.
- Identify any material changes in operation or policy since previous examination.
- Evaluate trends.
- Research significant variations from the previous examination to determine if there is cause for concern.
- Obtain explanations for any significant matters.

Assess management:

- Review adequacy of management reports to the board.
- Determine the extent of directors' involvement in monitoring performance.
- Review management's plan for future operations.
- Interview management and staff to determine if they have adequate knowledge of policies and procedures.
- Determine sufficiency of training and expertise to implement procedures.
- Determine if management is communicating and regularly updating policies and procedures.

Formulate conclusion:

- Keep the examiner-in-charge (EIC) informed of progress.
- Discuss concerns with other examiners.
- Identify, and determine significance of, regulatory violations and deficiencies.
- Discuss findings with management.
- Determine adequacy of management's response to problem issues.
- Consider possible strategies for corrective action and develop a recommended course of action.

Conduct post review activities:

- Review work to ensure the examination team satisfied examination objectives.
- Summarize results and conclusions.
- Draft comments, including scope and recommendations.
- Assign ratings, if applicable.
- Ensure that you properly cross reference work papers and support substantive findings and conclusions.
- Update the Electronic Continuing Examination Folder (ECEF) and Regulatory Profile, if applicable. (See [Examination Handbook Section 040](#).)

- Update the Continuing Examination File (CEF), if applicable. (See Examination Handbook Section 060.)
- Enter violations of laws and regulations under the Violations tab in the EDS/ROE system.
- File exceptions in the General File (GF).

### *Level I*

Level I procedures focus on the review of examination scoping materials and association documents, such as policies, procedures, and the compliance management program and self-assessment. After the Level I review, interview personnel to determine if practices conform to written guidelines. You should also confirm any other preliminary findings.

If you uncover significant items of concern during Level I analysis, or if you identify significant problems during preexamination monitoring and scoping, you may need to use

Level II procedures. In certain circumstances, you may need to complete Level III procedures as well.

#### Examination Focus

- Level I – Review of exam scoping materials and association documents
- Level II – Analysis of association documents
- Level III – Transaction or file analysis

### *Level II*

Level II procedures focus on the analysis of association documents such as loan files, management reports, and supporting financial records. You should select and complete Level II procedures when Level I procedures do not reveal adequate data to support a conclusion for a review area. In the Compliance area, you must determine if the association's compliance management program adequately fulfils the remaining SMAART criteria, that is systems, monitoring, accountability, responses, and training. You may develop an independent analysis of asset values at this level as well as independent verification of other items.

Level I and selected Level II procedures normally provide a comprehensive analysis to support conclusions. These procedures do not include any significant auditing procedures. If you cannot rely on the data contained in association records, Level III procedures may be necessary.

### *Level III*

Level III procedures include extensive transaction or file analysis. In the Compliance area, this includes completion of selected FFIEC and/or OTS examination procedures.

Level III also includes steps that auditors usually perform. Although certain situations may require Level III procedures, it is not standard practice for you to duplicate the testing efforts of auditors.

Again, it may not be necessary to complete every program or every procedure within a program. You must use discretion in determining which programs and procedures are necessary to address the scope and reach a sound conclusion. In some situations it may be appropriate to customize existing procedures. In other situations you may perform procedures outside a program to achieve the most efficient and meaningful analysis. You should document any decisions to deviate significantly from the initial scope instructions or to modify existing procedures on the relevant programs.

### *Summary, Recommendations, and Comments*

In this last section of the program, summarize the following:

- Examination scope, including identification of any procedures used that are not already printed on the program.
- Salient findings and a conclusion regarding the strengths and weaknesses of the association's operations in the particular review area.
- Recommendations for corrective action, which may include a statement about the adequacy of management's response and commitments. *Note:* You should address any recommendation for revising a formal supervisory action in a separate memorandum.

Your work papers should support all substantive findings regarding the overall condition of the association. It may be useful to attach copies of draft comments or schedules included in the ROE to this portion of the program.

### Programs and Work Papers

Properly prepared examination programs and work papers are essential to the examination process. OTS relies on work papers to support the conclusions and findings set forth in the ROE. The reader determines conclusions about the effectiveness of the OTS examination process, in part, by the adequacy of work paper documentation. Proper documentation of procedures and subsequent conclusions in the programs leaves an effective audit trail for users of the completed programs. Moreover, legal staff often uses examination work papers to support the OTS's position in litigation matters.

You are required to support all the applicable elements reviewed under each CAMELS component and Compliance 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.

You should avoid excessive documentation and include only information that is relevant or may require follow-up.

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 you obtained the information. Schedules prepared by the association should be clearly marked as such.

You should include the following items in work papers and programs, as appropriate:

- Statement of purpose, title, or heading.
- Scope of review.
- Sampling criteria used.
- Procedures performed.
- Legend or explanatory footnotes, if necessary.
- Results of testing.

The examination programs allow space to the right of each procedure to record a work paper cross-reference. This will lead the reader to supporting documentation found either under the same topic or in another program. You must support all substantive conclusions. Additional space between each procedure allows you to include any pertinent information.

The lower right-hand corner of each program contains an index block for the following items: Examination Date, Prepared By, Reviewed By, and Docket Number. Fill in each of these items before completing the examination. You should also include this information in your work papers.

The EIC or designee must review and initial all work papers, indicating agreement with the conclusions reached and ensuring that assistants complied with the applicable documentation requirements. You need only initial and date the first page of the TFR, UTPR, and other multi-page printed documents. The EIC should ensure that exam staff carefully checks all comments, charts, and appendices. At a minimum, the EIC's supervisor will review the work papers the EIC prepared and the supporting documentation for the report comments.

File work papers according to the OTS program number. To locate examination programs easily, you may use the Handbook table of contents or the program index. You may use the program index as a cover page for file folders. You should cross-reference information germane to the ROE or review process to supporting documentation.

### *Electronic Work Papers*

OTS recently introduced the electronic work paper database accessible via the EDS/ROE system. Follow your regional office instructions.

## Sources of Information

Following is a generic list of information sources that will help you successfully complete the programs.

### *OTS Documents*

- Laws and regulations.
- Transmittals.
- Regulatory and Thrift Bulletins.
- CEO Memos.
- Standard and supplemental accounting manuals.
- Published memos.
- OTS Professional Development materials.
- Uniform Thrift Performance Report (UTPR).

### *Regional Office Examination Materials*

- Previous ROEs, General File, and work papers.
- Correspondence from the regional office.
- ECEF and Regulatory Profile.
- CEF, if applicable.
- Thrift Financial Reports (TFRs).
- Regional office instructional manuals.

### *Association's Documentation*

- Completed PERK schedules.
- Business plan.
- Operating budget and forecasts.

- General ledger trial balance.
- Loan trial balance.
- Investment trial balance.

## *Reports and Minutes*

- Independent audit report.
- Internal audit report.
- Internal management and board reports.
- Securities and Exchange Commission (SEC) annual report, 10K, 10Q, and 8K (if stock association).
- Board of directors' minutes.
- Board committee minutes.
- Operating committee minutes.

## *New or Revised Policies, Procedures, and Corporate Documents*

- Compliance management program.
- Compliance self-assessment.
- Internal control policy.
- Real estate lending policies.
- Real estate appraisal policy.
- Environmental risk policy.
- Classification of assets policy.
- Investment policies.
- Interest rate risk policy.
- Asset/liability management policy.

- Interbank liabilities policy.
- Futures and options policy.
- Charter, bylaws.
- Security policy.
- Information security program (Gramm-Leach-Bliley Act § 501(b)).
- Bank Secrecy Act/ Anti-Money Laundering policy.
- CRA statement.
- Contracts (information systems, service bureau, employment, etc.).
- Contingency planning policy.
- Leases (office building, etc.).
- Payment systems risk policy.



## Conduct of Agency Personnel

This Handbook Section summarizes and discusses some of the more important rules and policies of professional conduct that apply to OTS personnel, including examiners, while performing on-site examinations. For purposes of this Handbook Section, we define “you” as OTS personnel.

All OTS employees must comply with the OTS Employee Standards of Conduct Resource Guide (Resource Guide) that contains the following federal regulations:

- Standards of Ethical Conduct for Employees of the Executive Branch (5 CFR Part 2635, §§ 2635.101-902).
- Employee Responsibilities and Conduct (5 CFR Part 735, §§ 735.101-203; p. 79).
- Department of the Treasury Employee Rules of Conduct (31 CFR Part 0, §§ 0.101-217; Appendix 2).
- Supplemental Standards of Ethical Conduct for Employees of the Department of the Treasury (5 CFR Part 3101, §§ 3101.101-104, 109; Appendix 3).

Additionally, financial restrictions and required disclosures apply to “covered” OTS employees, defined by 5 CFR § 3101.109(a) as examiners, employees in grades 17 and above, and any other OTS employee designated by the Director.

Each employee receives the Resource Guide. If you have any questions about the regulations, contact your regional ethics counselor or the OTS Ethics Counselor at (202) 906-7039.

### Summary of Major Restrictions and Responsibilities of OTS Employees

This summary of the important OTS restrictions and responsibilities comes from the above federal regulations and OTS policies. It is not all-inclusive. As an OTS employee you need to be aware of your responsibilities, restrictions, and disclosure requirements under these rules. If you need or desire further information, you may contact your regional ethics counselor or the OTS Ethics Counselor.

#### *All OTS Employees*

All OTS employees must comply with the following restrictions:

- You may not have any financial interest or obligation that conflicts or appears to conflict with your official responsibilities and duties.

- You may not, in an official capacity, participate personally and substantially in any particular matter in which you have a financial interest if the matter will have a direct and predictable effect on that financial interest. (However, the Chief Counsel, Regional Director, or designee may, when appropriate, waive this restriction.) You may not participate by decision, approval, disapproval, recommendation, advice, examination, or other action. This restriction also applies where any household member, general partner, or organization in which you have a substantial personal involvement has a known financial interest in the matter.
- You may not accept from a prohibited source (defined below) food, refreshments, or entertainment unless it is of a nominal value. You may only accept a nominal value item infrequently, such as during an official conference or other function that you may properly attend.
- You may not accept unsolicited advertising or promotional material if its retail value exceeds \$20. You must return items exceeding this value to the sender or dispose of them as directed by the Chief Counsel (or designee) or your ethics counselor.
- You must receive prior supervisory approval before speaking about OTS or publishing OTS-related material for a nonagency audience.
- You may not engage in any outside employment or business activity, paid or unpaid, without prior written supervisory permission from the Deputy Director, Managing Director, Regional Director, or Chief Counsel.
- You may not directly or indirectly make recommendations or suggestions concerning the acquisition, sale, or other divestiture of securities of any OTS-regulated savings association or savings association holding company.
- You may not purchase property owned by the government and under the control of OTS, or sold under the direction or incident to the functions of OTS, without an appropriate waiver.
- You may not have communications with a thrift, its holding company, or affiliates suggesting either of the following:
  - That the examination process is in any way influenced by political issues or considerations.
  - That either the thrift, its holding company, or affiliates should take a particular position on political or legislative issues.

You must notify your supervisor or ethics counselor if you are aware of any communications that might conflict with or compromise either of these restrictions.

### Definition of Prohibited Source

The term “prohibited source” (as used in this Handbook Section) means any person, or entity, who meets any one of the following criteria:

- Seeks official action by OTS.
- Does, or seeks to do, business with OTS.
- Conducts activities regulated by OTS.
- Has interests that may be substantially affected by the performance or nonperformance of your official OTS duties.
- Is an organization with a majority of members who fall within any of the above classifications.

### *Covered OTS Employees*

If you are a covered OTS employee, you must comply with the following restrictions and disclosure requirement(s):

- You (or your spouse or minor child) may not knowingly accept or become obligated on, directly or indirectly, any impermissible extension of credit from an OTS-regulated savings association or its subsidiary. However, you (or your spouse or minor child) may obtain a credit card from an OTS-regulated savings association or its subsidiary with certain limitations:

### *Nonexaminers*

- The terms and conditions are no more favorable than those offered to the public.

### *Examiners*

- The association is not headquartered in your region.
- You are not assigned to examine the association.
- The terms and conditions are no more favorable than those offered to the public.
- You must file a written statement disqualifying yourself from examining the association. (You may still participate in other supervisory matters involving the institution.)

(For limited exceptions, refer to Supplemental Standards 5 CFR § 3101.109(c).)

- You (or your spouse or minor child) may not purchase any asset from a savings association or its affiliate, including an institution in receivership or conservatorship. (For limited exceptions, refer to Supplemental Standards § 3101.109(f).)

- You (or your spouse or minor child) may not purchase, own, or control, directly or indirectly, any security of an OTS-regulated savings association and most savings association holding companies. (For limited exceptions, refer to Supplemental Standards § 3101.109(b).)
- You must file required financial disclosures as described below.

### Financial Disclosure

Employees in Grade 27 or below must file the annual financial disclosure form(s) by October 31 of each year. If you are an employee in Grade 28 or higher, you must file your forms by May 15 of each year.

- If you are an employee in Grades 17 through 20, or an examiner in Grades 20 or below, you must file an OTS Confidential Financial Disclosure Form (OTS 1569A).
- If you are an employee in Grades 21 through 27, you must file an Executive Branch Personnel Confidential Disclosure Report (OGE 450 or 450A).
- If you are an employee in Grade 28 or above, you must file an Executive Branch Personnel Public Financial Disclosure Report (SF 278).
- If you are an employee in Grade 21 or higher, you also must file a Confidential OTS Supplemental Financial Disclosure Form (OTS 1569).

Except for the SF 278, which is public, financial disclosure is confidential. The Privacy Act (5 USC §552a) governs disclosures of reported information. Authorized OTS, Treasury Department, and certain other officials use the information for the following reasons:

- To ensure ethical conduct.
- To prevent conflicts of interest.
- To monitor compliance with the Standards of Ethical Conduct for Employees of the Executive Branch regulations.
- To monitor the prohibitions on loans to and investments by covered OTS employees (5 CFR § 3101.109 (b) and (c)).

The disclosures also permit regions to schedule assignments so that no OTS employee will examine, supervise, or participate in decisions involving a savings association or savings association subsidiary that has taken any of the following actions:

- Extended credit to the OTS employee.<sup>1</sup>
- Employs a relative (especially in a policy-making position).
- Opened employment contacts, as discussed below.

### *Negotiations for Employment*

As an OTS employee you should not negotiate or have any arrangement concerning prospective employment with any person or organization while simultaneously representing OTS in any particular matter that affects the person or the organization. Under 18 USC § 208(a), such negotiations or arrangement may be a crime.

Concerning job offers, you must immediately inform your supervisor of offers of employment in either of the following circumstances:

- If you do not unconditionally and immediately reject the offer from a savings association or other prohibited source.
- The region has assigned, or you believe it is likely the region will assign, you to examine, supervise, or make any regulatory decision affecting that prohibited source.

Your supervisor and/or ethics counselor must decide if you should provide an employment restriction (recusal) to eliminate any potential conflict of interest. Recusal from any current assignment(s) should last until you resign or send a written rejection of the employment offer. Outright and immediate rejection of unsolicited offers requires no recusal, but a memorandum to the file or to your supervisor is advisable.

An OTS employee rejected for a job by a prohibited source should generally refrain from participating in OTS matters relating to the potential employer for at least one year. However, a written review of the matter by an OTS ethics official recommending an exception, may permit earlier participation by the employee.

## PROFESSIONAL CONDUCT IN INSTITUTIONS

The following presents professional conduct guidelines that address some issues that examiners may face in their day-to-day work in institutions.

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<sup>1</sup> Rules governing the conduct of OTS personnel prohibit covered OTS employees from obtaining new credit from savings associations or savings association subsidiaries. Employees with credit outstanding as of April 30, 1991, are grandfathered, provided they are repaying the debt according to the original terms of the note or the loan agreement.

### Duration of Onsite Examinations

Examiners should conduct each examination in the most efficient and least disruptive manner possible, to limit the time spent on site at each institution. To this end, you should thoroughly scope and plan each examination, targeting problem and high-risk areas.

Preexamination activities should include contacting the institution's management and obtaining lists of employees and documents necessary to perform the examination.

### Working Hours

EICs should manage time in a responsible and professional manner. The examination staff conducts examinations on an Alternative Work Schedule (AWS). This allows for eight nine-hour days, one eight-hour day, and one day off during each two-week pay period.

Examiners should obtain approval from the EIC for deviations from normal working hours during an examination and should explain to the EIC the reason for all absences not preapproved. Also, the EIC should inform the institution's management of any unusual variances, especially absences, from the normal work schedule. Absences without notice give the impression of lack of responsibility and care.

### Working Space

Savings associations should provide adequate working space for examiners. If space is inadequate, examiners may request additional or other space as long as its use does not unreasonably disrupt association operations.

To avoid any appearance of impropriety, when you are working in an institution you should take the following precautions:

- Ensure that a representative of the institution is on the premises whenever you are working.
- Not accept keys to the institution's offices or assume responsibility for its property.
- Not enter places where there is a possibility of access to cash or other negotiable instruments unless a representative of the institution accompanies you.

### Access to Information

When you are in an institution you must take care to adhere to the following procedures:

- Carefully protect all information an institution entrusts to you and secure it from unauthorized access.
- Never leave confidential documents unattended; you should lock them up when not in use.
- Never divulge confidential information in any form to unauthorized persons.

- Never leave computers unattended in the following circumstances:
  - While logged onto an OTS system.
  - While the computer is in a status that would allow unauthorized access to an OTS system or to any confidential data stored on diskettes or disk drives.

You should notify the EIC or other supervisors if the institution refuses to provide you with any information needed to conduct an examination.

### Breaks

The EIC will determine the propriety, times, and lengths of breaks.

### Lunches

You may use an institution's dining facilities if the institution invites you to do so and you pay for your own meals. Examiners on assignments with large crews should stagger their lunch breaks so that the entire crew is not absent from the work place simultaneously.

### Professional Decorum

The following guidelines are general prescriptions for interacting with other regulators and institution employees during an examination.

- You should limit unnecessary conversations with other regulators and the institution's employees.
- You should treat institution employees in a courteous, friendly, yet businesslike manner.
- You should not discuss work with unauthorized employees. You should generally confer with the EIC before discussing anything other than routine matters with employees or management.

### Smoking

OTS employees who smoke should always be courteous and considerate of others, and should follow any institution rules regarding smoking.

### Telephone Calls

You should limit telephone usage, even for official matters. You should avoid personal telephone calls unless they are absolutely necessary.

### Parking

You may use an institution's private parking facilities if invited to do so by the institution. The EIC must, however, approve such use, which should not unduly inconvenience employees or customers.

If the institution uses an independent parking facility, you may not park there at the institution's expense.

### Travel Expenses

All travel, lodging, and subsistence expenses incurred while on official duty shall be paid for or reimbursed only by OTS. For further information regarding reimbursement for travel and lodging refer to OTS's National Travel Policy manual.

### Business Attire

You should wear appropriate business attire at an institution. Standards of appropriateness may vary depending on regional policy, the institution, and the customs of the community.

## REFERENCES

See The OTS Employee Ethics and Standards of Conduct Resource Guide.

### United States Code (18 USC)

Chapter 11                      Bribery, Graft, and Conflicts of Interest  
§§ 201-219  
(Appendix 14)

### Code of Federal Regulations (5 CFR)

Part 2635                      Standards of Ethical Conduct for Employees of the Executive Branch  
§§ 2635.101-902

Part 735                        Employee Responsibilities and Conduct  
§§ 735.101-203 (p. 79)

Part 3101                      Supplemental Standards of Ethical Conduct for Employees of the Department  
§§ 3101.101-104,              of the Treasury  
109 (Appendix 3)



Code of Federal Regulations (31 CFR)

Part 0 §§0.101-217 Department of the Treasury Employee Rules of Conduct  
(Appendix 2)

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## Examination Systems

This Handbook Section provides you with information on OTS Examination Systems: the Examination Data System/Report of Examination (EDS/ROE) system, the Electronic Continuing Examination Folder (ECEP), and Regulatory Profiles. For purposes of this Handbook Section, we define “you” as OTS personnel.

### THE EDS/ROE SYSTEM

OTS uses a web-based EDS/ROE system. The EDS/ROE system collects and stores examination data and reports of examination for all entities examined and supervised by OTS.

EDS refers to the Examination Data System, which captures basic data from an institution’s examination and maintains it on a central database in Washington. The ROE or Report of Examination is stored as a separate file in the EDS/ROE system.

L I N K S	You may access EDS/ROE from the Electronic Continuing Examination Folder (ECEP) Docket Selector on the OTSNet home page. Refer to the “Examination Data System/Report of Examination Users Guide” for assistance when using the EDS/ROE system. The users guide is available in Exam Docs under the Systems menu on the OTSNet.
 <a href="#">Appendix A</a>	

The EDS/ROE system is easy to use, maintain, and troubleshoot; and provides flexibility in creating and editing reports of examination. You can develop standard reports for individual institutions or groups of institutions categorized by docket file, specific caseload, state, subregion, region, or all regions.

### The Examination Data System

The EDS is composed of various component screens – Main, Ratings, Supplemental, and Reportable Data – that you may access throughout the examination process.

#### *EDS Main*

At the EDS Main screen, record the following information as it becomes available during the examination:

- Examination type
- Lead region

- Examiner-in-charge
- Start date
- Completion date
- Close or ROE mail date
- Lead agency, other participating agencies, and the hours of each agency's participation.

Upon data entry, all information recorded in EDS Main is saved directly to the EDS/ROE database and becomes available on the ECEF system. This includes data entered into ratings, supplemental, and reportable data. ECEF users can immediately view all data saved to the database.

### Examination Types

There are several examination types. You can change the examination type at any point in the examination process before transfer of the final ROE. For a listing of valid examination types and the format and ratings required for each type, please refer to the "Examination Data System/Report of Examination Users Guide."

All examination types, except state examinations, may be joint examinations with other regulators.

All examination types,  
except state  
examinations, may be  
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other regulators.

OTS categorizes examinations as "regular" or "limited." Regular exams use ROE shell documents. The limited examination replaces the previously designated on-site and off-site supplemental examinations, field visit, and off-site monitoring. You can use letter or memo format, ROE shell documents, or any combination thereof for limited examinations.

For state examinations use a type 11, 16, or 68 (intervening compliance examination) depending on whether the examination is joint or intervening. See Examinations with State Regulators in this Handbook Section.

See Appendix A for a list of savings association safety and soundness, compliance, and comprehensive examination types. Refer to the "Report of Examination Instructions" in Exam Docs for guidance on completing a type 16 comprehensive ROE.

### Examination Start Date

Record the official examination start date in EDS Main anytime from the scheduling of an examination until the day the on-site examination work begins. For on-site examinations, the start date is always the day that you begin on-site work. On-site work includes examination procedures you perform while on

the subject institution's premises, courthouse, building site, real estate office, or other location outside of an OTS office. The EDS/ROE system automatically enters this date on the cover page of the ROE.

For off-site examinations, the start date is always the day you begin off-site work. Off-site work includes examination procedures you perform while in an OTS office. For off-site examinations, enter the date office work begins. The EDS/ROE system automatically enters this date on the cover page of the ROE.

You can change the start date at any point in the examination process before transferring the final ROE.

#### Examination Completion Date

Record the official completion date of the on-site examination work, which is the date of the last day you are on-site at the institution. For off-site examinations, enter the date office work ends.

#### Close (ROE Mail) Date

EDS Main also includes the date the examination is closed and the report is mailed to the institution and transferred to Washington. This date is referred to as the close, transmittal, or mail date. Do not confuse the close date with the completion (of on-site work) date. You enter the close (ROE mail) date from the ROE Transfer screen when executing the transfer of the final report.

It is no longer necessary to retransmit a ROE in order to amend the ROE mail date. You can now amend this date without requiring an additional ROE transfer.

#### *EDS Ratings*

The Examination Rating Section records the CAMELS composite and component ratings and the Compliance rating for the examination. The Examination Ratings Section also has a data field for Technology Risk Controls (TRC). CAMELS composite and component ratings and the Compliance ratings are entered as 1, 2, 3, 4, or 5. The "N" default rating is no longer valid. For TRC, the EIC answers Yes or No to indicate whether significant Information Technology (IT) concerns were noted in the Report of Examination (TRC Flag). The system will accept a blank entry until the transfer of the final report.

For regular examinations, OTS requires a rating for each component, including the TRC Flag.

At the conclusion of the examination, it is the responsibility of the EIC to assign ratings, and check Yes or No for the TRC Flag, when required. If the scope for a particular examination is not sufficient to assign a rating to each individual component, the EIC should only assign a rating to those components that were reviewed and leave blank those components that were not reviewed.

For regular examinations, OTS requires a rating for each component, including the TRC Flag. The eligibility and limited examination types require only the component ratings appropriate for the

individual examination. The TRC Flag is optional for these examination types. Regional Directors have the authority to accept a state examination as a substitute for an OTS examination on an alternating basis. See the discussion on state examinations in this Handbook Section.

Refer to Examination Handbook [Section 070, Ratings: Developing, Assigning, and Presenting](#), for a description of the criteria regarding the CAMELS composite and component ratings as well as for information regarding the Compliance and CRA ratings. OTS provides additional guidance in assigning CAMELS ratings in the “Report of Examination Instructions.”

### Risk Focused Exams

OTS modified the system to allow flexibility in completing the report of examination. For comprehensive type 16 exams where any CAMELS component or Compliance is rated 1 or 2, the system designates the corresponding ROE section as an optional section rather than as mandatory.

### *EDS Supplemental*

EDS Supplemental records examination findings as data that you can retrieve and analyze. Enter this data into EDS Supplemental during or soon after you complete an examination. This section supplements the ROE. OTS uses this information as a data source for analysis and planning, and for inclusion in the next ROE.

EDS Supplemental consists of two sections labeled on the data input screen as Asset Quality and Exposure Limits. Enter this information during the course of the examination.

EDS Supplemental also requires you to specify if OTS needs to take follow-up action. There are two options – follow-up action required for BSA or for Other.

### Asset Quality

Enter asset classifications in EDS and compare them with the asset classifications reported in the TFR as of the same date.

### *Classified as of TFR date*

The system stores the date of the quarterly TFR information used in an examination in the field identified on the input screen as: Classified as of TFR date. The system requires an entry into the Classified as of TFR date when you enter data into the asset classifications field. The date cannot be greater than current TFR cycle, and cannot be earlier than two TFR cycles.

### Exposure Limits

Enter the interest rate risk net portfolio value (NPV) exposure limits set by the thrift. This record allows a comparison of the limits with actual performance as reported in the Consolidated Maturity and Rate report (CMR).

### *EDS Reportable Data*

The system allows you to file information about regulatory violations. The EDS system stores the information in a database. OTS uses this information for reports to the Federal Reserve, Financial Crimes Enforcement Network (FINCEN), and to respond to Congressional or GAO inquiries.

You should list all substantive and technical violations of certain laws and regulations. You should also enter comments and other information called for in the drop down fields in EDS/ROE Reportable Data, even when you include them in the ROE. You may also enter any other violations you discussed with management but did not include in the ROE.

### Determining if a Violation is Substantive

The terms substantive, significant, and material have the same meaning in this area.

You should consider the association's overall record (S&S and Compliance) when determining if a violation is substantive. You should also consider the following factors:

- The severity of the violation.
- The time span of the violation.
- Whether the violation is widespread or isolated.
- Whether the violation is systemic.
- Related findings on prior exams.
- The risk profile of the institution.

### *Technical Violations*

You should note all technical violations, those violations that do not rise to the level of substantive, in the work papers and enter it into Reportable Data. You should discuss technical violations with management. For example, a common technical violation is the failure of the association to completely or correctly fill out a form in an isolated instance.

### *Repeat Substantive Violations*

To be a repeat substantive violation(s), OTS must have previously brought it to the association's attention. A violation can be a repeat violation if it was in a previous ROE, discussed with management, or be from another source, such as correspondence. It is not necessary that the violation(s) be in the previous examination report to be a repeat violation; however, you must have the discussion with management about the violation documented.

## The Report of Examination System

The Report of Examination system consists of the ROE Shell and the ROE Center.

### *ROE Shell*

The ROE shell is the document OTS uses to report examination findings. During the course of the examination, the examination team completes a draft version of the ROE on a personal computer using the Microsoft Word ROE preformatted shells that you download from the system.

OTS requires the ROE shell format for comprehensive and intervening compliance examinations.

By accessing the ROE Shell and selecting the pages pertinent to the type of examination, you create the report of examination that OTS eventually mails to the thrift. The system populates the financial data into the relevant sections and e-mails you the selected sections. You can download additional pages or sections throughout the examination process. It is not necessary for a single user to download the entire ROE shell. Different individuals on the examination team can download and complete sections of the ROE document.

You can make changes to a particular ROE section by uploading only the individual section.

You do not have to update headers in individual ROE documents. The system will automatically update headers during the compile process.

The system automatically generates the Table of Contents and necessary Rating Definitions documents during the compile process.

### Types of Examination Packages

Two types of ROE formats are available. They are the ROE shell format and the ROE memo/letter format.

#### *ROE Shell Format*

OTS requires the ROE shell format for comprehensive and intervening compliance examinations. The ROE shell format consists of mandatory and optional pages. The four federal financial institution regulatory agencies use similar report pages to promote consistency and reduce regulatory burden.

In general, the use of optional pages depends on the type of examination and the previous rating. You must use the CAMELS and Compliance pages if the institution has a 3, 4, or 5 CAMELS composite or Compliance rating. OTS encourages you to use only ROE pages that are useful in presenting examination findings.



*Memo/Letter Format*

The memo/letter ROE is just that, a memorandum or letter. You may use this format for shorter eligibility and limited examinations – previously designated on-site and off-site supplemental examinations, field visits, and off-site monitoring examinations. You can attach any of the ROE sections to the memo/letter report if needed. If necessary or desirable, you may also use the ROE format for eligibility or limited examinations.

*ROE Center*

The EIC is responsible for preparing examination reports according to established policies and procedures. The regional director, or designee, is responsible for final approval of examination reports. You should incorporate into the ROE, events that occur after the completion of the examination, but before the examination is closed, such as the institution's agreeing to corrective action.

Once the ROE is in final form, the appropriate regional office sends a copy to the institution and uploads the report to the EDS/ROE, thus closing the examination. (Limited ROEs with no ratings may be sent to the thrift at the region's discretion.) The region may send additional copies to other agencies, such as the FDIC or the state regulator. The EDS/ROE system does not accommodate transmittal letters that act as cover memos to distribute the ROE.

The regional office enters the date the report was transmitted to the institution into EDS/ROE, indicating its final acceptance of the ROE. The ROE document cannot be altered after this entry. However, you may use the EDS amendment function to correct errors. The paper copy of the ROE stored by the region is the official document of record.

At the time of transmittal, the examination must be current, based on all available information. The regional office should never send a ROE with an outdated rating to an institution. Any significant events occurring after the examination is closed should be addressed in a subsequent, limited examination and in the Regulatory Profile.

## Examinations with State Regulators

*Joint Examinations*

OTS submits examination reports jointly with certain state agencies. OTS also conducts examinations on an alternating basis with certain state agencies.

Use the type 16 ROE shell when OTS completes the ROE in a joint examination.

For the few states that use OTS's ROE shell when the state prepares the report (joint or intervening), provide them with the type 11 shell. Modify it accordingly. If it is an intervening state examination or joint examination when the state prepares the ROE and you need to conduct a compliance exam, use a type 68 ROE shell.

### *Intervening State Examinations*

OTS has agreements with some states to accept an intervening state examination. Regional offices may accept full-scope, on-site examinations conducted by the regulatory authorities of state-chartered depository institutions on an alternating basis instead of an OTS examination, if such examinations meet the requirements and objectives of OTS's examination strategy.

OTS accepts intervening state examinations for the following savings associations:

- Composite 1- or 2-rated associations.
- Stable and improving composite 3-rated associations if off-site monitoring between examinations confirms the last composite rating and OTS does not note any adverse trends from available information.

The length of time between examinations (regardless of whether OTS or the state conducts the examination) should not exceed 12 (or 18) months based on the statutory examination cycle requirements.

Use the type 11 memo-style ROE shell to enter text or upload information for intervening state examinations and OTS is not conducting the compliance examination.

If you cannot upload a state ROE into EDS/ROE (e.g., the ROE is a WordPerfect document) enter the following message into a memo-style ROE type 11 and upload into EDS/ROE:

“This is an intervening state examination in accordance with provisions set forth in the Federal Deposit Insurance Corporation Improvement Act of 1991. The official hard copy Report of Examination (ROE) is retained with the examination work papers. These files are stored at the OTS Regional Office. To obtain a copy of this ROE, contact the Regional Office.”

You may also scan ROEs conducted by a State Banking Authority into a portable document file (pdf) format and upload the document into ROE Center.

### *Compliance Examinations*

States generally do not perform Compliance examinations. OTS conducts a compliance examination as part of a comprehensive examination. However, OTS does not conduct a separate Compliance examination concurrently with intervening state examinations if all of the following conditions exist:

- The previous Compliance rating was 1 or 2.
- Off-site monitoring shows no material change in the association's compliance risk profile.
- The association corrected any previous compliance deficiencies.

If the association does not meet the above criteria, OTS conducts the compliance portion of the examination and uses the intervening compliance examination, type 68. The type 68 includes the following pages:

- Prohibition of Disclosure or Release
- Board Letter
- Signatures of Directors
- Table of Contents
- Examination Conclusions and Comments
- Matters Requiring Board Attention
- Compliance
- Compliance Rating Definitions.

### *FDIC*

When the FDIC and the OTS conduct a joint examination, the FDIC may prepare additional reports or information. The FDIC will provide copies to the OTS for internal purposes only; the institution, however, will receive only the OTS report. The OTS will provide the FDIC with copies of ROEs as follows:

#### For Associations:

3-, 4-, and 5-rated	cc FDIC
1- and 2-rated	bcc FDIC
Largest <sup>1</sup> 8 institutions	cc FDIC

#### For Holding Companies:

3-, 4-, or 5-rated institutions	cc of the HC report FDIC
Unsatisfactory rated HC	cc of the HC report FDIC
HC of largest <sup>1</sup> 8 institutions	cc of the HC report FDIC

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<sup>1</sup> Eight largest Institutions, National Banks and State Banks.

## THE ELECTRONIC CONTINUING EXAMINATION FOLDER

ECEF is an intranet-based system for storing and displaying documents related to a particular OTS-regulated savings association. Authorized users in each region use ECEF as a case management tool and add and manage ECEF documents on the intranet. ECEF documents include correspondence, regional reports, forms and other documents. At the conclusion of an examination, authorized users should update the ECEF and, if applicable, create or update the Regulatory Profile. The ECEF for the association will include a Regulatory Profile if the regional office has designated it as a high-profile association.

You may access ECEF from the OTSNet home page.

## REGULATORY PROFILES

A Regulatory Profile is a concise written summary of the characteristics and condition of an OTS-regulated savings association. The Regulatory Profile includes the association's:

- Name, address, docket number, and other identifying information.
- Latest examination ratings and dates.
- Selected quarterly operating results.

A Regulatory Profile is a concise written summary of the characteristics and condition of an OTS-regulated savings association.

When necessary as explained below, the Regulatory Profile includes a brief narrative summary with four sections: Operating Profile, Identified Risks, Enforcement Actions, and Supervisory Strategy.

For detailed policies and procedures, see the Regulatory Profile Users Guide on the OTS Intranet. This Guide is accessible to all employees by clicking on ECEF, selecting a region, clicking on Profiles, and opening the Reg Profile Help file.

## Policy

The Regulatory Profile System designates all savings associations as either low-profile or high-profile. Each designation has a different policy.

### *Low-Profile Savings Associations*

Low-profile savings associations generally meet all of the following criteria:

- Total assets less than \$10 billion.
- Composite CAMELS rating of 1 or 2.

- No significant risk factors.

The OTS system automatically generates Regulatory Profiles for every low-profile association using data from OTS national systems, including the Thrift Financial Report (TFR) and the EDS/ROE. Profiles for low-profile associations only include the following information:

Regulatory Profiles for *low-profile* associations are completely automated and do not require any input or maintenance by OTS employees. Regulatory Profiles for *high-profile* associations require periodic updates and regional employee input into the system.

- Name, address, docket number, and other identifying data.
- Latest examination ratings and dates.
- Selected quarterly operating results.

Regulatory Profiles for low-profile associations are completely automated and do not require any input or maintenance by OTS employees.

### *High-Profile Savings Associations*

High-profile savings associations generally include associations that meet any one of the following criteria:

- A Composite CAMELS rating of 4 or 5.
- A Compliance rating of 4 or 5.
- A CRA rating of Needs to Improve or Substantial Noncompliance.
- A Composite CAMELS rating of 3 and assets greater than \$1 billion.
- A Composite CAMELS rating of 3 and assets less than \$1 billion with an Enforcement Action (not including BSA).
- Total assets of \$10 Billion or greater.
- Unsatisfactory Holding Company Rating.
- Enforcement Action against the Holding Company.
- Associations designated by the Regional Director as High Profile for other reasons.

Regulatory Profiles for high-profile institutions consist of a narrative summary and the same system-generated identifying data, examination ratings, and operating results as low-profile institutions. In addition, Regulatory Profiles for “high-profile” institutions require regional employees to create a brief narrative summary for every high-profile association they supervise consisting of four sections:

1. **Operating Profile**: A brief description of the association’s financial condition and any unique operating strategies.
2. **Identified Risks**: A summary of any significant risks identified at the association, including safety and soundness, compliance, or other risks. This section should clearly identify any material problems or concerns.
3. **Enforcement Actions**: A summary of all active, outstanding enforcement actions, including a brief description of the violation or problem, the resulting enforcement action, and the date of the action.
4. **Supervisory Strategy**: The supervisory strategy for addressing each of the noted problems or concerns. This section may list monitoring procedures, corrective actions, and specific items for on-site examination.

The region creates this four-section narrative summary whenever an association meets any of the high-profile criteria listed above. Regional employees should update the summary, quarterly within 60 days after the end of each quarter, to include the following discussion points:

- Status of corrective action(s) and follow-up action(s).
- Status of the association’s efforts to address material problems identified during prior examinations.
- Plans for supervisory or enforcement action in situations where management and the board failed to correct material problems.
- Status of the association’s compliance with discretionary and non-discretionary PCA restrictions, or compliance with outstanding supervisory or enforcement actions.
- Whether the PCA situation warrants a field visit(s) or written reports from the board of directors.

If an association is high profile but there is no information to report in a particular section, note this explicitly within the relevant section. For example, “No outstanding enforcement actions.” The Regulatory Profile will not exceed two pages.

## REFERENCES

Report of Examination Instructions

Examination Data System/Report of Examination Users Guide

Regulatory Profile User's Guide

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EXAMINATION TYPES

	Comprehensive Exams			Non-Comprehensive Exams	
	Type 16	Type 30	Type 46	Type 11	Type 68
Name of Exam	Comprehensive Federal Exam with Regular Scope	Eligibility Exam	Comprehensive Exam with Limited Scope	State S&S <sup>1</sup>	Intervening Compliance Exam
Ratings Required	CAMELS, Compliance and TRC	None Required	None Required	CAMELS only	Compliance only
ROE or Memo	ROE	ROE or Memo	ROE or Memo	ROE or state format	ROE
Scope	Full scope	Full scope or limited scope	Limited scope	Full scope (S&S only)	Full scope (Compliance only)
On-site or Off-site	On-site	Either	Either	On-site	On-site
Conditions for use	Every 12-18 months, based on size and condition of the association. Use for OTS only, alternate, or joint exams with the State or FDIC.	For any entity desiring a thrift charter.	Whenever OTS needs to conduct an examination outside the normal cycle. Can change any ratings, which may affect the examination cycle.	When the state conducts and OTS accepts the S&S examination report every other year or when the state files the report during joint exams and uses the OTS ROE shell.	Only use when OTS must perform a compliance exam (due to rating or condition) when the state conducts an intervening state exam.

<sup>1</sup> Referred to as alternate exams on OTS years; use a type 16.

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## Examination Scheduling, Scoping, and Management

On April 11, 2002, the Director of the Office of Thrift Supervision (OTS) announced an initiative to improve the examination process by combining the safety and soundness (S&S) and compliance examination functions. Instead of having two separate examination teams (S&S and compliance), each performing an examination and issuing a report, OTS will conduct a comprehensive examination that produces one report of examination and a more thorough assessment of a savings association's risk profile.

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### L I N K S

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 [Program](#)

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 [Appendix A](#)

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 [Appendix B](#)

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 [Appendix C](#)

Since August 1, 2002, OTS has been moving towards a more comprehensive examination process. Currently, OTS is in the process of dually accrediting most of its examination staff. Ultimately one examiner-in-charge (EIC) will run comprehensive examinations. Until the agency has EIC level examiners capable of evaluating both safety and soundness and compliance risk, however, two EICs (one well versed in the CAMELS areas and one well versed in Compliance) will oversee the comprehensive examinations. OTS expects that these two EICs will work in tandem as one to ensure a well coordinated, risk focused, comprehensive examination. Therefore, in this Section, when we refer to EIC we mean either a dually accredited EIC or two EICs who are working together as a team. This means planning together, scoping together, conducting interviews together, etc., to conduct the CAMELS and Compliance reviews as one examination.

Other key considerations in a comprehensive examination:

- To consider findings related to Capital, Asset Quality, Earnings, Liquidity, Sensitivity and Compliance in the Management evaluation and component rating. Assess the overall adequacy and effectiveness of risk management and compliance management functions of the association.
- If the EIC determines that transactional level review of certain activities is necessary from both a safety and soundness and compliance review standpoint, then the EIC should ensure that one examiner conducts those reviews efficiently and without redundancy. For instance, when reviewing single-family loan files for the asset quality review, the same examiner can check compliance information such as flood and RESPA.

This Handbook Section integrates the S&S and compliance examination strategy, scoping, and management processes. This Section also provides guidance for Limited and Joint OTS/FDIC examinations.

## EXAMINATION STRATEGY AND OBJECTIVES

*Timely, efficient, and risk-focused* examinations are essential to an effective regulatory oversight function.

*Timely* examinations ensure that the agency stays abreast of changes in the condition or management of an association. A risk focused examination ensures that OTS examines those associations that pose most risk more frequently, and those with less risk, less frequently. An efficient examination eliminates multiple reviews of the same area for different purposes by combining safety and soundness and compliance reviews of the same areas such as lending or deposits.

*Timely, efficient, and risk-focused* examinations are essential to an effective regulatory oversight function.

OTS bases the timing of an on-site examination partly on the risk profile of the association, and partly on the scope of examination for any given association. All examinations should be *risk-focused*, meaning that you spend more time looking at higher risk areas within an organization and less time looking at low risk areas. Risk can be based on the nature of an associations operations, the quality of management and staff, and the adequacy of management and the board's ability to identify, manage and monitor risk, and take timely action to remedy identified problems.

Risk-focused examinations assist the agency in ensuring *efficient* use of its resources and ensures that examiners spend the most time looking at areas or activities that pose the most risk. We also achieve efficiency in the examination process through a well-managed examination. Staffing should be appropriate to the size of the association and the scope of the review. In addition, the EIC achieves economies of scale whenever possible to eliminate any redundancies in the review process, particularly between the safety and soundness and compliance transactional level reviews of loans or deposits during the examination. In those associations with adequate compliance management functions and a lower risk loan portfolio, transactional level review may be minimal and thus limit the opportunities for combining transaction review processes. However, the EIC should be mindful of situations where examiners can combine safety and soundness and compliance reviews (particularly at a transactional level).

The goal of the comprehensive examination process is to conduct a single examination where the exam team reviews the compliance and the CAMELS component areas. Based upon the findings in each of these areas, the examination team should be able to make an overall assessment of the association in terms of risk, adequacy of management and the system of risk and compliance management, and future prospects.

## SCHEDULING EXAMINATIONS

OTS must schedule full-scope (type 16), on-site examinations of insured depository institutions once during a 12-month cycle or once during an 18-month cycle. You may conduct a limited examination under certain conditions. (See the discussion of Limited Examinations at the end of this Handbook Section.)

A full-scope examination, according to the statute, means that you conduct an on-site examination and rate all CAMELS components. For comprehensive examination purposes, OTS also conducts a compliance review as part of a full-scope examination except as noted below under Intervening State Examinations.

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 OTS transmits the Report of Examination (ROE) to the association.

### Intervening State Examinations

Regional offices may accept full-scope, on-site examinations conducted by the regulatory authorities of state-chartered depository institutions on an alternating basis instead of an OTS examination, if such examinations meet the requirements and objectives of OTS’s examination strategy. OTS has certain agreements with some States to accept an intervening state examination. OTS accepts intervening state examinations for the following savings associations:

- Composite 1- or 2-rated associations.
- Stable and improving composite 3-rated associations if off-site monitoring between examinations confirms the last composite rating and OTS does not note any adverse trends from available information.

The length of time between examinations (regardless of whether OTS or the state conducts the examination) should not exceed 12 (or 18) months based on the statutory examination cycle requirements.

Generally, States do not perform a Compliance review as part of their examinations. OTS will conduct a separate Compliance review concurrently with intervening state examinations unless all of the following conditions exist:

- The previous Compliance rating was 1 or 2.
- Off-site monitoring shows no material change in the association’s risk profile.
- The association corrected any previous compliance deficiencies.

### 12-month Cycle

You must conduct a full-scope (type 16), on-site examination of the association once during each 12-month period unless the association meets the 18-month cycle requirements below.

By conducting examinations annually, you increase the 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 savings associations are subject to the 12-month examination cycle. The 12-month examination cycle should continue until management has demonstrated its ability to operate an association in a safe and sound manner and satisfied all conditions imposed at the time of approval.

### 18-month Cycle

An 18-month examination interval applies to insured savings associations with total assets of \$250 million or less that meet the following criteria in 12 CFR § 563.171:

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

Revert to the 12-month examination schedule if any of the following occurs:

- An enforcement action.
- An acquisition or change in control.
- A change in asset size to >\$250 million.
- A downgrade in PCA rating.
- A downgrade to a 3 or worse in the CAMELS composite rating, the Compliance rating, or Management component rating.

If a triggering event occurs in any of the following time frames at an association 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 association under a 12-month examination interval becomes eligible for an expanded interval, the regional office may immediately expand the interval to 18 months.

## EXAMINATION SCOPING AND PLANNING

### Scoping an Examination

Scoping is an integral part of a risk-focused examination process, assisting examiners in targeting higher risk areas for review and in determining the appropriate examination procedures for that review. Scoping is the examination planning process that matches the risk profile of an association with the examination programs to enable a focused evaluation of association performance and appropriate rating assignments and conclusions. Scoping is the starting point of any examination and usually begins off-site.

Scoping is an integral part of a risk-focused examination process, assisting examiners in targeting higher risk areas for review and in determining the appropriate examination procedures for that review.

In brief, scoping enables you to understand the present risk profile of an association based on the following:

- A review and analysis of prior examination reports and prior track record of management.
- A review of agency monitoring records and PERK data.
- Interviews with management.
- An assessment about changes in business operations, staffing, or external circumstances.

Based on this risk profile, the EIC can then determine the appropriate areas for examiner review, the depth of review required, the examination procedures to use, and the examination personnel requirements. The EIC may modify an examination scope based on findings during the course of an examination.

Scoping consists of three stages:

- Reviewing preexamination information.

- Conducting management interviews.
- Developing a risk assessment.

It is critical to the risk-focused examination process that you conduct these stages using the most effective off-site and on-site methods that regional resources permit.

### *Review Preexamination Information*

Generally, the EIC begins the scoping process off-site, before the start of the examination, leveraging off work performed by regional staff responsible for monitoring and updating the ECEF and Regulatory Profiles, prior exams and work papers, and relevant PERK materials.

A sample of items that you may review off-site include the following:

#### Agency Information

- The Electronic Continuing Examination Folder (ECEF), (including Quarterly Monitoring Reports (QMRs) and, if applicable, the Regulatory Profile for the association.
- Results of regional off-site monitoring.
- OTS financial reports including TFR and UTPR.
- Prior thrift, compliance, and holding company, work papers, and recommendations.
- Unresolved issues from preceding examinations.
- Correspondence covering significant matters involving the association that transpired between exams.
- Other correspondence and internal memoranda involving the association.
- Application information – conditions of approval and major applications filed.
- Documentation on supervisory and enforcement actions.
- Consumer complaints filed with OTS since the last examination.
- Suspicious Activity Reports and Currency Transaction Reports.
- CRA Wiz/ HMDA data.



PERK Information

- Preliminary Examination Response Kit (PERK) documents completed by association management before the start of the examination for information related to the following:
  - Changes in operations.
  - Changes in technology risk, systems and controls.
  - Board meetings.
  - Internal and external audits.
  - Compliance self-assessments.
  - Responses and corrective actions to exams and audits.
  - Significant changes in outsourcing or vendor relationships.

General Data

- Economic information about the association's market area(s).
- News articles, including Internet sources.

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

- Relevant PERK documents not available before the examination begins.
- Board reports, board minutes, and management reports.
- Compliance reviews and/or compliance self-assessments.
- Internal audit reports.
- Internal Asset Review reports.
- Business plan.
- Operating budget.
- Any new contracts (for example: employment, information systems, leases, etc.).
- Any new or revised policies and procedures.

- Any new product or delivery channel specifications and associated marketing plans.

### *Conduct Management Interviews*

In this stage of the scoping process, the EIC should conduct detailed interviews with the President/CEO, senior management, compliance officer, internal auditor, information security officer, general counsel, or other responsible staff, as applicable. You may conduct some of the initial discussions off-site. Further discussions will take place on-site at the start of the examination and continue (as needed) throughout the duration of the examination.

Use the interview process to confirm, modify, or supplement your preliminary judgment about the association's risk profile, changes in risk profile, management's response to those changes, and management's track record. As the EIC, you should communicate the results of the interviews to the examination team. Discussions should cover the operational impact of the following:

- Business strategic development and implementation.
- Modifications of organizational structure and lines of responsibility.
- Scope and effectiveness of employee training programs.
- Variations in financial condition or risk profile, and operating performance in comparison with the budget.
- Changes in operations that could affect ongoing safety and soundness and compliance performance.
- Actions taken to correct deficiencies identified in previous examinations, audits or compliance self-assessments.
- Management's perspective on economic conditions directly or indirectly affecting the association's financial performance and risk profile.
- Management's status in implementing a formal written compliance policy and self-assessment.
- Alteration of existing or development of new products.
- Significant internal or external audit findings, and management's response to those findings.
- Management's adherence to, or departure from, formally established procedures or standard practices.
- Addition or removal of third-party service providers.

- Adoption, deployment or modification of information technology platforms or tools.

You should adapt the interview process to address the particular circumstances at each association in response to findings from the pre-examination analysis. (Consult the [Basic Matrix in Appendix A](#) as an aide in identifying the regulatory obligations associated with particular products.) This process will assist you in refining the examination scope and in determining to what extent you examine certain operations, and particular laws and regulations.

### *Risk Assessment*

Proper scoping (through document reviews, data analysis and management interviews) allows the EIC to formulate initial conclusions about the savings association's condition and risk profile, including credit risk, operational risk, interest rate risk, compliance risk, strategic risk, and reputation risk.

Using preexamination information and management interviews allows the EIC to formulate an initial assessment of:

- Current financial condition.
- Management and the board's prior track record.
- Material changes in risk profile or operating strategy, and management's response to those changes.
- The association's internal controls, including technology risk controls, risk management, and compliance management systems.
- Responsiveness of management and the board in implementing corrective action to risk management and compliance management deficiencies since the previous examination, audits or reviews.
- Association's efforts to stay abreast of and train the board, management, and staff on safety and soundness and regulatory compliance developments.

Your assessment of these areas is a critical step for determining examination scope and the risk profile.

### Selecting Examination Programs and Procedures

Based upon the risk assessment, you will determine the appropriate examination programs and procedures to use. You should consider all programs and questionnaires within the scope of the examination, including the risk-focused and tailored examination procedures. You may use a combination of procedures when performing an examination. You should perform a more detailed review of areas with greater risk or with deteriorating performance indicators and actively pursue any concerns or red flags that you uncover during the examination process. For example, if risk factors require you to go beyond tailored examination procedures, you may use any examination procedures

included in the risk-focused examination procedures, examination procedures in the Examination Handbook, or conduct any other type of review determined appropriate to assess risk. You may expand the depth of review of any given area as additional facts surface that necessitate a more comprehensive review.

Use programs and questionnaires as appropriate, but only to the extent necessary to address the scope and support the examination conclusions. Programs provide guidance necessary to support examination findings and ROE comments. Wherever possible and indicated by the risk assessment conduct simultaneous reviews for safety and soundness and consumer compliance assessments.

In many circumstances, you will not need all or even a majority of the programs.

The EIC may find it helpful to use the [Examination Scope Worksheet in Appendix B](#) to indicate the examination programs to complete on an examination. Discuss the scope of the examination with the Field Manager (FM) or Assistant Regional Director (ARD) and document their concurrence on the worksheet. Before the start of the examination, the EIC will prepare a scoping memorandum, signed by the FM or ARD, that sets forth the risk assessment and exam programs. Retain a copy for the work papers.

For example, if your review of the policies, structure, administration, and results of the association's internal asset review program reveals that the program is sufficient and the results are accurate, you may place a greater reliance on the association's internal review. The risk that the association 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 association's condition, but is not excessive. For further information regarding the examination program and the three levels of review, refer to [Examination Handbook Section 010, Handbook and Program Use](#).

## EXAMINATION MANAGEMENT

Effective management of the examination expedites and enhances the examination process by ensuring that the examination team meets the exam objectives and does so in an efficient manner. The level and sophistication of examination management methods and procedures will vary depending on the size, nature, and activities of the association.

The EIC may elect to use an Examination Management Checklist such as that found in [Appendix C](#). The checklist provides the time frames of tasks that need to take place before, during, and after each examination.

## EIC Responsibilities

The EIC carries the primary responsibility for managing the examination. The EIC's responsibilities include:

- **Examination planning, organization, and implementation:** The EIC is responsible for scoping the examination, setting the examination objectives, communicating the examination objectives to the examination team, and ensuring that the exam team meets the examination objectives.
- **Assignments and job monitoring:** The EIC must determine the expertise necessary to perform certain aspects of the examination and make assignments accordingly. The EIC is responsible for realizing the maximum efficiency from conducting coordinated safety and soundness and compliance reviews consistent with the examination's scope. Depending on the size of the job, the EIC may delegate certain management responsibilities to assistants for efficiency and to improve upon administrative and management skills of assistants.
  - Assign priorities to examination tasks and determine optimal use of comprehensive reviews across exam programs. Maximize efficiency by assigning one assistant to conduct or coordinate interrelated S&S and compliance programs to avoid duplication of effort whenever feasible.
  - Brief the examination team members on their respective assignments, including their participation in examination segments that will involve comprehensive reviews across exam programs and/or cross training. Provide them with the necessary information and resources to conduct their assignments efficiently.
  - Explain the risk assessment and scoping judgment relevant to each assistant's assignment. Discuss the effect of information developed during the exam on the association risk profile, possible changes to the scope, opportunities for conducting comprehensive reviews across exam programs, and the ability to meet assignment deadlines throughout the examination. Adjust assignments as warranted by these considerations.
  - Consider completing the Examination Scope Worksheet in [Appendix B](#) when assigning tasks and budgeting examination hours. The EIC specifies the areas to review on the examination considering the scope. As needed, you may add any activities not included on the worksheet.
  - Monitor the progress of the examination to achieve examination objectives in a timely manner and to identify early adjustments to the scope, staffing, and completion date. The EIC should notify a supervisor as soon as adjustments to scope or other events may affect scheduling or the completion date. The supervisor might consider staff reassignment from other jobs, if necessary.

- Prepare Report of Examination: Incorporate program findings and conclusions, edit comments and finalize the ROE. Compile, index and file work papers. Properly record necessary exam data and regulatory violations in agency systems.
- Serve as the primary communications link: The EIC is the focal point for communications on significant matters. Assistants, association personnel, and regional office staff must all know how to communicate information and when to share information. During the examination, it is important that only one responsible individual provide answers to significant items. The EIC should coordinate this in case questions arise.
  - Examiners should communicate any significant changes to the scope and the reasons for them with examiners involved in holding company, trust and asset management, and information technology (IT) examinations. Share significant findings and conclusions to avoid duplicating efforts.
  - When the FDIC or the state participates in an examination, maintain close communication with FDIC regulatory authorities and appropriate state regulatory authorities. See “OTS/FDIC Joint Examinations Process” at the end of this Handbook Section.
  - Early in the examination, the EIC should discuss with the President/CEO, or with a designated association representative, some of the administrative aspects of the examination, including:
    - ♦ Time frames 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.
    - ♦ The expected duration of the examination.
    - ♦ Any planned interruptions (these should be kept to a minimum).
    - ♦ Names of assisting examiners.
  - The EIC should schedule regular meetings with the CEO to discuss the progress of the examination and to address any issues of concern. Conduct the examination efficiently to

minimize undue disruption for the association. Convey any unresolved concerns management expresses about exam progress to a supervisor.

- The EIC should schedule an examination exit meeting with the association's senior management to discuss examination findings, the examiner's overall conclusions, and recommendations (see [Handbook Section 070, Ratings: Developing, Assigning, and Presenting](#)).
- Manage staff development 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 they can make fair and constructive evaluations of their work.
  - 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 they are meeting objectives according to schedule and consistent with agency standards for quality work product. Early identification of work-related problems also allows the assistants the opportunity to correct mistakes and to immediately improve upon skills.
- Ensure 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 association staff.

## Off-Site vs. On-Site Examination Procedures

OTS may conduct some examination procedures off-site as proficiently as they conduct them on-site.

Performing examination procedures off-site is optional. Regional directors or their designee should determine whether off-site work is feasible and develop appropriate policies and procedures. In simple terms, you may perform certain procedures 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.

### *Savings Association Selection Criteria*

You should determine whether to use off-site examination procedures based on certain criteria, including:

- The association's CAMELS and Compliance ratings.
- Prior history.
- Complexity of operations.
- Reliability of data.
- Capabilities of staff assigned.

This approach is flexible because there are no firm guidelines such as asset size, rating, or location to determine when you can or cannot use off-site examination analysis.

Open lines of communication with association personnel are essential at all examinations, but you may have to take extra steps to keep those lines open during off-site portions of the examination. Advise association management of the start and completion of off-site work. Finally, exercise judgment so that you perform on-site work that is appropriate to on-site performance.

#### *PERK Information*

You may specify in the PERK letter that OTS will conduct some of the examination work off-site.

Unless it is necessary to retrieve items from the association, request some items in advance for delivery to the field office or other appropriate location. If you select this option, send the PERK 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 toward using off-site examination procedures. Again, keep open the lines of communication with management.

#### *Examination Data System/ Report of Examination*

The Examination Data System/Report of Examination (EDS/ROE) should continue to reflect the actual start and completion dates of examination work performed on-site. These dates should correspond with the dates disclosed in the cover page of the examination report.

### Continuing Examination File and the General File

#### *Continuing Examination File*

Include the following items, only if applicable to the particular association 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, if applicable.
- Approved Appraisers and Qualifications (PERK)
- All Contracts (PERK)
- Copies of Written Policies (PERK)

If you must include an association policy as part of work paper support, file it in the appropriate CAMELS or Compliance 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 Scope Worksheet ([Appendix B](#))
- Examination Scheduling, Scoping, and Management Program
- PERK Summary Schedule (for next exam)
- Pre-Assignment Analysis
- Overall Conclusions Program
- Recent Correspondence
- News articles

You should use exception sheets to record all specific regulatory and policy violations that you do not specifically discuss 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 Conclusion

The EIC is responsible for reviewing and compiling the examination findings and ensuring the Examination Conclusions and Comments page presents a concise and balanced portrayal of an association's condition and future prospects. The ratings should reflect the overall examination findings and conclusions. Update the ECEF and, if applicable, create or update the Regulatory Profile. Also, ensure that the association takes prompt corrective action for any problems found during the examination and closely monitor the association's condition for any recurrence of these or new problems.

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

Refer to [Examination Handbook Section 070, Ratings: Developing, Assigning, and Presenting](#), for other appropriate examination closing procedures.

### OTS/FDIC JOINT EXAMINATION PROCESS

Pursuant to the Information Sharing and Special Examination Agreement with the FDIC, 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. FDIC will perform all savings association examination activities 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 necessary, the EIC should decide how to conduct the examinations.

OTS is not required to provide the FDIC a copy of the proposed final report before transmitting it to the association.

OTS is responsible for specialty examinations such as Trust and Asset Management and Information Technology.

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

### Special Examinations and Information Sharing

A key principle of the information sharing agreement is that the federal banking agencies are committed to providing the FDIC information on and access to insured depository institutions that represent a heightened risk to the insurance fund.

OTS presumes that the following associations represent a “heightened risk” to the insurance fund:

A key principle of the information sharing agreement is that the federal banking agencies are committed to providing the FDIC information on and access to insured depository institutions that represent a heightened risk to the insurance fund.

- Insured depository institutions with a composite rating of 3, 4, or 5.
- Insured depository institutions that are undercapitalized as defined under Prompt Corrective Action.

In other cases, FDIC may request participation in examinations or meetings when an institution exhibits material deteriorating conditions or other adverse developments that could result in the institution becoming troubled in the near term. In limited instances, the FDIC will need to develop contingency plans for an institution’s possible failure or the commencement of the resolution process. FDIC’s Division of Resolution and Receiverships will work with the primary federal regulator to collect contingency planning information on the following institutions:

- Institutions with composite ratings of 4 that would pose unique or exceptional risks in the event of failure.
- Institutions with existing or anticipated composite ratings of 5.

- Institutions significantly or critically undercapitalized as defined under Prompt Corrective Action.
- Institutions otherwise identified as having adverse developments that could result in the institutions becoming troubled in the near term.

The FDIC will collect the information in the most efficient and least disruptive manner, relying on examiners, work papers, examination reports, and other supervisory information as sources for preliminary contingency planning information. If additional information is needed, FDIC staff will meet and coordinate with the institution's primary regulator prior to conducting any on-site information collection and will, to the extent possible, conduct on-site activities concurrently with the primary regulator's scheduled examinations. FDIC or the primary regulator will notify the appropriate institution contact of FDIC's scheduled on-site presence and purpose. The amount and type of information collected will depend on the nature and severity of an institution's problems or risk profile in the event of failure.

With respect to certain identified large savings associations supervised by OTS, FDIC will establish a dedicated examiner program. OTS will keep the dedicated examiner informed of all material developments in the supervision of the institution and will invite the dedicated examiner to observe and participate in certain examination activities. This will ensure that the FDIC has an understanding of the supervisory issues and risk management structure of the identified thrift.

FDIC will fully participate in the review and assessment of the risk of the credits within the Shared National Credit Program in certain large thrifts. When the agencies agree that FDIC's participation is appropriate to evaluate the risk of a particular banking activity to the deposit insurance funds, the FDIC dedicated examiner and other staff, as appropriate, should participate with OTS in selected supervisory reviews of that activity. This includes meetings with bank management relating to those reviews. In the event Agencies' staff cannot agree, the respective Agencies representative to the FFIEC Supervision Task Force will determine whether FDIC participation is appropriate. In the event the two representatives cannot agree, the Chairman of the FDIC and the Director of OTS will resolve the dispute.

## Report of Examination

Joint examinations 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 ensure that they achieve examination objectives 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 nonsubstantive differences in examination interpretations, conclusions, and report comments. If there are differences in CAMELS and Compliance ratings between FDIC and OTS, FDIC's senior management will, after consultation with OTS' senior management, make any decision to depart from OTS' assigned rating. 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 generally accepted accounting principles 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.

OTS should share, but retain, examination work papers, loan line sheets, report pages, and findings following completion of the examination, and provide interim examination access 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.

### LIMITED EXAMINATIONS

You may conduct a limited examination for the following associations:

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

Use the limited examination (type 46) for reviews focusing on high-risk areas. Limited examinations do not satisfy the 12/18-month requirement.

You may conduct a limited examination on-site or off-site. To determine if an association needs an on-site, limited examination focus on the following factors:

- Changes in business activity and strategy, such as a change in loan product lines, the investment portfolio, or the deposit structure.
- Action taken by management to correct items of concern noted at the most recent examination.
- Deterioration in asset quality indicators such as nonperforming assets.
- Circumstances indicating a deteriorating and deficient Compliance management program.
- Noncompliance 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.
- Changes in other key financial ratios and indicators.
- Other information such as the external audit report, news articles, supervisory correspondence, consumer complaints alleging discrimination, and information obtained from examinations of other savings associations.

You may also use the limited examination to ensure the association's compliance with certain conditions. Depending on the circumstances of the limited examination, you may use specific ROE pages or a memo-style format to report your findings.

## REFERENCES

### Code of Federal Regulations (12 CFR)

§ 563.171      Frequency of Examinations

### Office of Thrift Supervision Bulletins

TB 68a          Appeals and Ombudsman Matters

## Closely Related Handbook Sections

Section 010 [Handbook and Program Use](#)

Section 040 [Examination Systems](#)

Section 045 [Regulatory Action Data \(RAD\) System](#)

Section 070 [Ratings: Developing, Assigning, and Presenting](#)

## OTS Report of Examination Instructions

## Interagency Agreements

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

Information Sharing and Special Examination Agreement with the FDIC (January 25, 2002)

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# Examination Scheduling, Scoping, and Management Program

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## EXAMINATION OBJECTIVES

To ensure that OTS conducts the examination on time according to scheduling requirements.

To ensure that OTS conducts a well-scoped and risk-focused examination:

- Analyze agency records and Preliminary Examination Response Kit (PERK) materials, and conduct interviews with management.
- Develop a risk profile.
- Select examination procedures appropriate to the risks identified.
- Modify the scope and level of review as appropriate based on examination findings.

To ensure that the examination makes efficient use of resources:

- Combine areas of review where appropriate.
- Ensure the appropriate staffing and levels of expertise.
- Conduct off-site work where appropriate.
- Dedicate more resources to higher-risk areas and fewer resources to areas of less risk.
- Supplement formal education programs through on-the-job training.

To ensure that the examination is well-managed:

- Timely receipt of information.
- Open and timely communication with association management, agency staff, and other regulatory staff.
- The examination proceeds as scheduled or the schedule is revised based on adverse examination findings.
- Appropriate examiner conduct.

<b>Exam Date:</b>	
<b>Prepared By:</b>	
<b>Reviewed By:</b>	
<b>Docket #:</b>	

# Examination Scheduling, Scoping, and Management Program

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- Timely identification of material issues.
- Appropriate documentation of work.

To provide useful information for future planning, scoping, monitoring, and management.

## SCHEDULING

The regional office will determine the examination schedule on a 12- or 18-month cycle according to the criteria outlined in this Handbook Section.

## SCOPING PROCEDURES

WKP. REF.

Generally, you should follow the procedures below, however, you must modify these procedures based on the size and complexity of the savings association. For example, for smaller, well-rated associations with strong management and no changes in business operations, it may not be necessary to conduct an extensive review of records and interviews in order to determine the appropriate examination scope.

1. Prior to the examination, review the Electronic Continuing Examination Folder (ECEP) and, if applicable, the Regulatory Profile for the savings association. See [Handbook Section 040, Examination Systems](#).

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2. Tailor the PERK requests on the summary schedule to the savings association and type of examination. Send the PERK to the association at least four weeks prior to the examination start date.

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3. Review the most recent scoping materials available (those available in advance of the examination) and any relevant PERK materials received prior to the examination. This Handbook Section provides a list of scoping and PERK materials.

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4. If applicable, coordinate with the OTS speciality (information technology, etc.) EIC, and the FDIC EIC or FDIC regional office for joint scoping.

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<b>Reviewed By:</b>	
<b>Docket #:</b>	

# Examination Scheduling, Scoping, and Management Program

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WKP. REF.

5. Conduct management and compliance interviews. See this Handbook Section for interview discussion topics.

- Conduct interviews with management by phone, if possible.
- 

6. Formulate a risk assessment based on the following:

- The association's current financial condition.
  - Management and the BOD's prior track record in managing risk and taking corrective action.
  - Material changes in risk profile or operating strategy and management's response to those changes.
  - Quality of internal controls, technology controls, risk management, and compliance management systems.
- 

7. Establish and document the detailed scope for the examination in a scoping memo. Your field manager should review and sign the memo. Retain a copy in the work papers.

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*Note: For branch reviews, evaluate internal controls, management reporting, and audit coverage and findings before establishing scope. It may be necessary to perform only limited reviews of branches, particularly if the association can send credit files and other information to the office where the examiners are working.*

8. Finalize staffing and examination dates. Contact assistants and inquire whether they have scheduled any time off or will be attending any training seminars during the examination.

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# Examination Scheduling, Scoping, and Management Program

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WKP. REF.

9. Prepare assignments for assistants (before commencing the examination, if possible) based on the scope and areas of expertise. Assign examiners S&S and consumer compliance review in areas where there is overlap, such as lending and deposit areas. If helpful, prepare an Examination Scoping Worksheet and budget exam hours accordingly.

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10. Coordinate and oversee the review of association materials that might give an early indication of a need to change the scope (refer to this Handbook Section for a list of these materials). This review should include the following procedures:

- Review the association's current Thrift Financial Reports (TFR) and Management Information Systems (MIS) reports and determine if there have been significant changes in the level of capital, lending or investment activity, earnings, or nonperforming assets.
- Review the minutes of the board of directors' meetings. Focus attention on significant changes in the association's business activities (lending, investment, joint ventures, etc.). Assess the level of oversight performed by the directorate.
- Discuss with management any changes in key management, the directorate, or business activities that have occurred since the preceding examination. Also inquire as to any proposed changes or pending litigation that may affect earnings and capital.
- Determine through a review of correspondence, discussions with management, and other appropriate verification methods, if management corrected any problems related to the following areas:
  - Prior examination report comments and supervisory letters.
  - External auditor's exceptions.
  - Internal auditor's exceptions.
  - Any enforcement actions and directives.
- Determine if there are written policies governing key areas such as lending and investments. Evaluate the adequacy of new or revised written policies, procedures, and strategic plans. These guidelines should adequately address

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**Prepared By:** \_\_\_\_\_  
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**Docket #:** \_\_\_\_\_

# Examination Scheduling, Scoping, and Management Program

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WKP. REF.

safety and soundness (including internal controls), profitability, and compliance with laws and regulations.

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11. Make adjustments to the examination scope as necessary, but preferably as early as possible. Notify a supervisor if you anticipate significant changes in scope, staffing needs, duration, etc. Revise the risk assessment, as appropriate.

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12. Select exam procedures appropriate to the risk profile of the association.

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## EXAMINATION MANAGEMENT PROCEDURES

The EIC should perform the following procedures as soon as possible to ensure that the examination is properly managed.

1. Meet with the CEO or designee as soon as possible at the beginning of the examination. Refer to this Handbook Section for a list of recommended items to discuss. Discuss the administrative aspects of the examination. Notify the appropriate office when the examination begins.

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2. Discuss scope and assignments with assistants including estimated time for completion. Determine that assistants are aware of the specific activities included in the exam scope. Assist in establishing the scope for each of the assigned programs.

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3. As necessary, review with the examiners assigned lending and deposits the specific areas requiring review for interrelated S&S and compliance issues.

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# Examination Scheduling, Scoping, and Management Program

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WKP. REF.

4. If applicable, coordinate with the FDIC dedicated examiner to observe and participate in particular exam activities, and in the review and assessment of the risk of credits in the Shared National Credit Program.

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5. Ensure the timely receipt and dissemination of PERK materials requested from management. Discuss problems with the appropriate contact person and establish revised deadlines for receipt of materials, if necessary.

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6. Throughout the examination:

- Review on a regular basis the workflow, findings, and actual versus budgeted time.
  - Take appropriate steps to include on-the-job training. Consider your assistants' task records, if applicable.
  - Discuss all items of concern with the assistants to ensure that the OTS presents accurate information at the closing conference with the CEO.
  - Keep the supervisor and the CEO abreast of any developing significant issues.
  - Ensure that your assistants are preparing examination work in accordance with policies, including: work papers, interim reports, exception sheets, draft comments, report pages, time sheets, administrative reports, and transmittal file information. Refer to [Examination Handbook Section 070, Ratings: Developing, Assigning, and Presenting](#), for a discussion of report content.
- 

7. If you need additional verification, review, or analysis of any areas, complete or assign the completion of selected procedures from Levels I, II, and III for the particular area of review. (Refer to instructions for selecting Levels I, II, and III procedures in [Examination Handbook Section 010, Handbook and Program Use](#).)

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# Examination Scheduling, Scoping, and Management Program

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WKP. REF.

8. Ensure that the examination meets the Examination Objectives of this Handbook Section.
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## EXAMINATION CLOSING PROCEDURES

1. Schedule a closing conference and incorporate comments in the report. (For further instructions see [Examination Handbook Section 070, Ratings: Developing, Assigning, and Presenting](#).) Notify all attendants of the closing conference date and time, preferably with the use of an agenda.

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2. If appropriate, recommend any necessary administrative actions. Prepare a confidential memorandum if necessary.

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3. If deemed constructive, provide a copy of Thrift Bulletin (TB) 68a to the CEO and discuss the process for resolving differences with examiners, including the TB 68a appeal process.

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4. Complete the EDS/ROE. You should verify all totals in the examination report and other reports with a calculator or with the use of spreadsheet software. Refer to [Examination Handbook Sections 040, Examination Systems](#), and [070, Ratings: Developing, Assigning, and Presenting](#); and the ROE Instructions.

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5. Ensure the completion of the General File.

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# Examination Scheduling, Scoping, and Management Program

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WKP. REF.

6. Review work papers for completeness, proper indexing, date stamping etc. (The EIC may delegate this responsibility.) The EIC should have reviewed the work paper content and conclusions, and initialed all work papers, before finalization of the conclusions and comments.  

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7. Prepare, if appropriate, evaluations of assistants. Sign off on their task records. Recommend formal instruction and on-the-job experience that would further each of their careers. Discuss the evaluation with the individual and their supervisor, if applicable.  

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8. Complete a PERK summary schedule and summarize any other information useful to the planning, scoping, and control of future examination activities and include the information in the General File. Compare actual and budgeted exam hours.  

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9. Update the ECEF and, if applicable, create or update the Regulatory Profile with any significant data obtained from the examination. See [Examination Handbook Section 040, Examination Systems](#).  

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10. Transmit the completed report and return work papers and related files to the regional office in accordance with established procedures.  

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## EXAMINER'S SUMMARY, RECOMMENDATIONS, AND COMMENTS

**Exam Date:** \_\_\_\_\_  
**Prepared By:** \_\_\_\_\_  
**Reviewed By:** \_\_\_\_\_  
**Docket #:** \_\_\_\_\_



BASIC SCOPING MATRIX

Institution: Docket: Field Manager: EIC:  <b>Compliance Areas</b>	<b>Product Lines</b>										
	Savings Accounts	Transaction Accounts	Mortgage Loans (Including Construction)	Consumer Non-Mortgage Loans	Commercial Non-Mortgage Loans	Finance Leasing	Monetary Instrument Sales	Payment Systems Risk	Insurance Sales	Securities Sales	Branch Security & Notices
Equal Credit Opportunity – EH 1205			X	X	X	X					X
Fair Housing – EH 1210			X								X
Home Mortgage Disclosure – EH 1215			X								X
Fair Credit Reporting – EH 1300	X	X	X	X	X				X		
Truth-in-Lending – EH 1305			X	X							
OTS Mortgage Regulations – EH 1315			X								
Real Estate Settlement Procedures – EH 1320			X								
Homeowners Protection – EH 1323			X								
Consumer Leasing – EH 1325						X					
Electronic Funds Transfer – EH 1330	X	X									
Expedited Funds Availability – EH 1335		X									X
Flood – EH 1340			X								
Right to Financial Privacy – EH 1345	X	X	X	X	X	X	X	X	X	X	X
Fair Debt Collection – EH 1350			X	X							
Unfair or Deceptive Acts – EH 1355			X								
Homeownership Counseling – EH 1360			X								
Truth-in-Savings – EH 1365	X	X									
Electronic Banking – EH 1370	X	X	X	X	X	X	X	X	X	X	
Gramm-Leach-Bliley Privacy – EH 1375	X	X	X	X	X		X	X			
Insurance Consumer Protection – EH 1380				X	X	X			X		
Bank Secrecy Act – FFIEC BSA/AML	X	X	X	X	X		X	X	X	X	
Bank Protection Act – EH 1405											X
Economic Sanctions – FFIEC BSA/AML	X	X	X	X	X		X	X	X	X	
Interest on Deposits – EH 1420	X	X									
Advertising – EH 1425	X	X	X	X	X		X	X	X	X	X

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# Appendix B: Examination Scheduling, Scoping, and Management

## Section 060

### EXAMINATION SCOPE WORKSHEET

Association: \_\_\_\_\_ Docket No.: \_\_\_\_\_  
 Exam Type: \_\_\_\_\_ Start Date: \_\_\_\_\_  
 Review Period: \_\_\_\_\_  
 Examiner-in-Charge: \_\_\_\_\_  
 Compliance Examiner-in-Charge: \_\_\_\_\_

Scope Summary and areas of risk:

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Examination Procedures (*Required)	Incl. In scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No

#### Administration

Exam Scheduling, Scoping, Management (060)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

#### Capital

Risk-Focused Procedures (ND 02-12)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (ND 04-09)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Capital Stock and Ownership (110)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Capital Adequacy (120)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

#### Asset Quality

Risk-Focused Procedures (ND 02-12)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (ND 04-09)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Overview: Lending Ops/Portfolio Risk (201)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Appraisal (208)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Sampling (209)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Loans to One Borrower (211)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
One- to Four-Family RE Lending (212)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Construction Lending (213)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Other Commercial Lending (214)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Letters of Credit (215)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Floor Plan and Indirect Lending (216)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**APPENDIX B: EXAMINATION SCHEDULING, SCOPING,  
AND MANAGEMENT**

**SECTION 060**

Examination Procedures (*Required)	Incl. In scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Consumer Lending (217)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Credit Card Lending (218)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Leasing Activities (219)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Equity Investments (230)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Troubled Debt Restructurings (240)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Other Assets/Liabilities (250)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Owned and Other Repossessed Assets (251)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fixed Assets (252)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Classification of Assets (260)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Adequacy of Valuation Allowances (261)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Qualified Thrift Lender Test (270)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Margin Securities Regulation U (280)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Management**

Risk-Focused Procedures (ND 02-12)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (ND 04-09)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Oversight by the Board of Directors (310)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Management Assessment (330)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Internal Control (340)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Technology Risk Controls (341)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
External Audit (350)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Internal Audit (355)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fraud/Insider Abuse (360)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Enforcement Actions (370)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Transactions with Affiliates (380)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Earnings**

Risk-Focused Procedures (ND 02-12)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (ND 04-09)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Financial Records and Reports (410)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Operations Analysis (430)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Liquidity**

Risk-Focused Procedures (ND 02-12)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (ND 04-09)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Funds Management (510)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**APPENDIX B: EXAMINATION SCHEDULING, SCOPING,  
AND MANAGEMENT**

**SECTION 060**

Examination Procedures (*Required)	Incl. In scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Cash Flow and Liquidity Management (530)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Investment Securities (540)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Deposits/Borrowed Funds (560)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Reserve Requirements Reg D (561)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Government Securities Act (563)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Mortgage Banking – Overview (571)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Mortgage Banking – Profitability (572)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Mortgage Banking – Accounting (573)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Mortgage Banking – Production (574)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Mortgage Banking – Secondary Marketing (575)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Mortgage Banking – Servicing (576)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Payment Systems Risk (580)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Sensitivity to Market Risk**

Risk-Focused Procedures (ND 02-12)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (ND 04-09)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Interest Rate Risk Management (650)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Derivative Instruments and Hedging (660)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Other Activities**

Networking Arrangements (710)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Insurance (720)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Subordinate Organizations (730)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Development (740)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Compliance Management**

Tailored Procedures (ND 04-09)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Compliance Oversight Examination Program (1100)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Fair Lending/Nondiscrimination**

Fair Lending – Potential for Discriminatory Conduct (1201)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Nondiscrimination (1200)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fair Lending – other (1201)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Equal Credit Opportunity Act (1205)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**APPENDIX B: EXAMINATION SCHEDULING, SCOPING,  
AND MANAGEMENT**

**SECTION 060**

Examination Procedures (*Required)	Incl. In scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Fair Housing Act (1210)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Home Mortgage Disclosure Act (1215)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Equal Employment Opportunity (1410)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Americans with Disabilities Act	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Predatory Lending Issues	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Privacy**

Gramm-Leach-Bliley Act Privacy Provisions (1375)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fair Credit Reporting Act – privacy components (1300)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Right to Financial Privacy Act (1345)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Electronic Banking (1370)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Bank Secrecy Act (BSA), USA PATRIOT Act, Office of Foreign Assets Control (OFAC) Economic Sanctions**

Bank Secrecy Act (1400)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Bank Protection Act (1405)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
USA Patriot Act	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OFAC Economic Sanctions (1415)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Lending Laws and Regulations**

Fair Credit Reporting Act (1300)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Truth in Lending Act (1305)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Truth in Lending Act Restitution (1310)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OTS Mortgage Regulations (1315)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Settlement Procedures Act (1320)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Homeowners Protection Act (1323)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Consumer Leasing Act (1325)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Flood Disaster Protection Act (1340)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fair Debt Collection Practices Act (1350)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Unfair or Deceptive Acts (1355)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Homeownership Counseling Procedures (1360)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Electronic Banking – lending aspects (1370)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Advertising (1425)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**APPENDIX B: EXAMINATION SCHEDULING, SCOPING,  
AND MANAGEMENT**

**SECTION 060**

Examination Procedures (*Required)	Incl. In scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Federal Housing Administration Awareness Requirements	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Miscellaneous OTS Lending Regulations (late charges, prepayment penalties, due-on-sale or transfer clauses)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Soldiers and Sailors Relief Act	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Deposit Operations Laws and Regulations**

Fair Credit Reporting Act (1300)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Electronic Fund Transfer Act (1330)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Expedited Funds Availability Act (1335)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Check 21 (1336)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Truth in Savings Act (1365)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Electronic Banking (1370)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Insurance Consumer Protection (1380)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Bank Protection Act (1405)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Interest on Deposits (1420)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Advertising (1425)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Branch Closings (1430)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Branch Review Procedure	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Americans with Disabilities Act	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
FDIC Insurance of Accounts	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

# Appendix B: Examination Scheduling, Scoping and Management

## Section 060

### Estimated Time to Complete Exam

This Exam:

Estimated # of examiner weeks needed to complete exam with above scope.  
(For example: 3 examiners X 4 weeks = 12 examiner weeks)

\_\_\_\_\_

\_\_\_\_\_

Next Exam:

Estimated # of examiner weeks recommended to complete exam with above scope. (For example: 3 examiners X 4 weeks = 12 examiner weeks)

\_\_\_\_\_

\_\_\_\_\_

### Other Comments

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

### Scope for This Exam

Prepared by: \_\_\_\_\_

Date: \_\_\_\_\_

Approved by: \_\_\_\_\_

Date: \_\_\_\_\_

### Scope Recommendations for Next Exam

Prepared by: \_\_\_\_\_

Date: \_\_\_\_\_

After the exam has concluded, please:

- Include this form with your exam work papers.
- Send the completed scope worksheet to the caseload FM or ARD for posting on the ECEF.



EXAMINATION MANAGEMENT CHECKLIST

**Association:** \_\_\_\_\_ **Docket No.:** \_\_\_\_\_  
**Exam Type:** \_\_\_\_\_ **Start Date:** \_\_\_\_\_  
**Review Period:** \_\_\_\_\_  
**Examiner(s)-in-Charge**  
*Safety and Soundness:* \_\_\_\_\_  
*Compliance:* \_\_\_\_\_  
**Field Manager:** \_\_\_\_\_  
**Assistant Regional Director:** \_\_\_\_\_

**Prior to the Examination**

60+ days prior to exam	Initial When Completed
Contact ARD/FM/Compliance EIC/Office Examiner/Financial Analyst/CRA Specialist to discuss the following (contact association management for an update, if warranted):	
<ul style="list-style-type: none"> <li>• Developments at the association since the prior examination</li> </ul>	
<ul style="list-style-type: none"> <li>• Staffing and assignments</li> </ul>	
<ul style="list-style-type: none"> <li>• Potential need for specialists, including:</li> </ul>	
<ul style="list-style-type: none"> <li>– Capital Market Examiners</li> </ul>	
<ul style="list-style-type: none"> <li>– Appraiser</li> </ul>	
<ul style="list-style-type: none"> <li>– Accountant</li> </ul>	
<ul style="list-style-type: none"> <li>– TRC Examiner/ IT Examiner</li> </ul>	
<ul style="list-style-type: none"> <li>• Items to be reviewed /prepared prior to customization of the PERK</li> </ul>	
<ul style="list-style-type: none"> <li>• Travel issues</li> </ul>	
<ul style="list-style-type: none"> <li>• Telecommuting options</li> </ul>	
<ul style="list-style-type: none"> <li>• Involvement of other agencies, if applicable</li> </ul>	
<ul style="list-style-type: none"> <li>• Application Condition Monitoring Report, if applicable</li> </ul>	
Date of Meeting/Discussion:	

Appendix C: Examination Scheduling, Scoping,  
and Management

Section 060

<b>45 to 60 days prior to exam</b>	<b>Initial When Completed</b>
Review items for the PERK customization	
<ul style="list-style-type: none"> <li>• Prior ROEs/Work papers/Board Responses/EDS III</li> </ul>	
<ul style="list-style-type: none"> <li>• ECEF (TFR/UTPR/Association Profile/Enforcement Actions/Application History/etc.)</li> </ul>	
<ul style="list-style-type: none"> <li>• OTS Correspondence Files</li> </ul>	
<ul style="list-style-type: none"> <li>• Business Plans/Board of Directors Minutes/Audits/Any other information sent to OTS during review period</li> </ul>	
<ul style="list-style-type: none"> <li>• FDIC Website (Branches/Market Share/Financial Analysis)</li> </ul>	
<ul style="list-style-type: none"> <li>• Consumer Complaint Records/Reports</li> </ul>	
<ul style="list-style-type: none"> <li>• Information regarding litigation</li> </ul>	
<ul style="list-style-type: none"> <li>• CRA Wiz Reports</li> </ul>	
<ul style="list-style-type: none"> <li>• IRS/FinCEN Reports (SARs, CTRs, etc.)</li> </ul>	
Complete Examination Scope Worksheet with assistance from Compliance EIC and submit to ARD/FM for approval	

<b>No later than 45 days prior to exam</b>	<b>Initial When Completed</b>
Customize and send out PERK – Date sent:	
Ensure CRA PERK is issued, if applicable – Date sent:	
Contact CRA Specialist for preparation of fair lending summaries	
E-mail assisting examiners regarding assignments, travel issues, telecommuting options, and other logistical information	

<b>Week before exam</b>	<b>Initial When Completed</b>
Finalize Scope Worksheet	
Review ILDR and LARs and create loan samples	
Contact CEO regarding exam logistics (start time, dress code, etc.) and to schedule initial meeting	
E-mail assisting examiners with any additional information obtained since initial e-mail	
Complete and submit Exam Supply Checklist	
Send prior exam work papers, supplies, etc. to exam site	
Input exam start date online and download the appropriate ROE shell	
Review telecommute requests and forward to ARD/FM for approval	

**During the Examination**

<b>First week of exam</b>	<b>Initial When Completed</b>
Provide phone number(s) to appropriate personnel	
Conduct initial meeting with CEO/senior management	
Establish ongoing meetings with management of savings association	
Establish ongoing updates with ARD/FM/Compliance EIC/CRA Specialist	
Distribute exam shells to appropriate examiners	

<b>Ongoing</b>	<b>Initial When Completed</b>
Coordinate schedules/timeframes	
Establish exit meeting and other meeting dates	
Coordinate interactions with association staff (control flow of memos and findings sheets)	
Provide written summaries of findings and issues to association management for its review and response, if necessary	
Adjust scope to address issues/findings/concerns and reallocate resources if warranted; discuss with ARD/FM	
Review examiner work and work papers as completed	
Communicate with other agencies as warranted	
Review telecommute requests as submitted and forward to ARD/FM	
Monitor the following:	
<ul style="list-style-type: none"> <li>• Telecommuting issues</li> <li>• Travel issues</li> <li>• WebTA/Leave issues</li> </ul>	
Review work papers to ensure that conclusions and ratings are supported	
Prepare preliminary findings and conclusions	
Draft ROE comments and edit comments prepared by assisting examiners	
Discuss potential ratings with ARD/FM	

<b>Last week of exam</b>	<b>Initial When Completed</b>
Prepare for exit meeting	
Assemble OTS materials (work papers, reference materials, supplies) for shipment	
Return association materials	

**Post-examination**

	<b>Initial When Completed</b>
Complete ROE and upload Field Final	
<ul style="list-style-type: none"> <li>• Send ROE to FDIC for review, if applicable</li> </ul>	
Input completion date online	
Input EDS information online (ratings, supplemental, reportable data)	
Complete and discuss examiner assignment records with examiners and case FM/ ARD	
Complete work paper documentation	
<ul style="list-style-type: none"> <li>– Upload/review remaining electronic work papers</li> </ul>	
<ul style="list-style-type: none"> <li>– Ensure indexes of hard copy work papers identify all electronic work papers</li> </ul>	
<ul style="list-style-type: none"> <li>– Ensure electronic work papers include index of hard copy work papers</li> </ul>	
<ul style="list-style-type: none"> <li>– Lock electronic work papers</li> </ul>	
<ul style="list-style-type: none"> <li>– Send hard copy work papers to ARD/FM/record center</li> </ul>	
Discuss ongoing role of EIC with ARD/FM, including possible role in ongoing monitoring of the association	
Prepare memo and update Scope Worksheet for inclusion in Administration File that sets forth information for the next exam, i.e. areas that should be reviewed next field visit or exam, new activities or management that were not in place during the full review period; send an electronic copy of the updated Scope Worksheet to the FM/ARD for filing on the ECEF	
Complete the Comprehensive Exam Feedback Form	
Recommend postings to ECEF	
Discuss findings with FAU/Office Examiner	
<ul style="list-style-type: none"> <li>• Ensure Regulatory Profile is updated</li> </ul>	
Send original IT Overview Form and IT Update Form to regional office; file copies in Management work papers. (Not applicable if a separate IT exam is performed.)	
Trust Exams – complete Trust Regulatory Profile	
Ensure holding company ROE and rating are finalized, if applicable	
Prepare for the Board meeting, if applicable	
Prepare for ERC meeting, if applicable	
Close out any outstanding issues with other agencies, if applicable	
Update Application Condition Monitoring Report, if applicable	
Review response to ROE, if applicable	
File this form in the Administration work papers	




## Ratings: Developing, Assigning, and Presenting

This Handbook Section provides guidance in the following areas:

- Summarizing regulatory findings for the comprehensive Report of Examination (ROE) comments and conclusions.
- Assigning appropriate CAMELS and Compliance ratings.
- Meeting with association management and the board of directors to present the ROE findings.

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### LINKS

-  [Program](#)
-  [Appendix A](#)
-  [Appendix B](#)

### COMMENTS AND CONCLUSIONS

There are unique factors to consider when developing conclusions, comments, and ratings for each CAMELS component and Compliance area. Each comment should be accurate, complete and concise.

## Developing Report Comments

The following checklist will assist in developing individual CAMELS and Compliance comments for the ROE:

- Present the scope of the review.
- Clearly state conclusions.
- Clearly identify patterns, practices, trends, and their causes.
- Present comments in a meaningful order, discussing major strengths and weaknesses, with proper emphasis and tone accorded to individual topics. The severity of the problem will dictate its order of presentation. Consider how the problem affects the association's other activities and any mitigating circumstances.
- Identify substantive safety and soundness and compliance issues. See [Examination Handbook Section 040](#) for a discussion of the characteristics of a substantive violation.

- Include the deficient underlying practices when you note patterns of regulatory noncompliance.
- Support conclusions with appropriate analysis and prepare an effective summary that does not lose the reader in detail.
- Assess the effect of examination findings on future operations.
- Include a discussion of corrective action where necessary.
- Identify actions needed to correct weaknesses, outstanding deficiencies, or violations as appropriate.
- Support the comments with work papers and other retained documents. Include information that provides a clear understanding of the overall condition, adequacy of management practices, causes of major problems, and recommendations for remedial action.
- Disclose the rating.

The Compliance comment should:

- Assess and record any association-identified regulatory violations or program deficiencies and distinguish among them as follows:
  - Those the association corrected.
  - Those the association is in the process of correcting.
  - Those the association has not corrected.
- Assess regulatory compliance violations or program deficiencies identified by the examination, but not found by the association or its self-assessment or audit processes. Address only violations deemed substantive in the ROE.

For 1- and 2-rated savings associations, if there are no findings of deteriorating performance or materially inadequate controls in a particular CAMELS or Compliance section, you may eliminate the individual narrative page and summarize the conclusions on the Examination Conclusions and Comments page in the ROE. You must address the association's compliance program in the Examination Conclusions and Comments if you do not use the Management page. See the ROE Instructions for additional guidance.

### Primary Factors to Consider

Consider the following primary factors when developing your conclusions and ratings:

- Material items that relate to safety and soundness, and significant adverse findings for technology risks, or compliance, and the causes of those problems.
- An assessment of the compliance management program's performance.
- An assessment of the effectiveness of overall risk management.
- Regulatory violations and the reasons for any material patterns. A simple listing of violations is usually ineffective, particularly in the case of an isolated incident or error. While it is appropriate, in certain situations, to consider isolated violations, you should not bring them forward to the Examination Conclusions and Comments page unless they are significant.
- How your findings within each of the CAMELS and Compliance areas interrelate, affect the overall financial condition and safety and soundness of the association's operations, and reflect on the effectiveness of management.
- Material adverse findings outstanding from the prior examination and management's efforts to date to correct the problems.

### Formulating an Overall Conclusion

As you complete individual report comments and compile work papers, you should begin to formulate an impression of the association's overall condition.

The development of a substantive overall conclusion requires that you:

- Review major findings from the examination (including trends).
- Consider the association's operating environment (both internal and external factors).
- Consider the need for supervisory monitoring or enforcement action.
- Convert ultimate determinations into ratings.
- Communicate results effectively.
- Facilitate the corrective action process.
- State conclusions and the overall evaluation in the ROE.

There are both objective and subjective factors involved in a comprehensive analysis of the association's present and expected future condition. You must weigh the significance of criticisms, deficiencies, and exceptions that may offset strengths. This requires reviewing CAMELS comments, compliance management comments, and other findings for interrelationships. Whenever a practice or other factor materially affects safety and soundness or compliance performance, you must look at both the present and potential future consequences.

One goal of the regulatory process is to prevent problems from developing or escalating in the future. Therefore, early identification of risk or weaknesses in management practices is key. Support any projections with adequate facts and analyses.

When developing a conclusion about the association's future prospects, consider:

- Existing systems, policies, and procedures.
- The business plan.
- Corrective action.
- Projections for operating performance.
- Use of information technology.
- Management effectiveness and ability to effect corrective actions.
- Market and economic factors.

One goal of the regulatory process is to prevent problems from developing or escalating in the future.

## ASSIGNING RATINGS

After formulating the conclusions, you can begin the rating process. In a comprehensive examination, OTS rates a savings association in the following areas:

- CAMELS components and composite ratings – OTS uses the CAMELS rating system to evaluate a savings association's overall condition and performance by assessing six rating components. The six components are Capital Adequacy, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk. OTS then assigns each association a composite rating based on your assessment of its overall condition and level of supervisory concern.
- Compliance rating – OTS uses a Compliance Rating System that addresses general compliance with fair lending, consumer protection, and other public interest laws and regulations. This rating system is substantially equivalent to the FFIEC-approved interagency compliance rating system.



In order to assess management and the association's overall condition, you must adequately consider all areas and their interrelationships. This section briefly presents the main areas you must review in order to assign the six CAMELS component and composite ratings, and the Compliance rating. (See also the Appendices that follow this Section for detailed rating guidelines.)

You should follow the examination procedures within each of the chapters as required by the examination scope to develop the ratings.

OTS personnel use the ratings for a variety of purposes:

- To reflect trends for a particular association.
- To make comparisons with peers.
- To assess the condition of the industry.

The ratings help determine appropriate strategies including the following:

- Frequency and scope of off-site and on-site analysis.
- Enforcement actions.
- Meetings with association representatives.
- Analyzing applications (such as, merger, acquisitions, subordinated debt issuance), and notifications (such as, transactional website filings).

Because ratings determine a variety of critical decisions, a systematic and logical analysis is essential. While objective analysis and findings primarily determine ratings, there are some subjective factors, too.

## CAMELS Rating System

The Uniform Financial Institutions Rating System (UFIRS) is the definitive statement on safety and soundness ratings. (See [Appendix A](#).) Aggregate rating information enables the public and Congress to assess the condition of the savings and loan industry. Because the four banking regulatory agencies adopted the UFIRS, Congress and others can readily compare composite rating data for all types of insured savings associations.

This section expands on, or highlights certain parts of the policy statement as it applies to savings associations.

### *Composite Rating*

The composite rating is a qualitative assessment by the agency of the association's condition and the agency's overall level of supervisory concern.

Composite ratings reflect a careful evaluation of an institution's managerial, operational, financial, and compliance performance.

Composite ratings are based on a careful evaluation of an institution's managerial, operational, financial, and compliance performance. The six key components used to assess an institution's financial condition and operations are: capital adequacy, asset quality, management capability, earnings quantity and quality, the adequacy of liquidity, and sensitivity to market risk. The rating scale ranges from 1 to 5, with a rating of 1 indicating: the strongest performance and risk management practices relative to the institution's size, complexity, and risk profile; and the level of least supervisory concern. A 5 rating indicates: the most critically deficient level of performance; inadequate risk management practices relative to the institution's size, complexity, and risk profile; and the greatest supervisory concern.

Although the composite rating assigned to the association should normally have a close relationship to the individual CAMELS component ratings, you should not derive the composite rating merely by computing an arithmetic average of the component ratings. Such a simplistic, mechanical approach will not reflect the true condition of the savings association; nor will it indicate the appropriate supervisory actions.

The composite CAMELS rating, the CAMELS component ratings, and supporting documentation all play an important part in the regulatory process in support of any necessary enforcement action.

One of the principal objectives of the CAMELS rating process is to identify, through an overall assessment of the association as

reflected in the composite rating, those associations that pose a risk of failure and merit more than normal supervisory attention. Thus, you should give more weight to individual CAMELS criteria that more strongly affect the condition and viability of the association. The composite CAMELS rating, the CAMELS component ratings, and supporting documentation all play an important part in the regulatory process in support of any necessary enforcement action.

The Examination Conclusions and Comments page, the CAMELS comments, and the work papers should support the composite rating. In the ROE, disclose the composite CAMELS and compliance ratings, refer to the definition of the assigned ratings, and explain the correlation between the association's circumstances and the ratings.

OTS uses an association's composite rating as one of the factors to determine whether OTS should designate the association as being in "troubled condition." OTS designates in troubled condition any association that has a composite CAMELS rating of 4 or 5. OTS defines other qualifiers of troubled condition in 12 CFR § 563.555. These associations are subject to greater regulatory scrutiny and restrictions, such as requirements to receive prior approval before engaging in certain activities.

When you examine an association in troubled condition, you should consult the regulatory profile, supervisory correspondence, the previous examination, and any other pertinent information to determine the operating restrictions to which an association is subject. You must then analyze the association's operations and ensure that it complies with all restrictions. For further information regarding operating restrictions, refer to [Examination Handbook Section 370, Enforcement Actions](#).

The composite rating also supports OTS's differential regulation policy. The composite rating establishes both the OTS and the Federal Deposit Insurance Corporation (FDIC) fee assessment levels and determines the levels of supervisory oversight and restrictions. This policy provides tighter restrictions for thrifts with lower composite ratings and other factors, and is evident in the following guidance:

- [Examination Handbook Section 370, Enforcement Actions](#).
- RB 3b (Growth Restrictions).
- OTS assessment regulation at 12 CFR § 502.10.
- OTS audit regulation at 12 CFR § 562.4.
- OTS transactions with affiliates regulation at 12 CFR § 563.41.
- OTS capital regulation at 12 CFR § 565.4.
- OTS directors' regulation at 12 CFR §§ 563.550 through 563.590.
- FDIC risk-based deposit insurance assessment regulation at 12 CFR Part 327.

### *Component Ratings*

Generally, component ratings reflect examination findings and an examiner's assessment of an association's performance in the six key performance groups that are common to all associations. We highlight below, the UFIRS definition for each CAMELS component.

#### Capital Adequacy

Maintaining an adequate level of capital is a critical element for depository associations. While meeting regulatory capital requirements is a key factor in determining capital adequacy, the association's operations and risk position may warrant additional capital beyond the minimum regulatory requirements. You should determine whether capital is adequate in relation to the risk profile and operations of the association. In addition, you should evaluate capital levels in relation to future needs.

Maintaining an adequate level of capital is a critical element for depository associations.

Since maintaining a sufficient level of capital is critical for an association to maintain operations, you should appropriately weigh the importance of capital on the viability of the association when formulating the composite rating. You should also consider the association's dividend payout policy and practice. You should rate an association's capital adequacy considering all criteria cited in the UFIRS statement.

#### *PCA Levels*

In general, an association in any of the three lower-tier Prompt Corrective Action (PCA) categories warrants a 4 or 5 Capital component rating. A capital rating of 4 is appropriate if the association is undercapitalized or significantly undercapitalized but asset quality, earnings, or interest rate risk problems will not cause the association to become critically undercapitalized in the next 12 months. Also, a capital rating of 4 may be appropriate for an association that does not have sufficient capital based on its capital level compared with the risks present in its operations, even though the association may meet the minimum regulatory requirements.

An association warrants a 5 rating if it is "critically undercapitalized," or has significant asset quality problems, negative earning trends, or high interest rate risk exposure that will cause the association to become critically undercapitalized within the next 12 months.

See the Capital Chapter of this Handbook for more detailed instructions for reviewing capital adequacy.

#### Asset Quality

An accurate evaluation of an association's asset quality can be one of the most important products of the examination. The asset quality rating reflects the extent of credit risk associated with the loan and investment portfolios, real estate owned, other assets, and off-balance-sheet risks as well as the association's ability to manage those risks. The evaluation of an association's asset quality is dependent on the association's policies and procedures relating to loan underwriting and asset procurement, the proper monitoring and classification of assets, the nature of the risk inherent in the association's portfolios, and the adequacy of the association's valuation allowances.

When asset quality is in doubt because of excessive or inadequately controlled risk, the association's asset quality component rating should reflect this concern. In order to attain a 1 or 2 Asset Quality component rating, an association must fully control its credit risk. If an association has a high exposure to credit risk, it is not sufficient to demonstrate that the loans are profitable or that the association has not experienced significant losses in the near term. Management must demonstrate that it has identified credit risks, measured the potential exposure to loss, established systems to monitor such risk on an ongoing basis, and has taken adequate steps to limit and control those risks. Otherwise, a significant supervisory concern will exist relative to the association's asset quality.

#### Management

This rating reflects the capability of the board of directors and management, in their respective roles, to identify, measure, monitor, and control the risks of an institution's activities and to ensure a financial

institution's safe, sound, and efficient operation in compliance with applicable laws and regulations. Generally, directors need not be actively involved in day-to-day operations; however, they must provide clear guidance regarding acceptable risk exposure levels and ensure that they have established appropriate policies, procedures, and practices. Senior management is responsible for developing and implementing policies, procedures, and practices that translate the board's goals, objectives, and risk limits into prudent operating standards.

Depending on the nature and scope of an association's activities, management practices may need to address some or all of the following risks:

- Credit
- Market
- Operating or transaction
- Reputation
- Strategic
- Compliance
- Legal
- Liquidity
- Other risks.

The following practices demonstrate sound management:

- Active oversight by the board of directors and management.
- Competent personnel.
- Adequate policies, processes, and controls taking into consideration the size and sophistication of the association.
- Maintenance of an appropriate audit program and internal control environment.
- Effective risk monitoring and management information systems.

This rating should reflect the board's and management's ability as it applies to all aspects of banking operations as well as other financial service activities in which the association is involved.

Consistent with the UFIRS definition, your assessment and rating of the management component must reflect the board of directors and management's ability and effectiveness in managing all aspects of an association's operations and risks, including the compliance management function. The Management rating component should also include its approach to compliance, its demonstrated capacity to administer and implement a compliance program using SMAART components.

Assigning a compliance rating of 3 identifies a less than satisfactory compliance position. When the compliance rating is 3, the Management component cannot receive a rating any higher than 2. Compliance ratings lower than 3 should further constrain the potential rating of the Management component. Generally, the level of substantive violations, programmatic deficiencies and OTS supervisory attention associated with compliance ratings of 4 or 5 are inconsistent with management performance under the CAMELS system of anything higher than a 3 for Management, and may be sufficient alone, or in combination with other management shortcomings, to compel even lower ratings of Management.

Your assignment of the management rating must also consider the findings and conclusions for technology risk controls. The management rating should always reflect serious control deficiencies for technology risks.

### Earnings

You must determine whether earnings are sufficient for necessary capital formation. An association should have minimum earnings sufficient to absorb losses without impairing capital. Quality (stability) and composition (source) of earnings are important criteria. The thrift cannot rely on income that is nonrecurring, such as gains on the sale of portfolio loans, to maintain profitability. You should consider the extent to which extraordinary items, such as nonrecurring securities transactions and tax effects contribute to net income.

In some cases, associations are able to sustain volume and stable earnings from noninterest sources of income.

In some cases, associations are able to sustain volume and stable earnings from noninterest sources of income; for example, mortgage banking operations. In these associations (as well as all other associations), you should use professional judgment and analyze the stability and sufficiency of noninterest earnings. This includes the association's ability to react quickly to changing economic conditions, such as a decline in mortgage originations.

You should consider the adequacy of transfers to the general and specific valuation allowances; if the association needs more allowances, earnings will be negatively affected.

You should also consider the association's operating risks to determine if its earnings position is stable and sufficient. For example, if an association's interest rate risk management is inadequate, the association's earnings may be adversely affected by a change in market interest rates.

### Liquidity

OTS measures liquidity in relation to an association's level of liquid assets, its outside sources of funds, and the adequacy of its funds (or cash flow) management practices. Historically, most associations have held sufficient liquid assets. OTS-supervised associations generally rely upon liquidity available from secured lines of credit with the Federal Home Loan Banks (FHLBs). As long as the association's performance is sufficient to allow it to maintain a favorable credit standing with the FHLBs, and as long as the FHLBs also have adequate liquidity, associations can continue to confidently rely upon them for their liquidity needs.

### Sensitivity to Market Risk

The UFIRS bases the sensitivity to market risk component rating on two dimensions:

- The association's level of market risk.
- The quality of the association's practices for managing market risk.

Because few savings associations have significant exposure to foreign exchange risk or commodity or equity price risks, OTS generally assesses interest rate risk as the only form of market risk. You must assess both dimensions and combine those assessments into a component rating.

You must base your conclusions about an association's level of interest rate risk – the first dimension for determining the Sensitivity component rating – primarily on the interest rate sensitivity of the association's net portfolio value (NPV). You must pay primary attention to two specific measures of risk: Interest Rate Sensitivity Measure and Post-shock NPV Ratio. (See the TB 13a glossary for definitions.)

- Interest Rate Sensitivity Measure. This measure by itself, may not give cause for supervisory concern when the association has a strong capital position. Because an association's risk of failure is inextricably linked to capital and, hence, to its ability to absorb adverse economic shocks, an association with a high level of economic capital, that is, NPV, may be able safely to support a high sensitivity measure.
- Post-shock NPV Ratio. This ratio is a more comprehensive gauge of risk than the sensitivity measure because it incorporates estimates of the current economic value of an institution's portfolio, in addition to the reported capital level and interest rate risk sensitivity. There are three potential causes of a low, that is, risky, post-shock NPV ratio:
  - Low reported capital
  - Significant unrecognized depreciation in the value of the portfolio
  - High interest rate sensitivity.

Although the first two situations may cause supervisory concern and receive attention under the portions of the examination devoted to evaluating Capital Adequacy, Asset Quality, or Earnings, they do not necessarily represent an interest rate risk problem. Only when an association's low post-shock NPV is, in whole or in part, caused by high interest rate sensitivity is there suggestion of an interest rate risk problem.

Refer to TB 13a (Section IV, Table 1) for the guidelines to determine the level of interest rate risk. Use these risk levels as starting points in your ratings assessments; however, you have broad discretion to exercise judgment. TB 13a provides these risk levels as guidance; they are not mandatory.

OTS produces quarterly estimates of the sensitivity measure of the post-shock NPV ratio for each association that files TFR Schedule CMR. You can find these estimates in the Interest Rate Risk Exposure Report for the association.

In drawing conclusions about the quality of an association's risk management practices – the second dimension of the Sensitivity component rating – you must assess all significant facets of the association's risk management process.

Consider the following eight factors when assessing the quality of an association's risk management practices:

- Quality of oversight by the board and senior management.
- Prudence of board-approved IRR limits.
- Adherence to IRR limits.
- Quality of system for measuring NPV sensitivity.
- Quality of system for measuring earnings sensitivity.
- Integration of risk management with decision-making.
- Investments and derivatives including risk management policies and procedures.
- Association's size, complexity, and risk profile.

Although TB 13a (Table 2) provides guidelines on how to combine your assessment of these two dimensions into a component rating, you must exercise judgment in assigning ratings based on the facts you encounter at each association. TB 13a (Section IV) provides a nonexhaustive list of factors you might consider in applying the Sensitivity rating guidelines to a particular association.



*Thrift Performance Evaluation and CAMELS Rating Assignments*

The Uniform Thrift Performance Report (UTPR) provides percentile rankings for many measures of association performance as compared to peer performance. Use the Risk Monitoring System (RMS)

The mere fact that an association meets its minimum regulatory capital or other regulatory requirement does not guarantee that its condition is viable.

Query Builder to find the CAMELS composite ratings of other associations with similar key ratios. These tools are useful in comparing an association's performance with that of its peers to assign ratings that are consistent with

associations having similar ratios. However, since the composite CAMELS rating is an indicator of the overall health and viability of an association, it is important that you rate associations on their absolute performance as well as against regional or state peer performance. Associations in some states or regions may perform better than peer averages or medians, but perform poorly in absolute terms or when compared with peer averages or medians of other regions. Peer performance in such cases would not necessarily reflect associations that were being operated in a safe and sound manner. Rather, those averages could reflect substandard performance. The CAMELS ratings should accurately reflect the condition of an association, regardless of local or regional peer performance.

You cannot measure an association's performance solely in numbers. The mere fact that an association meets its minimum regulatory capital or other regulatory requirement does not guarantee that its condition is viable. Therefore, you must use professional judgment and consider both qualitative and quantitative criteria when analyzing an association's performance, taking into account:

- Quality of management and the board of directors.
- Quality and composition of the asset portfolio.
- Risks inherent in the business activities, including technology risks, and quality of risk management practices.
- Financial performance.

Further, since financial numbers are lagging indicators of an association's condition, you must also conduct a qualitative analysis of current and projected operations when assigning CAMELS ratings. You should weigh the analysis of quantitative and qualitative data to determine the rating for each CAMELS component.

## Compliance Rating System

OTS adopted a Compliance Rating System substantially equivalent to the FFIEC-approved interagency compliance rating system. The FFIEC consumer compliance rating system states that a consumer compliance rating evaluates and weighs the following:

- The nature and extent of present compliance with consumer protection and civil rights statutes and regulations.
- The commitment of management to compliance and its ability and willingness to take the necessary steps to assure compliance.
- The adequacy of operating systems, including internal procedures, controls, and audit activities designed to ensure compliance on a routine and consistent basis.

The primary purpose of the Compliance Rating System is to help identify those associations whose compliance with civil rights, consumer protection and other public interest statutes and regulations, displays weaknesses requiring special supervisory attention and is cause for more than a normal degree of supervisory concern.

### *Assigning the Compliance Rating*

In assigning a Compliance Rating, you must identify and evaluate all factors relevant to ensuring compliance with civil rights, consumer protection and other public interest statutes and regulations.

In general, these factors include:

- Implementation of a formal written compliance management program reliably covering OTS's SMAART components suitable to the size and operational complexity of the association.
- The commitment of the board and management, as evidenced by its ability and willingness to maintain compliance.
- Internal self-assessments and compliance reviews.
- Competency of management, as evidenced by the adequacy of operating systems, including internal procedures and controls designed to ensure compliance.
- Appropriate compliance training programs.
- The nature and extent of violations (including repeat violations) and deficiencies in actual compliance performance as a measure of the effectiveness of management's efforts.

Other factors unique to specific situations will require attention if you determine they significantly affect the overall effectiveness of an association's compliance efforts.

The Compliance Rating System is a scale of 1 through 5, in increasing order of supervisory concern. A rating of 1 indicates excellence, while a rating of 5 represents the lowest, most critically deficient level of performance and the highest level of

The Compliance Rating System is a scale of 1 through 5, in increasing order of supervisory concern.

supervisory concern. The Compliance Rating System is a single-value rating system. The single rating value assigned reflects overall compliance performance and you must substantiate the rating by the contents of the ROE and the examination work papers. Characteristics of the five Compliance Ratings available to the examiner will conform to the rating descriptions in [Appendix B](#). However, as these descriptions are a composite, not all characteristics will be present at every institution. You must apply this guidance to capture an accurate overall evaluation of the association's compliance management performance for the examination period, keeping in mind the policy to encourage self-identifying and self-correcting controls.

See [Appendix B](#) for a detailed description of the characteristics of the five Compliance Ratings.

### Consistency in Rating Assignments

It is essential that OTS apply ratings on a nationally consistent basis. Inconsistencies in assigning Compliance and CAMELS component or composite ratings may result in confusion and degrade the integrity of the supervisory process. With consistently applied ratings, OTS can compare the condition of the association between the previous examination and the most recent examination. Furthermore, and particularly with CAMELS ratings, you can compare associations on an intraregional and a national basis using RMS Query Builder reports sorted by key ratios. To ensure consistency in the rating process, you must have a thorough understanding of the criteria to assign the different Compliance and CAMELS component and composite ratings.

### Maintaining and Updating the Ratings

It is essential that regional offices monitor new developments for each association and update the ratings, as needed, so that the rating is always a current indicator of the association's condition. (Refer to [Examination Program 070](#) for off-site ratings procedures.) Maintaining these ratings requires periodic monitoring with an emphasis on the criteria supporting the CAMELS ratings for the association. For this reason, it is imperative that you document the significant points supporting the CAMELS rating.

Deterioration or significant changes in the association's operations or condition, or noncompliance with laws and regulations, may indicate a need for some special supervisory attention.

Deterioration or significant changes in the association's operations or condition, or noncompliance with laws and regulations, may indicate a need for enhanced supervisory attention. Supervisory attention may include a telephone inquiry or written request for additional information, a limited examination, or a regular examination. Any changes in the criteria that support the current ratings or any new developments may require a change in the CAMELS ratings and the supervisory treatment needed.

Since ratings affect the association's assessment and supervisory treatment, OTS must keep them current. Analyze and adequately document any updates to the ratings. The rating OTS reports to an association must always be the most recent rating based on all sources of information.

### *Documentation and Support*

Given the importance of the ratings, it is critical to clearly show and support how you determined these ratings. Include this documentation in the work papers. Discuss adverse findings in the individual sections of the ROE. Summarize overall findings and conclusions in the Examination Conclusions and Comments page of the ROE. For CAMELS ratings in particular, you should review ROE ratios, UTPR schedules, and customized RMS reports and use them to concisely document and support the analysis. You may also find these reports useful in assimilating and reviewing work paper conclusions and organizing your thoughts before drafting the ROE.

### *Disclosure of Ratings*

OTS discloses composite and component ratings to each association's management and board of directors. Disclosure of the CAMELS component ratings encourages a more complete and open discussion of examination findings and recommendations between examiners and association management. Further, disclosure of the CAMELS component and Compliance ratings in addition to the composite rating provides management with a better understanding of how OTS derives the composite rating. Disclosure also enables management to better address any weaknesses in specific areas before OTS finds it necessary to downgrade the association's overall composite rating.

Obtain sufficient concurrence from regional management, so that the ratings you disclose are final, or subject to revisions only in rare instances. If the ratings are subject to further review, let association management know that the ratings are not final.

You should disclose the elements considered in assigning each component rating and those considered in assigning the overall rating. You should indicate that a careful evaluation of the association's managerial, operational and financial performance and their compliance with laws and regulations determines the composite rating.

You must disclose the assigned composite rating in accordance with OTS's ROE instructions. Add the component rating to each ROE core component page. The Examination Conclusions and Comments page should provide a concise narrative statement of the major findings of the examination. In addition, the Examination Conclusions and Comments page should clearly state how the examination findings within each of the CAMELS and Compliance areas interrelate and affect the overall financial condition and safety and soundness of the association's operations.

### *Supervisory Letter*

When the regional office changes the CAMELS composite rating or the Compliance rating off-site, they send a supervisory letter to the board of directors to notify them of the change. A change in rating may result from changes in the association's operating strategies or conditions. An on-site review may be appropriate when conditions warrant a downgrade in rating. When the CAMELS composite rating changes, we advise evaluating the need to change all six CAMELS component ratings. Include in the supervisory letter a prohibition against outside disclosure and explain why the rating changed.

## MEETINGS WITH MANAGEMENT AND THE BOARD OF DIRECTORS

You must disclose CAMELS composite and component ratings and the Compliance rating at exit conferences with senior management and, when appropriate, the board of directors. You should obtain sufficient concurrence with the ratings from regional management, so that the component ratings disclosed are final, or subject to revisions only in rare instances. If the ratings are subject to further review, you should disclose to management and the board that the ratings are not final. Each region has office procedures to implement this policy.

### Management Discussions

During the discussion with management, you should discuss the criteria you considered in assigning each rating as well as the overall composite rating and the compliance rating. You should indicate that you based the composite rating on a careful evaluation of the association's managerial, operational and financial performance, and compliance with laws and regulations. You should clarify that you did not base the composite rating on an arithmetic average of the components, but on a qualitative analysis of the criteria comprising each component, the interrelationship between components, and, more importantly, the overall level of supervisory concern.

The quality of management is the single most important element in the successful operation of an association, and is usually the factor that is most indicative of how well the association identifies, measures, monitors, and controls risk. For this reason, you should take sufficient time to explain to senior management and, when appropriate, to the board of directors, the criteria you considered in assigning the management component rating, and the meaning of the rating. Your written comments in support of the management rating should include an assessment of the effectiveness of existing processes to identify, measure, monitor, and control risk. Finally, you should remind management that the ratings disclosed in the examination report remain subject to the confidentiality rules imposed by 12 CFR Part 510 of the OTS Regulations. This includes the verbal disclosures made at the conclusion of the examination.

The quality of management is the single most important element in the successful operation of an association.

### Meetings with the Board of Directors

In addition to meeting with management, OTS encourages you to meet with the boards of directors. Meetings between regulatory staff and the board of directors – the individuals ultimately responsible for a savings association's affairs – serve a variety of functions. They provide opportunity for interaction, and they facilitate long-term communication, especially important when the regulatory process reveals significant adverse information. Meetings help keep directors and regulators mutually informed by providing them an opportunity to discuss any of the following items:

- The examination process and findings.

- The association, its functions, and strategic plans and goals.
- The general financial environment.
- Industry-related concerns.

Meetings give regulators an opportunity to obtain commitments from the board for corrective action.

## Types of Meetings

There are two primary types of meetings between regulators and the board: *regular* – those relating to examinations; and *special* – not primarily for presenting examination findings. However, a meeting can serve multiple purposes. For example, a regular meeting can serve to acquaint regulators with the board, enhance communication, and present findings.

### *Regular Meetings*

A regular meeting can result from a regular or limited examination. Generally held at the conclusion of the examination, its primary purpose is to discuss findings and agree on corrective action. These meetings can also enhance the directors' understanding of the regulatory process, establish a rapport, and build lines of communication with regulators.

You should consider attending a regularly scheduled board meeting that occurs during an examination. The purpose is not necessarily to discuss findings although it may be an opportunity to discuss scope and preliminary findings. The main objective, however, is to observe the board in action and establish a rapport.

You should hold a meeting if you note adverse trends, increased risk profile, or other matters that need the board's attention. If no such issues exist, you may honor any request from management to forgo a meeting with the board. You must meet with the board of directors if the association has:

- A CAMELS composite or Compliance rating of 4 or 5.
- A CAMELS composite or Compliance rating of 3 if the rating represents a downgrade from the previous examination.
- A Holding Company rating of Unsatisfactory.

Generally, you should meet with the boards of all 3-rated associations. However, you may, with the concurrence of the field manager, determine it is not necessary to meet if the 3 rating is not a downgrade from a prior examination.

Sometimes you might schedule a meeting with the board of an association that does not have an adverse rating. This is appropriate when you note adverse trends, increased risk profile, or other matters

that you need to bring to the board's attention. If no issues exist, you should honor any request from management to forgo a meeting.

If an association's assets exceed \$1 billion, you should schedule a meeting with the board regardless of adverse trends. The field manager must concur with any decision to forgo a meeting.

While you normally meet after the examination, you could arrange a regular meeting during the last week. This is appropriate if you have already discussed the examination results with management. Your meeting can also coincide with the board's next regularly scheduled meeting. You can mutually agree on another time to meet as long as that date is within 60 days of completing the examination. Also when scheduling, consider whether directors would benefit from receiving a copy of the ROE before the meeting.

### *Participation*

When meeting with the board, you should meet with the entire board to ensure all directors are aware of regulatory findings and commitments to correct deficiencies. If all directors cannot attend, you can meet with a group, such as the audit, examination, or executive committee if:

- Outside directors are present.
- There are no material or adverse findings.
- The circumstances do not require a full board.

Honorary directors can participate in meeting discussions, but may not vote. Any person or organization connected with the association, auditor, or holding company representative can attend the meeting upon board resolution. However, you can excuse such people if appropriate. As a rule, state supervisory authorities should attend meetings with the boards of state-chartered institutions.

### *Special Meetings*

Reasons to schedule a special meeting include the following:

- To effect a supervisory action, such as a supervisory agreement or cease and desist order.
- To gather information in order to act on a proposal, application, or request by the association.
- To discuss an association's progress toward corrective action.
- To become acquainted following a change in directorate or a change in regulatory staff.
- To comply with directorate's request to meet.

### Meeting Preparation, Presentation, and Documentation

Schedule a mutually acceptable, convenient date and time to hold the meeting. Prepare yourself thoroughly when meeting with the directorate. Conduct yourself professionally and prepare sufficient documentation to ensure appropriate follow-up. A successful meeting will include all of the following steps:

- **Preparation**

- Ensure that the scheduling and selection of attendees satisfies the meeting's goal.
- Choose attendees and determine their responsibilities.
- Select a chairperson.
- Determine time and location.
- Develop an agenda.
- Notify participants of the meeting and its purpose.
- Meet with regulatory staff participants to discuss the agenda and other related issues.
- Prepare and organize supporting data, including comparative figures and ratios that indicate trends and graphs to illustrate significant points or trends.
- Prepare any handouts or overheads for presentation.

- **Presentation**

- Conduct the meeting in a professional, objective fashion.
- Present the agenda and follow it within reason.
- Establish good communication and maintain creditability.
- Encourage directors' involvement and solicit questions.
- Answer questions accurately. When unable to do so, tell the board you will find an answer. You may need to refer inquiries to the OTS regional or Washington office.
- Obtain commitment from board to correct deficiencies, if appropriate.



- **Documentation**

- Evaluate and document results of the meeting.
- Prepare a memorandum to record results, date, time, location, and participant's names and titles.
- Describe the items discussed, the board's reactions, and any commitments for corrective action.
- If the board promises corrective action, send the memorandum to them for concurrence.
- At the conclusion of any meeting conducted by the board (rather than the regulators), you should ask for a copy of the minutes and review them for accuracy.
- Keep a copy of the post-meeting memorandum and agenda in the appropriate supervisory file.
- Amend the association's regulatory profile to reflect any changes or future commitments as a result of the meeting. [See Examination Handbook Section 040.](#)

## REFERENCES

### Code of Federal Regulations (12 CFR)

#### *OTS Regulations*

- §502.10 Assessments
- §562.4 Audit of Savings Associations and Holding Companies
- §563.41 Loans and Other Transactions With Affiliates
- §563.550 Additions of Directors and Employment of Senior Executive Officers
- §565.4 Capital Measures and Capital Category Definitions

#### *FDIC Regulations*

- Part 327 Assessments

## Office of Thrift Supervision Bulletins

RB 3b Policy Statement on Growth for Insured Institutions

RB 18 General Enforcement Policy Series

TB 13a Management of Interest Rate Risk, Investment Securities, and Derivative Activities

## Other References

OTS Report of Examination Instructions

FFIEC Press Release, Uniform Financial Institutions Rating System, December 19, 1996

OTS Transmittal 166: Regulatory Citations to UFIRS

# Ratings: Developing, Assigning, and Presenting Program

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## EXAMINATION OBJECTIVES

To formulate conclusions regarding the risks, condition, trends, management practices, and future prospects of the savings association.

To formulate conclusions on the safety and soundness and regulatory compliance of the thrift and propose supervisory action, if needed.

To evaluate the performance of the compliance management program and evaluate any self-assessment reviews.

To effectively communicate conclusions and recommendations, both orally and in writing, in the Report of Examination according to the ROE Instructions and plain language principles.

To consider all significant financial, operational, and compliance performance measures for a savings association and assign CAMELS and Compliance ratings that accurately reflect the association's condition and viability.

To clearly support the CAMELS and Compliance ratings in the examination report and enable OTS to initiate corrective action with the association's directors and management.

To provide the association's management and the board of directors with CAMELS and Compliance ratings that signifies the OTS's assessment of the association's overall condition.

To record management's response to examination findings, conclusions, and proposed corrective action.

## EXAMINATION PROCEDURES

WKP. REF.

1. Review analyses, comments, exceptions, and conclusions in the work papers for each CAMELS and Compliance area, and perform the following:
  - Resolve any contradictory conclusions. Support all conclusions with facts obtained during the examination.
  - Determine the significance of the findings related to safety and soundness and overall regulatory compliance.
  - Discuss findings with appropriate institution personnel and verify conclusions

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as appropriate.

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2. Review the draft CAMELS and Compliance comments. Review assisting examiners' comments on management's self-assessment efforts and record of self-correcting compliance deficiencies. Talk with assisting examiners about their overall observations and findings applicable to the comments and determine whether conclusions are reasonable. Consider the interrelationships between findings noted for each CAMELS component and Compliance. If necessary, make adjustments to ensure that comments are comprehensive and to eliminate any duplication. If the EIC is aware of other criteria that are not known to assisting personnel, the EIC should determine if these criteria are relevant and whether or not to include the comments.

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3. Revise CAMELS and Compliance comments so that they fairly represent examination results according to ROE instructions. Ensure conclusions are well supported in work papers and comments include any significant items noted in work papers. The tone and content of each comment should be concise and appropriate, as outlined in the Handbook.

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4. Review the proposed corrective actions related to any violation or exception to ensure it is appropriate.

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5. Review the preliminary CAMELS component and Compliance ratings and meet with assisting examiners. Follow definitions and instructions pertinent to the rating system to ensure national consistency. Discuss the recommendations with assistant examiners to ensure the accuracy of their interpretations. Ensure that assistant examiners provided well-supported conclusions and opinions. Ensure that assistant examiners consistently applied the standard criteria set forth in this Handbook Section for determining and weighing the CAMELS and Compliance criteria and assigning the ratings.

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6. If necessary, adjust the CAMELS component and Compliance ratings so that they accurately and objectively present the association's performance in each area. Document the basis for each rating. Include the ROE ratios as well as any other pertinent ratios. Also include the most significant points supporting each rating. Review CAMELS comments again to ensure that they are consistent with the component ratings assigned.

Consider the impact of findings for compliance management performance and technology risk controls in rating the Management component.

- 
7. Make an overall assessment of the association and its future prospects in terms of risk, including technology risk, and adequacy of management and its system for risk and compliance management.

- 
8. Prepare the Examination Conclusions and Comments page. Refer to the ROE Instructions for a list of elements you should include on this page. Ensure the report is written in plain language.

- 
9. Determine the CAMELS composite rating and Compliance rating by weighing the importance of various criteria used to develop conclusions. To ensure national consistency, you should follow the rating instructions in the UFIRS Statement following this Handbook Section. Clearly support the composite rating with the facts and comments within the ROE.

- 
10. Review the Examination Conclusions and Comments page to ensure the tone and content supports the assigned composite rating. Finalize the CAMELS and Compliance ratings and comments after a thorough review. Ensure that the assistant examiner correctly completed the EDS/ROE ratings section, including the Technology Risk Controls (TRC) flag.
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11. Discuss findings with management, typically the CEO. We recommend that you use an agenda. Discuss at least the following topics:

- The purpose of the meeting.
  - All items that you might include in the examination report.
  - Overall conclusions regarding the institution.
  - Management's corrective action responses.
  - Composite and component ratings.
- 

12. After the meeting, correct any items in the ROE that are inaccurate, misleading, or misinterpreted.

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13. The Matters Requiring Board Attention page should include corrective actions, if appropriate. These include specific recommendations to correct deficiencies and violations listed in the report. Obtain a firm commitment for improvement of corrective action.

You may also include on this page recommendations for: supervisory agreements, consent agreements, cease-and-desist orders, receiverships, conservatorships, civil money penalties, compliance plans pursuant to 12 CFR Part 570, Appendix A and Appendix B, and criminal referrals to appropriate agencies. For suspected violations of criminal statutes, refer to [Examination Handbook Section 360, Fraud/Insider Abuse](#).

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14. Provide any information to the regional office that will be useful for revising the Regulatory Profile.

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15. Prepare the ROE cover page letter, if necessary, in accordance with regional office policy.
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16. Prepare to meet with the board of directors regarding findings.
- 

17. Ensure that your review meets the Objectives of this Handbook Section.
- 

## Off-Site Ratings

*Supervisory managers, analysts, or other staff should complete the following procedures as applicable when analyzing and updating CAMELS and Compliance ratings off-site.*

*Note: You should use the Type 46 Limited Examination Report to make any off-site rating updates.*

1. Review the most recent examination report and the Regulatory Profile to identify areas of concern.
- 

2. Review the association's compliance management program and the reports made as a result of the association's self-assessment process.
- 

3. Analyze reported financial information to determine current trends and any new areas of concern, with an emphasis on the period since the last examination.
- 

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4. Review any applications and notifications the association submitted since the last rating to determine whether there are any material changes in the structure or business plan.
- 

5. Review correspondence between the association and OTS to learn the status of significant issues arising since the most recent examination. Verify, to the extent possible, through a review of the financial statements and other reports that the association is correcting any problem areas.
- 

6. Review the most recent external audit report, the certified public accountant's management letter addressing internal control issues, and the association's response to that letter to determine if management corrected all reported internal control deficiencies.
- 

7. If necessary, contact the association to verify specific facts or address concerns.
- 

8. Identify any changes in the association's condition and operating practices. Determine if a change in a CAMELS component or composite rating, or Compliance rating, more appropriately reflects the condition of the association.
- 

9. Determine the need for and recommend, if necessary, a regular examination or a limited on-site examination of areas that you cannot adequately analyze off-site.
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10. Recommend any change in the CAMELS component or composite ratings, or Compliance rating, to the supervisory manager or other appropriate manager in the regional office. Support any recommendation for change with a narrative memorandum and documented analysis explaining and supporting the reasons for the change.
- 

11. If the regional office approves a change in a composite or component CAMELS rating, or Compliance rating, prepare a supervisory letter or memorandum to the association's board of directors to inform them of the change in the rating. The memo should explain the reasons for the change and any resulting consequences. The memorandum should also contain a definition of the new rating assigned and standard language prohibiting disclosure of the rating.
- 

12. Enter the new rating(s) in the EDS ratings section and make certain they are correct.
- 

13. Update the Regulatory Profile with any other appropriate information.
- 

## EXAMINER'S SUMMARY, RECOMMENDATIONS, AND COMMENTS

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FFIEC Press Release, December 19, 1996 [61 FR 67021]

## UNIFORM FINANCIAL INSTITUTIONS<sup>1</sup> RATING SYSTEM

### Introduction

The Uniform Financial Institutions Rating System (UFIRS) was adopted by the Federal Financial Institutions Examination Council (FFIEC) on November 13, 1979. Over the years, the UFIRS has proven to be an effective internal supervisory tool for evaluating the soundness of financial institutions on a uniform basis and for identifying those institutions requiring special attention or concern. A number of changes, however, have occurred in the banking industry and in the Federal supervisory agencies' policies and procedures which have prompted a review and revision of the 1979 rating system. The revisions to UFIRS in 1997 included the addition of a sixth component addressing sensitivity to market risks, the explicit reference to the quality of risk management processes in the management component, and the identification of risk elements within the composite and component rating descriptions.

The revisions to UFIRS were not intended to add to the regulatory burden of institutions or require additional policies or processes. The revisions are intended to promote and complement efficient examination processes. The revisions have been made to update the rating system, while retaining the basic framework of the original rating system.

The UFIRS takes into consideration certain financial, managerial, and compliance factors that are common to all institutions. Under this system, the supervisory agencies endeavor to ensure that all financial institutions are evaluated in a comprehensive and uniform manner, and that supervisory attention is appropriately focused on the financial institutions exhibiting financial and operational weaknesses or adverse trends.

The UFIRS also serves as a useful vehicle for identifying problem or deteriorating financial institutions, as well as for categorizing institutions with deficiencies in particular component areas. Further, the rating system assists Congress in following safety and soundness trends and in assessing the aggregate strength and soundness of the financial industry. As such, the UFIRS assists the agencies in fulfilling their collective mission of maintaining stability and public confidence in the nation's financial system.

### Overview

Under the UFIRS, each financial institution is assigned a composite rating based on an evaluation and rating of six essential components of an institution's financial condition and operations. These

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<sup>1</sup> For purposes of this rating system, the term "financial institution" refers to those insured depository institutions whose primary Federal supervisory agency is represented on the Federal Financial Institutions Examination Council (FFIEC). The agencies comprising the FFIEC are the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision. The term "financial institution" includes Federally supervised commercial banks, savings and loan associations, mutual savings banks, and credit unions.

component factors address the adequacy of capital, the quality of assets, the capability of management, the quality and level of earnings, the adequacy of liquidity, and the sensitivity to market risk. Evaluations of the components take into consideration the institution's size and sophistication, the nature and complexity of its activities, and its risk profile.

Composite and component ratings are assigned based on a 1 to 5 numerical scale. A 1 indicates the highest rating, strongest performance and risk management practices, and least degree of supervisory concern, while a 5 indicates the lowest rating, weakest performance, inadequate risk management practices and, therefore, the highest degree of supervisory concern.

The composite rating generally bears a close relationship to the component ratings assigned. However, the composite rating is not derived by computing an arithmetic average of the component ratings. Each component rating is based on a qualitative analysis of the factors comprising that component and its interrelationship with the other components. When assigning a composite rating, some components may be given more weight than others depending on the situation at the institution. In general, assignment of a composite rating may incorporate any factor that bears significantly on the overall condition and soundness of the financial institution. Assigned composite and component ratings are disclosed to the institution's board of directors and senior management.

The ability of management to respond to changing circumstances and to address the risks that may arise from changing business conditions, or the initiation of new activities or products, is an important factor in evaluating a financial institution's overall risk profile and the level of supervisory attention warranted. For this reason, the management component is given special consideration when assigning a composite rating.

The ability of management to identify, measure, monitor, and control the risks of its operations is also taken into account when assigning each component rating. It is recognized, however, that appropriate management practices vary considerably among financial institutions, depending on their size, complexity, and risk profile. For less complex institutions engaged solely in traditional banking activities and whose directors and senior managers, in their respective roles, are actively involved in the oversight and management of day-to-day operations, relatively basic management systems and controls may be adequate. At more complex institutions, on the other hand, detailed and formal management systems and controls are needed to address their broader range of financial activities and to provide senior managers and directors, in their respective roles, with the information they need to monitor and direct day-to-day activities. All institutions are expected to properly manage their risks. For less complex institutions engaging in less sophisticated risk taking activities, detailed or highly formalized management systems and controls are not required to receive strong or satisfactory component or composite ratings.

Foreign Branch and specialty examination findings and the ratings assigned to those areas are taken into consideration, as appropriate, when assigning component and composite ratings under UFIRS. The specialty examination areas include: Compliance, Community Reinvestment, Government Security Dealers, Information Systems, Municipal Security Dealers, Transfer Agent, and Trust.

The following two sections contain the composite rating definitions, and the descriptions and definitions for the six component ratings.

## COMPOSITE RATINGS

Composite ratings are based on a careful evaluation of an institution's managerial, operational, financial, and compliance performance. The six key components used to assess an institution's financial condition and operations are: capital adequacy, asset quality, management capability, earnings quantity and quality, the adequacy of liquidity, and sensitivity to market risk. The rating scale ranges from 1 to 5, with a rating of 1 indicating: the strongest performance and risk management practices relative to the institution's size, complexity, and risk profile; and the level of least supervisory concern. A 5 rating indicates: the most critically deficient level of performance; inadequate risk management practices relative to the institution's size, complexity, and risk profile; and the greatest supervisory concern. The composite ratings are defined as follows:

### Composite 1

Financial institutions in this group are sound in every respect and generally have components rated 1 or 2. Any weaknesses are minor and can be handled in a routine manner by the board of directors and management. These financial institutions are the most capable of withstanding the vagaries of business conditions and are resistant to outside influences such as economic instability in their trade area. These financial institutions are in substantial compliance with laws and regulations. As a result, these financial institutions exhibit the strongest performance and risk management practices relative to the institution's size, complexity, and risk profile, and give no cause for supervisory concern.

### Composite 2

Financial institutions in this group are fundamentally sound. For a financial institution to receive this rating, generally no component rating should be more severe than 3. Only moderate weaknesses are present and are well within the board of directors' and management's capabilities and willingness to correct. These financial institutions are stable and are capable of withstanding business fluctuations. These financial institutions are in substantial compliance with laws and regulations. Overall risk management practices are satisfactory relative to the institution's size, complexity, and risk profile. There are no material supervisory concerns and, as a result, the supervisory response is informal and limited.

### Composite 3

Financial institutions in this group exhibit some degree of supervisory concern in one or more of the component areas. These financial institutions exhibit a combination of weaknesses that may range from moderate to severe; however, the magnitude of the deficiencies generally will not cause a component to be rated more severely than 4. Management may lack the ability or willingness to effectively address weaknesses within appropriate time frames. Financial institutions in this group generally are less capable of withstanding business fluctuations and are more vulnerable to outside influences than those institutions rated a composite 1 or 2. Additionally, these financial institutions

may be in significant noncompliance with laws and regulations. Risk management practices may be less than satisfactory relative to the institution's size, complexity, and risk profile. These financial institutions require more than normal supervision, which may include formal or informal enforcement actions. Failure appears unlikely, however, given the overall strength and financial capacity of these institutions.

#### Composite 4

Financial institutions in this group generally exhibit unsafe and unsound practices or conditions. There are serious financial or managerial deficiencies that result in unsatisfactory performance. The problems range from severe to critically deficient. The weaknesses and problems are not being satisfactorily addressed or resolved by the board of directors and management. Financial institutions in this group generally are not capable of withstanding business fluctuations. There may be significant noncompliance with laws and regulations. Risk management practices are generally unacceptable relative to the institution's size, complexity, and risk profile. Close supervisory attention is required, which means, in most cases, formal enforcement action is necessary to address the problems. Institutions in this group pose a risk to the deposit insurance fund. Failure is a distinct possibility if the problems and weaknesses are not satisfactorily addressed and resolved.

#### Composite 5

Financial institutions in this group exhibit extremely unsafe and unsound practices or conditions; exhibit a critically deficient performance; often contain inadequate risk management practices relative to the institution's size, complexity, and risk profile; and are of the greatest supervisory concern. The volume and severity of problems are beyond management's ability or willingness to control or correct. Immediate outside financial or other assistance is needed in order for the financial institution to be viable. Ongoing supervisory attention is necessary. Institutions in this group pose a significant risk to the deposit insurance fund and failure is highly probable.

### COMPONENT RATINGS

Each of the component rating descriptions is divided into three sections: an introductory paragraph; a list of the principal evaluation factors that relate to that component; and a brief description of each numerical rating for that component. Some of the evaluation factors are reiterated under one or more of the other components to reinforce the interrelationship between components. The listing of evaluation factors for each component rating is in no particular order of importance.

#### Capital Adequacy

A financial institution is expected to maintain capital commensurate with the nature and extent of risks to the institution and the ability of management to identify, measure, monitor, and control these risks. The effect of credit, market, and other risks on the institution's financial condition should be considered when evaluating the adequacy of capital. The types and quantity of risk inherent in an institution's activities will determine the extent to which it may be necessary to maintain capital at levels

above required regulatory minimums to properly reflect the potentially adverse consequences that these risks may have on the institution's capital.

The capital adequacy of an institution is rated based upon, but not limited to, an assessment of the following evaluation factors:

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

### *Ratings*

- 1 A rating of 1 indicates a strong capital level relative to the institution's risk profile.
- 2 A rating of 2 indicates a satisfactory capital level relative to the financial institution's risk profile.
- 3 A rating of 3 indicates a less than satisfactory level of capital that does not fully support the institution's risk profile. The rating indicates a need for improvement, even if the institution's capital level exceeds minimum regulatory and statutory requirements.
- 4 A rating of 4 indicates a deficient level of capital. In light of the institution's risk profile, viability of the institution may be threatened. Assistance from shareholders or other external sources of financial support may be required.
- 5 A rating of 5 indicates a critically deficient level of capital such that the institution's viability is threatened. Immediate assistance from shareholders or other external sources of financial support is required.

## Asset Quality

The asset quality rating reflects the quantity of existing and potential credit risk associated with the loan and investment portfolios, other real estate owned, and other assets, as well as off-balance sheet transactions. The ability of management to identify, measure, monitor, and control credit risk is also reflected here. The evaluation of asset quality should consider the adequacy of the allowance for loan and lease losses and weigh the exposure to counterparty, issuer, or borrower default under actual or implied contractual agreements. All other risks that may affect the value or marketability of an institution's assets, including, but not limited to, operating, market, reputation, strategic, or compliance risks, should also be considered.

The asset quality of a financial institution is rated based upon, but not limited to, an assessment of the following evaluation factors:

- The adequacy of underwriting standards, soundness of credit administration practices, and appropriateness of risk identification practices.
- The level, distribution, severity, and trend of problem, classified, nonaccrual, restructured, delinquent, and nonperforming assets for both on- and off-balance sheet transactions.
- The adequacy of the allowance for loan and lease losses and other asset valuation reserves.
- The credit risk arising from or reduced by off-balance sheet transactions, such as unfunded commitments, credit derivatives, commercial and standby letters of credit, and lines of credit.
- The diversification and quality of the loan and investment portfolios.
- The extent of securities underwriting activities and exposure to counterparties in trading activities.
- The existence of asset concentrations.
- The adequacy of loan and investment policies, procedures, and practices.
- The ability of management to properly administer its assets, including the timely identification and collection of problem assets.
- The adequacy of internal controls and management information systems.
- The volume and nature of credit documentation exceptions.



### *Ratings*

- 1 A rating of 1 indicates strong asset quality and credit administration practices. Identified weaknesses are minor in nature and risk exposure is modest in relation to capital protection and management's abilities. Asset quality in such institutions is of minimal supervisory concern.
- 2 A rating of 2 indicates satisfactory asset quality and credit administration practices. The level and severity of classifications and other weaknesses warrant a limited level of supervisory attention. Risk exposure is commensurate with capital protection and management's abilities.
- 3 A rating of 3 is assigned when asset quality or credit administration practices are less than satisfactory. Trends may be stable or indicate deterioration in asset quality or an increase in risk exposure. The level and severity of classified assets, other weaknesses, and risks require an elevated level of supervisory concern. There is generally a need to improve credit administration and risk management practices.
- 4 A rating of 4 is assigned to financial institutions with deficient asset quality or credit administration practices. The levels of risk and problem assets are significant, inadequately controlled, and subject the financial institution to potential losses that, if left unchecked, may threaten its viability.
- 5 A rating of 5 represents critically deficient asset quality or credit administration practices that present an imminent threat to the institution's viability.

### Management

The capability of the board of directors and management, in their respective roles, to identify, measure, monitor, and control the risks of an institution's activities and to ensure a financial institution's safe, sound, and efficient operation in compliance with applicable laws and regulations is reflected in this rating. Generally, directors need not be actively involved in day-to-day operations; however, they must provide clear guidance regarding acceptable risk exposure levels and ensure that appropriate policies, procedures, and practices have been established. Senior management is responsible for developing and implementing policies, procedures, and practices that translate the board's goals, objectives, and risk limits into prudent operating standards.

Depending on the nature and scope of an institution's activities, management practices may need to address some or all of the following risks: credit, market, operating or transaction, reputation, strategic, compliance, legal, liquidity, and other risks. Sound management practices are demonstrated by: active oversight by the board of directors and management; competent personnel; adequate policies, processes, and controls taking into consideration the size and sophistication of the institution; maintenance of an appropriate audit program and internal control environment; and effective risk monitoring and management information systems. This rating should reflect the board's and management's ability as it applies to all aspects of banking operations as well as other financial service activities in which the institution is involved.

The capability and performance of management and the board of directors is rated based upon, but not limited to, an assessment of the following evaluation factors:

- The level and quality of oversight and support of all institution activities by the board of directors and management.
- The ability of the board of directors and management, in their respective roles, to plan for, and respond to, risks that may arise from changing business conditions or the initiation of new activities or products.
- The adequacy of, and conformance with, appropriate internal policies and controls addressing the operations and risks of significant activities.
- The accuracy, timeliness, and effectiveness of management information and risk monitoring systems appropriate for the institution's size, complexity, and risk profile.
- The adequacy of audits and internal controls to: promote effective operations and reliable financial and regulatory reporting; safeguard assets; and ensure compliance with laws, regulations, and internal policies.
- Compliance with laws and regulations.
- Responsiveness to recommendations from auditors and supervisory authorities.
- Management depth and succession.
- The extent that the board of directors and management is affected by, or susceptible to, dominant influence or concentration of authority.
- Reasonableness of compensation policies and avoidance of self-dealing.
- Demonstrated willingness to serve the legitimate banking needs of the community.
- The overall performance of the institution and its risk profile.

### *Ratings*

- 1 A rating of 1 indicates strong performance by management and the board of directors and strong risk management practices relative to the institution's size, complexity, and risk profile. All significant risks are consistently and effectively identified, measured, monitored, and controlled. Management and the board have demonstrated the ability to promptly and successfully address existing and potential problems and risks.

- 2 A rating of 2 indicates satisfactory management and board performance and risk management practices relative to the institution's size, complexity, and risk profile. Minor weaknesses may exist, but are not material to the safety and soundness of the institution and are being addressed. In general, significant risks and problems are effectively identified, measured, monitored, and controlled.
- 3 A rating of 3 indicates management and board performance that need improvement or risk management practices that are less than satisfactory given the nature of the institution's activities. The capabilities of management or the board of directors may be insufficient for the type, size, or condition of the institution. Problems and significant risks may be inadequately identified, measured, monitored, or controlled.
- 4 A rating of 4 indicates deficient management and board performance or risk management practices that are inadequate considering the nature of an institution's activities. The level of problems and risk exposure is excessive. Problems and significant risks are inadequately identified, measured, monitored, or controlled and require immediate action by the board and management to preserve the soundness of the institution. Replacing or strengthening management or the board may be necessary.
- 5 A rating of 5 indicates critically deficient management and board performance or risk management practices. Management and the board of directors have not demonstrated the ability to correct problems and implement appropriate risk management practices. Problems and significant risks are inadequately identified, measured, monitored, or controlled and now threaten the continued viability of the institution. Replacing or strengthening management or the board of directors is necessary.

## Earnings

This rating reflects not only the quantity and trend of earnings, but also factors that may affect the sustainability or quality of earnings. The quantity as well as the quality of earnings can be affected by excessive or inadequately managed credit risk that may result in loan losses and require additions to the allowance for loan and lease losses, or by high levels of market risk that may unduly expose an institution's earnings to volatility in interest rates. The quality of earnings may also be diminished by undue reliance on extraordinary gains, nonrecurring events, or favorable tax effects. Future earnings may be adversely affected by an inability to forecast or control funding and operating expenses, improperly executed or ill-advised business strategies, or poorly managed or uncontrolled exposure to other risks.

The rating of an institution's earnings is based upon, but not limited to, an assessment of the following evaluation factors:

- The level of earnings, including trends and stability.
- The ability to provide for adequate capital through retained earnings.

- The quality and sources of earnings.
- The level of expenses in relation to operations.
- The adequacy of the budgeting systems, forecasting processes, and management information systems in general.
- The adequacy of provisions to maintain the allowance for loan and lease losses and other valuation allowance accounts.
- The earnings exposure to market risk such as interest rate, foreign exchange, and price risks.

### *Ratings*

- 1 A rating of 1 indicates earnings that are strong. Earnings are more than sufficient to support operations and maintain adequate capital and allowance levels after consideration is given to asset quality, growth, and other factors affecting the quality, quantity, and trend of earnings.
- 2 A rating of 2 indicates earnings that are satisfactory. Earnings are sufficient to support operations and maintain adequate capital and allowance levels after consideration is given to asset quality, growth, and other factors affecting the quality, quantity, and trend of earnings. Earnings that are relatively static, or even experiencing a slight decline, may receive a 2 rating provided the institution's level of earnings is adequate in view of the assessment factors listed above.
- 3 A rating of 3 indicates earnings that need to be improved. Earnings may not fully support operations and provide for the accretion of capital and allowance levels in relation to the institution's overall condition, growth, and other factors affecting the quality, quantity, and trend of earnings.
- 4 A rating of 4 indicates earnings that are deficient. Earnings are insufficient to support operations and maintain appropriate capital and allowance levels. Institutions so rated may be characterized by erratic fluctuations in net income or net interest margin, the development of significant negative trends, nominal or unsustainable earnings, intermittent losses, or a substantive drop in earnings from the previous years.
- 5 A rating of 5 indicates earnings that are critically deficient. A financial institution with earnings rated 5 is experiencing losses that represent a distinct threat to its viability through the erosion of capital.

### *Liquidity*

In evaluating the adequacy of a financial institution's liquidity position, consideration should be given to the current level and prospective sources of liquidity compared to funding needs, as well as to the adequacy of funds management practices relative to the institution's size, complexity, and risk profile.

In general, funds management practices should ensure that an institution is able to maintain a level of liquidity sufficient to meet its financial obligations in a timely manner and to fulfill the legitimate banking needs of its community. Practices should reflect the ability of the institution to manage unplanned changes in funding sources, as well as react to changes in market conditions that affect the ability to quickly liquidate assets with minimal loss. In addition, funds management practices should ensure that liquidity is not maintained at a high cost, or through undue reliance on funding sources that may not be available in times of financial stress or adverse changes in market conditions.

Liquidity is rated based upon, but not limited to, an assessment of the following evaluation factors:

- The adequacy of liquidity sources compared to present and future needs and the ability of the institution to meet liquidity needs without adversely affecting its operations or condition.
- The availability of assets readily convertible to cash without undue loss.
- Access to money markets and other sources of funding.
- The level of diversification of funding sources, both on- and off-balance sheet.
- The degree of reliance on short-term, volatile sources of funds, including borrowings and brokered deposits, to fund longer term assets.
- The trend and stability of deposits.
- The ability to securitize and sell certain pools of assets.
- The capability of management to properly identify, measure, monitor, and control the institution's liquidity position, including the effectiveness of funds management strategies, liquidity policies, management information systems, and contingency funding plans.

### *Ratings*

- 1 A rating of 1 indicates strong liquidity levels and well-developed funds management practices. The institution has reliable access to sufficient sources of funds on favorable terms to meet present and anticipated liquidity needs.
- 2 A rating of 2 indicates satisfactory liquidity levels and funds management practices. The institution has access to sufficient sources of funds on acceptable terms to meet present and anticipated liquidity needs. Modest weaknesses may be evident in funds management practices.
- 3 A rating of 3 indicates liquidity levels or funds management practices in need of improvement. Institutions rated 3 may lack ready access to funds on reasonable terms or may evidence significant weaknesses in funds management practices.

- 4 A rating of 4 indicates deficient liquidity levels or inadequate funds management practices. Institutions rated 4 may not have or be able to obtain a sufficient volume of funds on reasonable terms to meet liquidity needs.
- 5 A rating of 5 indicates liquidity levels or funds management practices so critically deficient that the continued viability of the institution is threatened. Institutions rated 5 require immediate external financial assistance to meet maturing obligations or other liquidity needs.

### Sensitivity to Market Risk

The sensitivity to market risk component reflects the degree to which changes in interest rates, foreign exchange rates, commodity prices, or equity prices can adversely affect a financial institution's earnings or economic capital. When evaluating this component, consideration should be given to: management's ability to identify, measure, monitor, and control market risk; the institution's size; the nature and complexity of its activities; and the adequacy of its capital and earnings in relation to its level of market risk exposure. For many institutions, the primary source of market risk arises from nontrading positions and their sensitivity to changes in interest rates. In some larger institutions, foreign operations can be a significant source of market risk. For some institutions, trading activities are a major source of market risk.

Market risk is rated based upon, but not limited to, an assessment of the following evaluation factors:

- The sensitivity of the financial institution's earnings or the economic value of its capital to adverse changes in interest rates, foreign exchanges rates, commodity prices, or equity prices.
- The ability of management to identify, measure, monitor, and control exposure to market risk given the institution's size, complexity, and risk profile.
- The nature and complexity of interest-rate risk exposure arising from nontrading positions.
- Where appropriate, the nature and complexity of market risk exposure arising from trading and foreign operations.

### *Ratings*

- 1 A rating of 1 indicates that market risk sensitivity is well controlled and that there is minimal potential that the earnings performance or capital position will be adversely affected. Risk management practices are strong for the size, sophistication, and market risk accepted by the institution. The level of earnings and capital provide substantial support for the degree of market risk taken by the institution.
- 2 A rating of 2 indicates that market risk sensitivity is adequately controlled and that there is only moderate potential that the earnings performance or capital position will be adversely affected. Risk management practices are satisfactory for the size, sophistication, and market risk accepted

- by the institution. The level of earnings and capital provide adequate support for the degree of market risk taken by the institution.
- 3 A rating of 3 indicates that control of market risk sensitivity needs improvement or that there is significant potential that the earnings performance or capital position will be adversely affected. Risk management practices need to be improved given the size, sophistication, and level of market risk accepted by the institution. The level of earnings and capital may not adequately support the degree of market risk taken by the institution.
  - 4 A rating of 4 indicates that control of market risk sensitivity is unacceptable or that there is high potential that the earnings performance or capital position will be adversely affected. Risk management practices are deficient for the size, sophistication, and level of market risk accepted by the institution. The level of earnings and capital provide inadequate support for the degree of market risk taken by the institution.
  - 5 A rating of 5 indicates that control of market risk sensitivity is unacceptable or that the level of market risk taken by the institution is an imminent threat to its viability. Risk management practices are wholly inadequate for the size, sophistication, and level of market risk accepted by the institution.

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## COMPLIANCE RATING SCALE

OTS defines the five-point Compliance Ratings as follows:

### Rating 1

An association in this category is in a strong compliance management position. The compliance management program completely and reliably covers all six SMAART components and applies best practices in developing, maintaining and executing that program. The institution conducts thorough and reliable self-assessments in accordance with a well-conceived risk schedule and promptly corrects any violations or operational deficiencies. System records are complete. Review reports are well prepared and integral to management and board decisions. Training maintains staff compliance expertise. Monitoring controls are strong resulting in any compliance violations being infrequent, self-identified and timely corrected. There is no evidence of prohibited discrimination, reimbursable violations, or systemic deficiencies resulting in repeated substantive violations. The institution's compliance management gives no cause for supervisory concern.

### Rating 2

An association in this category is in an adequate compliance management position. Management has a demonstrated capacity to administer an effective compliance program that satisfactorily addresses the SMAART components. Self-assessments may or may not be conducted, but in any case are not thorough enough, or their results adequately assimilated, to be a sufficient basis upon which to grade compliance management performance. Separate evaluation of the other SMAART components by the examiner supports favorable findings of compliance management capabilities and performance given the institution's size, business strategy, operational complexity and risk profile. Some areas of programmatic weakness or areas for improvement may occur that either had not been self-identified or were self-identified but not promptly self-corrected. Readily attainable enhancements to the institution's compliance program and/or the establishment of additional review/audit procedures will eliminate performance deficiencies. Although there may be technical compliance violations and limited infrequent substantive violations readily remedied, there is no evidence of prohibited discrimination, reimbursable violations, or programmatic deficiencies resulting in repeated substantive violations.

### Rating 3

An association in this category is in a less than satisfactory compliance position requiring a further supervisory review. Management does not conduct reliable self-assessments, and the other components of the compliance management program do not perform sufficiently well to prevent systemic or repeated non-technical compliance violations. Overall implementation of the SMAART components is not up to the standards expected of institutions of similar capacity. Violations may be numerous. Substantive regulatory violations were either not self-identified or were not fully remedied as part of the institution's regular monitoring or response processes. There is no finding of prohibited discrimination. By identifying an institution with marginal compliance early,

additional supervisory oversight may be employed to assure compliance management improvements are implemented and further deterioration of the institution's compliance performance is prevented.

#### Rating 4

An association in this category requires prompt supervisory intervention to correct serious compliance program deficiencies. Management has material shortfalls in its implementation of a comprehensive compliance management program as measured by SMAART. Management failures have resulted in substantive compliance violations, often involving a significant segment of consumers or requiring substantial monetary remedies, that have not been remedied on the institution's initiative in a timely fashion, or are significantly below standards for the institution's expected level of competence given its size, strategy, sophistication and risk profile. Close supervision of agency-directed institution self-assessment may be required to assure reliability or thoroughness of corrective actions. Transaction analysis supports the need for agency intervention to effectively supervise the institution's return to an acceptable level of compliance performance.

#### Rating 5

An association in this category is in need of the strongest supervisory intervention and oversight. SMAART components have been ineffectually implemented or ignored. The association is substantially in noncompliance with several of the civil rights, consumer or public interest statutes and regulations. The severity of its noncompliance creates legal and financial exposure of significant risk to the association. Management has demonstrated its unwillingness or inability to operate within the scope of these statutes and regulations. Previous efforts on the part of the regulatory authority to obtain voluntary compliance have not been effective. Discrimination, substantial overcharges or other practices resulting in systemic or serious repeat violations are present.

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## Enforcement Actions

The Office of Thrift Supervision (OTS) uses its statutory authorities to take prompt and vigorous enforcement action when warranted. Proper use of OTS's formal enforcement powers and informal supervisory responses is critical in helping OTS meet its functional responsibilities:

- Ensuring the safety and soundness of the thrift industry.
- Ensuring that all associations and their holding companies comply with laws and regulations.
- Maintaining the soundness of the insurance fund.

OTS uses its enforcement powers primarily to eliminate unsafe or unsound practices and to require corrective action. OTS may take enforcement action against savings associations, savings and loan holding companies, service corporations, operating subsidiaries, other affiliates, or institution-affiliated parties (IAP).<sup>1</sup>

[LINKS](#)  
[Program](#)  
[Appendix A](#)

The enforcement policies in this handbook section apply to all the parties listed in the paragraph above as well as all examination types.<sup>2</sup>

OTS uses formal and informal enforcement tools to carry out its supervisory and enforcement responsibilities to address violations of laws and regulations, conditions imposed in writing, and written agreements with the agency. These tools are the focus of this handbook section.

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<sup>1</sup> Institution-affiliated party means:

- Any director, officer, employee, or controlling stockholder (other than a savings and loan holding company) of, or agent for, an insured depository institution.
- Any other person who filed or OTS requires to file a change-in-control notice with OTS under 12 USC § 1817(j).
- Any shareholder (other than a savings and loan holding company), consultant, joint venture partner, or any other person as determined by OTS (by regulation or case-by-case) who participates in the conduct of the affairs of an insured depository institution.
- Any independent contractor (including any attorney, appraiser, or accountant) who knowingly or recklessly participates in any:
  - violation of law or regulation,
  - breach of fiduciary duty, or
  - unsafe or unsound practice,which caused or is likely to cause more than a minimal financial loss to, or have a significant adverse effect on, the insured depository institution. 12 USC § 1813 (u).

<sup>2</sup> These policies and procedures only provide guidance. They are not intended to, do not, and may not be relied upon to, create rights, substantive or procedural, enforceable at law or in any administrative proceeding.

## SUPERVISORY POLICIES

OTS considers the following items before determining whether an association's problems warrant any enforcement action:

- An analysis of the facts.
- An assessment of the seriousness of the problem.
- The association's supervisory history.
- The quality and cooperation of management involved.
- The results of any meetings with the board of directors.
- An evaluation of whether management has demonstrated it will take appropriate corrective action.
- An assessment of the potential harm to the association if the association does not take corrective action.
- Information or referrals from another financial regulator, including a functional regulator such as the SEC.
- Severity of the effect the holding company enterprise is having on the savings association.

## Selecting the Appropriate Tool

Choosing the appropriate supervisory response involves the careful balancing of factors and the exercise of sound supervisory judgment. The general considerations for determining whether to use a formal or informal enforcement action are:

- The extent of actual or potential damage, harm, or loss to the savings association because of its action or inaction.
- Whether the misconduct or unsafe or unsound practice is repeated.
- The likelihood based on prior conduct that the unsafe or unsound practice may occur again.
- The association's prompt remedial and corrective action in the present matter as well as past violations.
- The capability, cooperation, integrity, and commitment of the association's management, board of directors, and ownership to correct identified problems.

- The extent the identified problems were preventable.
- The effect of the misconduct, or unsafe or unsound practice on other financial institutions, depositors, or the public.
- The examination rating of the association.
- Whether the association's condition is improving or deteriorating based on exam findings.
- The presence of unique circumstances.
- The supervisory goal OTS wants to achieve.

The last factor, the supervisory goal, is especially important in determining the appropriate supervisory action. For example, a Cease and Desist (C&D) order may require affirmative corrective actions, including the payment of restitution or reimbursement to an institution, but cannot require the removal or prohibition of an individual from participating in the institution's affairs. That remedy requires issuance of a Removal and Prohibition (R&P) order, based on the statutory elements in 12 USC § 1818(e).

## Policy on Enforcement Actions

### *When to Take Formal Enforcement Action*

For serious problems or deficiencies, formal enforcement action may be the appropriate initial action. There is a strong presumption that OTS will take prompt formal enforcement action against any association with serious problems regardless of examination ratings or capital levels. Examples of when OTS will consider taking formal enforcement action include, but are not limited to, one or more of the following situations:

For serious problems or deficiencies, formal enforcement action may be the appropriate initial action.

- The association's records, systems, controls, policies, or internal audit program exhibit significant problems or weaknesses.
- There is insider abuse.
- There are violations of law or regulations.
- There is material noncompliance despite prior commitments to take corrective actions.
- The board does not take corrective action.
- Informal actions are or would be insufficient.

- The association does not maintain satisfactory books and records or provide OTS or other regulatory authorities with prompt and complete access to books and records.

#### *4- and 5-Rated Associations and Holding Companies*

There is a strong presumption that savings associations and holding companies with a composite examination rating of 4 or 5 warrant formal enforcement action. Because a 4- or 5-rated association or holding company requires close supervisory attention and failure is possible if the problems and weaknesses are not satisfactorily addressed and resolved in a timely manner, a formal OTS enforcement action is presumed necessary.

#### *3-Rated Associations and Holding Companies*

There is a presumption that savings associations or holding companies with a composite examination rating of 3 warrant informal enforcement action. Although failure appears unlikely given the association's overall strength and financial capacity, 3-rated institutions require more than normal supervision and an informal enforcement action is presumed necessary. The capability, cooperation, integrity, and commitment of management, the board, and owners and the timeliness of remedial actions are important considerations in choosing the appropriate action. OTS will consider taking formal enforcement action under one or more of the following circumstances:

- Management rating of the association or risk management rating of the holding company is 3 or below.
- There is uncertainty as to whether management and the board have the ability or willingness to take appropriate corrective measures.
- Overall condition is rapidly deteriorating.
- A 3-rating continues for two consecutive examinations following the association or holding company entering into the informal enforcement action or the informal action is deemed insufficient to address the issues.
- The association or holding company is not in compliance with prior commitments to take corrective action.

### Consulting with State Authorities and the FDIC

Communications with other regulators is essential to ensure an effective resolution of a problem association. Consultation with state banking supervisors should occur in parallel with examinations, supervisory efforts, and enforcement actions. For example, when considering a supervisory agreement with a state-chartered association,

Communications with other regulators is essential to ensure a smooth resolution of a problem association.

OTS will consult with the state supervisor and solicit concurrence. If OTS issues an Individual Minimum Capital Requirement directive to a state-chartered savings association, OTS will notify the state regulator (12 CFR § 567.3(d)(1) and (3)). OTS consults with the FDIC and other appropriate regulatory agencies, as well as state regulators, before taking formal enforcement actions against state-chartered associations.

In coordinating these consultations, OTS will comply with existing information sharing agreements and laws that govern information sharing between regulators.

## TYPES OF ENFORCEMENT ACTIONS

This section discusses the specific types of enforcement actions, formal and informal, that OTS may take, the regulatory considerations in deciding whether and what type of enforcement action to take, and the procedures for investigating and initiating enforcement actions.

OTS generally attempts to obtain consent to the issuance of an enforcement action from an association's board of directors. Where an immediate cessation to an activity is necessary, OTS will proceed without seeking consent (e.g., if books and records of the association are in danger of being destroyed or if the books and records of the association are so incomplete or inaccurate that OTS cannot determine the financial condition of the association).

### Informal Enforcement Actions

When an association's overall condition is sound, but it is necessary to obtain written commitments from an association's board of directors or management to ensure that it will correct the identified problems and weaknesses, OTS may use informal enforcement actions. OTS commonly uses informal actions for problems in the following types of associations:

- Well or adequately capitalized associations.
- Associations with a composite rating of 1, 2, or 3 .

Informal actions notify the board and management that OTS has identified problems that warrant attention. A record of informal action is beneficial in case formal action is necessary later.

Informal actions are not enforceable in and of themselves. If the association violates or refuses to comply, OTS cannot enforce compliance in federal court or assess civil money penalties for noncompliance, but OTS may take more severe enforcement actions if the association fails to comply. The effectiveness of the informal tools depends in part on the willingness and ability of the association to correct deficiencies that OTS notes.

OTS has a number of informal enforcement tools available to address unsafe or unsound practices or violations of laws and regulations. Those informal enforcement actions include:

- **Memorandum of Understanding.** A Memorandum of Understanding is a commitment by an association to OTS in which the association agrees to correct a violation of law, regulation or an unsafe or unsound practice.
- **Board Resolution.** A document designed to address one or more specific concerns identified by OTS and adopted by the association's board of directors.
- **Supervisory directive.** A directive to the association to cease an activity or take an affirmative action to remedy or prevent an unsafe or unsound practice.
- **Notice of deficiency and request for safety and soundness compliance plan.**
- **Individual Minimum Capital Requirement (IMCR) Directives.** OTS may establish an IMCR for a savings association that varies from the requirement that would otherwise apply to the association. OTS may establish an IMCR for a savings association, as necessary on a case-by-case basis, pursuant to 12 CFR § 567.3.

Minimum capital levels higher than those normally required may be appropriate for savings associations:

- Needing special supervisory attention.
- Exhibiting a high degree of exposure to interest rate risk, credit risk, and other risks.
- Experiencing poor liquidity or cash flow problems due to weak credit quality, operational losses, and other factors.

Savings associations have the opportunity to respond in writing when they are notified that OTS is imposing an IMCR. Failure to satisfy an IMCR may constitute grounds for issuance of a capital directive or other formal enforcement action.

If informal tools do not resolve the problem, OTS will use formal enforcement tools. An association's unwillingness to comply with an appropriate informal remedy is a significant factor in determining whether a formal enforcement action is appropriate.

Formal actions are appropriate when an association has significant problems, especially when there is a threat of harm to the association, depositors, or the public.

## Formal Enforcement Actions

A formal enforcement action is enforceable under the Federal Deposit Insurance Act (FDIA) (12 USC § 1818). Formal actions are appropriate when an association has significant problems, especially when there is a threat of harm to the association, depositors, or the public. OTS will use formal enforcement actions when informal remedial actions are considered inadequate, ineffective, or otherwise unlikely to secure correction of safety and soundness or compliance problems.



Because formal actions are enforceable, OTS can assess civil money penalties against associations and individuals for noncompliance with a formal agreement or final orders. OTS can also request a federal court to require the association to comply with an order. Unlike informal actions, formal enforcement actions are public.

Formal enforcement actions include the following:

- Formal written agreements pursuant to 12 USC § 1818. These agreements include supervisory agreements and capital directives under 12 CFR § 567.
- Cease-and-desist orders (C&Ds).
- Temporary C&Ds.
- Removal and/or prohibition orders (R&Ps).
- Temporary suspensions for certain criminal indictments.
- Civil money penalties (CMPs).
- Prompt Corrective Action (PCA) directives, including capital plans under 12 USC § 1831o and 12 CFR Part 565 (including temporary restrictions on operations).
- Safety and soundness orders pursuant to Section 39 of the FDIA.
- Injunctive actions.
- Immediate suspensions during removal and prohibition proceedings.
- Suspension or debarment of attorneys, accountants, and accounting firms.
- Conservatorships and receiverships.
- Enforcement of orders in United States District Court.

### *Supervisory Agreements*

Supervisory agreements are formal written agreements used only with savings associations or their holding companies that are subject to OTS's continuing supervision and jurisdiction, not with individuals or other entities. OTS may use supervisory agreements to require savings associations or holding companies to take corrective action with respect to the association's violation of law or regulation or continued unsafe or unsound practice. The agreements may also require affirmative corrective action to address any existing violations, management or operational deficiencies, or other

unsound practices. In short, they may include the same broad range of provisions that OTS may incorporate into C&D orders.

Violations of supervisory agreements, unlike violations of other types of formal enforcement actions, are not enforceable in federal court (12 USC § 1818 (i)). However, a violation of a supervisory agreement may form the basis for the assessment of CMPs, C&D actions, and R&P actions. To ensure that supervisory agreements, if violated, will properly form the basis for other enforcement actions, each supervisory agreement should state that “the Agreement is a ‘written agreement’ for the purposes of Section 8 of the FDIA, 12 USC § 1818.”

Violations of supervisory agreements, unlike violations of other types of formal enforcement actions, are not enforceable in federal court.

### *Capital Directives*

A capital directive is an order designed to establish and enforce capital levels and for taking capital-related action. OTS may issue a capital directive based on any of the following:

- A savings association’s noncompliance with a capital requirement established under 12 CFR §§ 567.2 and 567.3.
- By a written agreement under 12 USC § 1464(s).
- As a condition for approval of an application.

### *Cease-and-Desist Orders*

A C&D order normally requires the association to correct any violation of law, regulation, or an unsafe or unsound practice. OTS may issue a C&D order in response to violations of federal banking, securities, or other laws by associations or individuals, or if it believes that an unsafe and unsound practice or violation is about to occur.

OTS authority for issuing C&D orders is the FDIA (12 USC § 1818(b)). OTS may issue a C&D order if one of the following factors is present:

- An unsafe or unsound practice.
- A violation of law, rule, or regulation.
- A violation of any condition imposed in writing in connection with the granting of an application, or any written agreement with OTS.

OTS can issue a C&D order by consent or following a formal administrative hearing.

OTS can issue a C&D order against a savings association, its service corporation or subsidiary, an IAP, a savings and loan holding company, a holding company subsidiary, or service providers.

If an entity or individual fails to comply with a final order, OTS may seek enforcement of the order through the United States District Court. Violations of an order may form the basis for civil money penalties and for removal and prohibition actions. A party subject to the C&D order may request modification or termination of the order.

### *Temporary Cease-and-Desist Orders*

OTS uses temporary C&D orders to address situations requiring immediate action. When issuing a temporary order, OTS also issues a notice of charges, which also initiates a proceeding to obtain a permanent C&D order. In the notice of charges, OTS must state that it has determined that there is a violation, an unsafe or unsound practice, or a threatened violation or practice that is likely to result in one or more of the following conditions:

- Insolvency or significant dissipation of assets or earnings.
- Weakening of the association's condition.
- Prejudice to the interests of the depositors before the completion of the C&D proceeding.

A temporary C&D order may require affirmative action to prevent insolvency, dissipation of assets, a weakened condition, or prejudice. OTS may use a temporary C&D order to require that an association restore its books and records to a complete and accurate state under the following conditions:

A temporary C&D order may require affirmative action to prevent insolvency, dissipation of assets, a weakened condition, or prejudice.

- An association's books and records are so incomplete or inaccurate that OTS is unable, through the normal supervisory process, to determine the financial condition of the association.
- An association's books and records are so incomplete or inaccurate that OTS cannot determine the details or purpose of a transaction that may have a material effect on the association's financial condition.

OTS may also use a temporary C&D to order cessation of any activity pending the completion of the C&D proceeding. For example, OTS may issue a temporary C&D order to freeze assets pending the outcome of litigation or to require immediate change in management. OTS can also require cessation of activities causing incomplete or inaccurate books or records.

A temporary C&D order terminates automatically when OTS dismisses the charges in the notice initiating the C&D proceeding or when a permanent C&D order against the same party becomes effective.

### *Orders of Removal and Prohibition*

OTS can remove an IAP from office and prohibit a person or entity from further participation in any insured depository institution under Section 8(e) of the FDIA, 12 USC § 1818(e), if one element of each of the following three statutory prongs is met:

- The IAP directly or indirectly engaged in any of the following practices:
  - Violated a law, regulation, or final C&D order.
  - Violated any condition imposed in writing by the appropriate federal banking agency in connection with the grant of any application or other request by the depository institution.
  - Violated any written agreement between the depository institution and the agency.
  - Engaged or participated in any unsafe or unsound practice with respect to any insured depository institution or business institution.
  - Committed or engaged in any act, omission, or practice that constitutes a breach of fiduciary duty.
- As a result of the violation, unsafe or unsound practice, or breach of fiduciary duty described above, any of the following occurred:
  - The insured depository institution suffered or will probably suffer financial loss or other damage.
  - The interests of the insured depository institution's depositors have been or could be prejudiced.
  - The IAP received financial gain or other benefit from the violation, practice, or breach.
- The violation, unsafe or unsound practice, or breach of fiduciary duty:
  - Involves personal dishonesty.
  - Demonstrates a willful or continuing disregard for the safety or soundness of the insured depository institution or business institution.

An R&P order has industry-wide effect and bars an individual from holding office in, being employed by, or participating in any manner in the conduct of the affairs of any insured depository institution, including credit unions, and from working for any depository institution regulatory agency without the prior written consent of the agency issuing the order. Removed or prohibited individuals may request modification or termination of the R&P order. Individuals who violate R&P orders are subject to criminal penalties.

Anyone convicted of a criminal offense involving dishonesty or breach of trust, or who has agreed to enter into a pre-trial diversion or similar program in connection with such a prosecution, is automatically subject to an industry-wide prohibition by operation of law (12 USC § 1829).

### *Temporary Suspensions*

OTS may issue an order temporarily suspending an individual from a position in conjunction with a notice of intention to remove or prohibit the individual (12 USC § 1818(e)(3)). By statute, OTS can issue a temporary suspension only if the suspension is necessary to protect the interests of the depository institution or its depositors. The suspension remains in effect pending the removal or prohibition proceeding initiated by the notice, unless a district court stays the suspension as provided by the FDIA (12 USC § 1818(f)).

OTS staff must adequately document violations or unsafe or unsound practices underlying the temporary suspension. OTS will use the documentation when presenting its action to a reviewing court. Appropriate documentation may include the following materials:

- Examination reports.
- Sworn testimony.
- Other materials documenting violations or personal gain to the individual.
- Periodic reports to OTS showing a decline in an association's financial condition.

A suspended individual may apply to the U.S. District Court for an injunction or stay of the temporary suspension within ten days of service of the suspension. The court will consider both the reasonableness of OTS's decision to issue the suspension and the traditional standards for injunctive relief.

OTS has authority to temporarily suspend or remove an individual charged with committing or participating in a crime involving dishonesty or breach of trust, which is punishable by a term of imprisonment exceeding one year, if the individual's continued service poses a threat to the interests of the association's depositors or threatens to impair public confidence in any relevant depository institution (12 USC § 1818(g)). In such cases, the temporarily suspended or prohibited individual may request an opportunity to appear before the agency to show that his or her continued participation does not pose a threat or may pose a threat to the interests of depositors or threaten or may threaten to

impair public confidence. The suspension or prohibition remains in effect until resolution of the criminal charges or termination of the order of suspension.

### *Civil Money Penalties*

OTS possesses statutory authority under the FDIA and other statutes to assess CMPs against savings associations, their service corporations or subsidiaries, savings and loan holding companies, subsidiaries of holding companies, and IAPs. Assessment of a CMP is appropriate for any of the following violations:

- Violations of any law or regulation.
- Violations of the terms of any final or temporary order.
- Violations of any condition OTS imposed in writing in connection with the granting of any application or other request by the association.
- Violations of any written agreement between the association and OTS.
- Breaches of fiduciary duty.
- Failure to maintain adequate records.
- Failure to file, or filing late or inaccurate OTS-required reports.
- Unsafe or unsound practices.

When assessing a CMP, OTS considers the following factors:

- Financial resources and good faith of the person, association, or company.
- Whether the person, association, or company will make financial resources available.
- The gravity of the violation.
- The history of previous violations.
- Any such other matters as justice may require.

OTS uses the Civil Money Penalty Form in [Regulatory Bulletin \(RB\) 18-3a](#) as guidance in considering and assessing CMPs. The form consists of the Civil Money Penalty Tier Matrix to determine the tier of a violation, and the Civil Money Penalty Calculation Sheet to assess a penalty amount for the violation. There are two tier matrices: the General Tier Matrix and the Reporting Violation Tier Matrix.

While OTS expects to use these matrices in all cases where it is considering an assessment, they are not substitutes for sound supervisory judgment. Individual cases may possess particularly egregious or mitigating characteristics not included as factors in the matrices.

For detailed information on the application of civil money penalties, refer to the FFIEC Policy Statement on Civil Money Penalties (6/3/98) and to [RB 18-3a](#), Enforcement Policy Statement on Civil Money Penalties (7/30/93).

### *Prompt Corrective Action*

Prompt Corrective Action (PCA) is triggered by an association's capital category, as defined in 12 USC § 1831o and 12 CFR Part 565. Depending on an association's PCA capital category, certain restrictions and actions are automatically imposed by operation of law. Other PCA actions are discretionary. (See [Appendix A](#)).

### Capital Plans

In addition to mandatory and discretionary operating restrictions, the FDIA requires all savings associations with a capital category below adequately capitalized to submit a capital restoration plan (Capital Plan) within 45 days of receiving notice or being deemed to have notice of becoming undercapitalized. OTS regulations provide the timing, content, and approval standards for Capital Plans in 12 CFR § 565.5. The Capital Plan must explain in detail the proposed strategy for becoming, at a minimum, adequately capitalized, and for accomplishing the association's overall objectives.

Under 12 USC § 1831o(e)(2), OTS must consider various factors in determining whether to approve the plan. These factors include, but are not limited to, the following criteria:

- How the association will comply with restrictions and requirements under the FDIA.
- The association's proposal to become adequately capitalized.
- The association's activities.
- Whether the association's assumptions are realistic.
- Likelihood of success.
- Risk exposure.

Each controlling company of an undercapitalized association must guarantee that the association will comply with the Capital Plan until adequately capitalized (on average) during four consecutive quarters, and provide adequate assurances of performance (12 USC § 1831o(e)(2)(c)(ii)).

If OTS approves the Capital Plan submitted by the association, it becomes the basis for a PCA Directive along with any mandatory or discretionary operating restrictions applicable to the association.

If OTS determines that the association's Capital Plan is not acceptable or if the association fails to file one, OTS issues a PCA Directive. The PCA Directive becomes the basis for curtailing certain activities, and mandating the steps necessary to either increase capital to acceptable levels, or otherwise move the association toward resolution. See discussion in [Appendix A](#) on Capital Plans.

#### Prompt Corrective Action (PCA) Directives

The FDIA requires that the agencies take prompt enforcement against undercapitalized institutions. Under PCA standards, an institution is in one of five capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, or critically undercapitalized. Mandatory, discretionary, and presumed restrictions and sanctions apply for institutions in the three undercapitalized categories. Additional information regarding the five capital categories is contained in the [Examination Handbook Section 120, Capital Adequacy](#). A PCA directive establishes a capital-based supervisory scheme that requires OTS to place increasingly stringent restrictions on associations as regulatory capital levels decline. The primary objective of PCA is "to resolve problems of insured depository institutions at the least possible long-term loss to the deposit insurance fund" (12 USC § 1831o(a)(1)).

PCA mandates the imposition of certain restrictions once an association falls below the well capitalized category. Most of the restrictions are limited to associations at the undercapitalized level or below. The following two restrictions, however, pertain to all adequately capitalized associations:

PCA mandates the imposition of certain restrictions once an association falls below the well capitalized category.

- No association can make a capital distribution if it results in undercapitalization; and
- The FDIC restricts associations from receiving brokered deposits or acting as a deposit broker unless they meet the well capitalized definition.

For associations at the undercapitalized level and below, there are additional mandatory operating restrictions that apply automatically without regard to whether a PCA directive is in place. These restrictions set out in 12 USC § 1831o(e) and 12 CFR § 565.6(a)(2), include the following actions:

- Restricting asset growth.
- Restricting capital distributions and certain management fees.
- Limiting the ability to make acquisitions, branch, or enter new lines of business.
- Requiring compliance with a capital restoration plan submitted by the association.
- Monitoring by OTS. (This may include more frequent field visits by OTS or written quarterly reports from the board of directors on adherence to the PCA restrictions.)



In addition to the mandatory restrictions, the PCA regulations provide OTS with authority to apply a wide range of discretionary remedies (12 USC § 1831o(e)(5) and § 1831o(f)(5)). OTS will consider imposing the following discretionary restrictions when conditions warrant:

- Require recapitalization.
- Restrict transactions with affiliates.
- Restrict interest rates paid.
- Restrict asset growth more stringently than required by statute.
- Restrict activities (for example, banning certain types of lending).
- Improve management (for example, mandating the election of a new board of directors, dismissing current directors and members of senior management, or requiring the hiring of certain qualified employees subject to OTS approval) (12 USC § 1831o(f)(2)(F) and 12 CFR §§ 565.6 and 565.9).
- Prohibit deposits from correspondent banks.
- Require prior approval for capital distributions by a bank holding company.
- Require divestiture.
- Restrict executive or senior officer compensation more stringently than required by statute (for example, restricting bonuses) (12 USC § 1831o(f)(4)).
- Take any other action necessary to resolve the problems of the association at the least possible long term loss to the insurance fund.

The above provisions apply to associations that fail to submit and implement Capital Plans. OTS regulations at 12 CFR § 565.7 pertain to the process for issuance of PCA directives. See also Appendix A under PCA Directives.

In addition to the PCA remedies available for undercapitalized savings associations, the statutory framework allows OTS to reclassify an association's PCA category if it operates in an unsafe and unsound condition (12 USC § 1831o(g) and 12 CFR § 565.8). Associations may request a hearing regarding the reclassification and the restrictions under 12 CFR § 565.8(a)(5) and (6). Once OTS has implemented a reclassification, an association can petition OTS for a PCA category upgrade if it successfully rectifies the unsafe and unsound conditions. See discussion in Appendix A on PCA Reclassifications.

*Safety and Soundness Orders Pursuant to Section 39 of the FDIA*

OTS also has authority to issue a Safety and Soundness Order against a savings association under 12 USC § 1831p-1 and the implementing regulations, 12 CFR Part 570.

The process begins with OTS issuing a notification to the association of its failure to meet the safety and soundness standards, and requesting that the association submit a compliance plan.

Generally, this tool addresses unsafe and unsound conduct that is not reflected in capital levels. These notices of deficiencies may also address specific problems in well or adequately capitalized associations. OTS generally only uses Part 570 safety and soundness notices of deficiency when the following conditions are present:

- The problems or weaknesses are narrow in scope and correctable.
- OTS is confident of the board's and management's commitment and ability to correct problems or weaknesses.

If the association fails to submit a compliance plan, or fails to comply with an approved compliance plan, OTS may issue a Safety and Soundness Order. The association has the right to respond in writing to the proposed issuance of an order. There are serious consequences for an association's failure to comply with a Safety and Soundness Order. OTS can impose CMPs or seek enforcement through judicial or administrative proceedings.

## POST-ENFORCEMENT ACTIONS

### Checking for Compliance with Outstanding Agreements and Orders

The recurrence of a problem previously addressed by an informal method of supervision, such as a supervisory directive, raises a presumption that OTS will pursue a C&D action or assess a CMP. That is, a material violation of an informal enforcement action should cause OTS to consider a C&D action or a CMP assessment, unless there are substantial mitigating factors.

A significant violation of a formal enforcement order raises a presumption that OTS will take a more severe formal enforcement action (for instance, CMPs against the board or management if the association has failed to comply with a C&D order).

During every comprehensive examination, examiners will expressly check for compliance with each outstanding directive, agreement, or order. Examiners must document compliance or noncompliance in the report of examination (ROE). The terms of the directive, agreement, or order will dictate the scope of the inquiry. For example, an agreement requiring an association to develop and adopt effective, written lending procedures necessitates that examiners review the procedures for clarity, effectiveness, and proof that the board of directors adopted them. An agreement that the association must comply fully with new loan procedures requires a review of a sample of loans for compliance with those

procedures. This review should be in addition to the normal loan review for compliance with applicable regulations and safety and soundness standards. (See [Handbook Section 060](#), Examination Scheduling, Scoping, and Management).

## Documentation

Supervisory and enforcement actions require thorough documentation. In the event an association violates a formal enforcement action, OTS will enforce the formal enforcement action in court. OTS will rely on the examiners' determination and documentation of the source of noncompliance (or other conduct). Discussions with management should be documented and summarized. The documentation should include management's verbal and written explanations of why such violations occurred and OTS's opinion as to the necessity of further enforcement action.

In all cases, OTS should obtain clear documentary evidence of the violations or conduct to provide evidence in the event OTS issues an order or must enforce the order in District Court.

## Termination or Modification of Enforcement Actions

Generally, OTS does not terminate an enforcement action until the association has complied with all the articles in the enforcement action document.

Generally, OTS does not terminate an enforcement action until the association has complied with all the articles in the enforcement action document.

OTS must document a decision to terminate or modify an enforcement action. An OTS examination documenting compliance with the enforcement action is usually a prerequisite to removal of the action unless OTS can obtain the appropriate documentation to support such modification or termination without an examination. In limited instances, OTS will permit a modification or termination of an enforcement action without an examination if deemed appropriate.

## METHODS OF GATHERING INFORMATION

### Regular and Special Examinations

Generally, OTS will attempt to informally obtain information before requesting a formal examination with subpoena power. OTS will obtain and use reliable information from savings associations and their affiliates, employees, and agents.

Because of OTS's authority to examine the records of any savings association and that association's affiliates, OTS does not need to issue subpoenas to compel the production of the records of the savings association or their affiliates. HOLA § 5(d)(1)(B) entitles OTS to prompt and complete access to all association personnel and agents, and to all association documents. Examiners should notify Regional Counsel or Regional Enforcement Counsel immediately if the association or its personnel refuse to supply association records or otherwise obstructs the progress of an OTS examination.

Section 5(d)(1)(B) grants OTS specific authority to go to federal court to obtain an order requiring that the association provide such access. Informal requests to interview persons outside of the association or to review records of a borrower or other entity that is not a savings association or its affiliate may also be informative.

The Gramm-Leach-Bliley Act [Pub. L. No. 106-102, 113 Stat. 1338 (1999)] established a framework of procedural requirements and criteria for working with functionally related entities, which may be a subsidiary, affiliate, or other depository institution engaged in activities regulated by another regulatory agency, such as the SEC. OTS will work cooperatively with the primary regulator of the entity to request information and reports. In limited circumstances, if the regulator is unable or unwilling to obtain the information, OTS can request the information directly from the entity. If the information is insufficient, OTS can, in some instances, conduct an on-site examination of the entity if OTS can meet certain requirements showing need for the information.

## REFERENCES

### United States Code (12 USC)

§ 1464(d)	Regulatory Authority
§ 1464(s)(2)	Individual Minimum Capital Requirement
§ 1464(s)(4)	Directive to Increase Capital
§ 1467a	Regulation of Holding Companies
§ 1467a(g)	Administration and Enforcement
§ 1813(u)	Institution-Affiliated Party
§ 1817(j)	Change in Control of Insured Depository Institutions
§ 1818(b)	Cease-and-Desist Proceedings
§ 1818(e)	Removal and Prohibition Authority
§ 1818(f)	Stay of Suspension and/or Prohibition of Institution-Affiliated Party
§ 1818(g)	Suspension or Removal of Institution-Affiliated Party Charged with Felony
§ 1818(i)(1)	Proceedings to Enforce Compliance
§ 1818(i)(2)	Civil Money Penalties
§ 1818(i)(4)	Prejudgment Attachment

§ 1818(n)	Subpoena Power
§ 1820(c)	Subpoena Power
§ 1831o	Prompt Corrective Action
§ 1831p-1	Actions to be Taken for Failure to Comply with Safety and Soundness Standards

### Code of Federal Regulations (12 CFR)

Part 508	Removals, Suspensions, and Prohibitions Where a Crime Is Charged or Proven
§ 509 et seq	Adjudicatory Proceedings
§ 512 et seq	Investigative and Formal Examination Proceedings
Part 513	Practice Before the Office
Part 565	Prompt Corrective Action
§ 565.7	Directives to Take Prompt Corrective Action
§ 567.3	Individual Minimum Capital Requirements
§ 567.4	Capital Directives
Part 570	Safety and Soundness Orders

### Office of Thrift Supervision Bulletins

RB 18	Issuance of Enforcement Policies
RB 18-3a	Enforcement Policy Statement on Civil Money Penalties

### Other References

FFIEC Interagency Policy Regarding the Assessment of Civil Money Penalties by the Federal Financial Institutions Regulatory Agencies, June 3, 1998

# Enforcement Actions Program

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## EXAMINATION OBJECTIVES

To determine if the association and individuals are in compliance with the requirements of outstanding agreements or orders.

To determine if new or additional enforcement actions need to be taken to correct deficiencies.

## EXAMINATION PROCEDURES

### LEVEL I

WKP. REF.

1. Review any written enforcement action that is in effect between the association and OTS, FDIC, or state supervisory authorities, if applicable.

- 
2. Review the ECEF "Actions History" report on the Intranet for any open enforcement actions associated with the association.

- 
3. Identify what the association or individual is required to do or is prohibited from doing by the enforcement action.

- 
4. Evaluate how the association monitors compliance with enforcement actions. Assess how the association communicates with officers and employees and determine whether the appropriate employees are aware of any corrective action needed.

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5. Review the appropriate areas of concern to determine whether or not the association or individual is in compliance with the provisions of the enforcement action. Work papers should fully support all conclusions.
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<b>Exam Date:</b>	
<b>Prepared By:</b>	
<b>Reviewed By:</b>	
<b>Docket #:</b>	

# Enforcement Actions Program

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WKP. REF.

6. If compliance is determined, summarize the findings, including comments for the report of examination (ROE) as necessary.
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7. If noncompliance is found, proceed to Level II procedures.
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8. Discuss overall examination findings with the examiner-in-charge (EIC).

- If a composite rating of 3, 4, or 5 is anticipated, determine what enforcement action(s), if any, is(are) necessary.
  - Document your decision and proceed to Level II procedures.
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## LEVEL II

1. Determine if there is another regulatory agency that is the primary regulator of the entity from whom you must obtain information. If so, work with your regional office staff to coordinate your information requests and any examination of a functionally regulated entity.
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2. If documents required by the enforcement action, such as an appraisal or financial statements, cannot be located, request them in writing from management. If you fail to receive the requested material, request a written response. If management will only respond orally, assure that two examiners are present and immediately write a summary of the response signed by both examiners.
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<b>Exam Date:</b>	
<b>Prepared By:</b>	
<b>Reviewed By:</b>	
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# Enforcement Actions Program

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WKP. REF.

3. Gather documents or materials that support the noncompliance such as poor appraisals, modified notes, loan register, loans in process ledger, etc. Separate and identify all appropriate work papers, ensuring they are factual, complete, and do not contain expressions of examiner opinion.
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4. Assess whether noncompliance is due to the association's administrative oversight, lack of knowledge, or willful disregard. State facts, be objective, and avoid speculation.
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5. Formulate recommendations for any necessary supervisory action. State the facts such as whether a previous supervisory agreement is violated and recommend an appropriate enforcement action such as a cease & desist (C&D) or assessment of a civil money penalties (CMP).
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6. The EIC must notify the regional office's legal staff by telephone and report the findings, recommending any further enforcement action.
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7. Per discussion with EIC or regional office staff, write an interim report detailing your findings.
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8. Prepare all comments and conclusions for the ROE as necessary.
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## EXAMINER'S SUMMARY, RECOMMENDATIONS, AND COMMENTS

<b>Exam Date:</b>	
<b>Prepared By:</b>	
<b>Reviewed By:</b>	
<b>Docket #:</b>	



## PROMPT CORRECTIVE ACTION GUIDELINES

The PCA statutory, regulatory, and policy framework provides OTS with effective supervisory remedies to minimize losses to the deposit insurance fund.<sup>1</sup>

The statutory authority for PCA is found in the Federal Deposit Insurance Act (FDIA) at 12 USC 1831o. OTS has implemented that authority in regulations at 12 CFR Part 565. PCA requires that certain operating restrictions take effect when an association is undercapitalized. The statute creates five capital categories, which are defined as follows by OTS at 12 CFR § 565.4(b) (consistent with the other banking agencies):

### PCA Categories

Savings associations fall into one of five PCA categories. The PCA minimum requirements are as follows:

	<u>Total Risk- Based</u>		<u>Tier 1/Risk- Based</u>		<u>Tier 1/Leverage</u>
Well Capitalized*	10% or greater	<i>and</i>	6% or greater	<i>and</i>	5% or greater
Adequately Capitalized	8% or greater	<i>and</i>	4% or greater	<i>and</i>	4% or greater (3% for 1-rated)
Undercapitalized	Less than 8%	<i>or</i>	Less than 4%	<i>or</i>	Less than 4% (except for 1-rated)
Significantly Undercapitalized	Less than 6%	<i>or</i>	Less than 3%	<i>or</i>	Less than 3%
Critically Undercapitalized	Has a ratio of tangible equity to total assets that is equal to or less than 2%. Tangible equity is defined in 12 CFR § 565.2(f) and differs from the definition of tangible capital under FIRREA.				

<sup>1</sup> OTS has additional powers under the Home Owners Loan Act (HOLA) for association's failure to meet capital requirements as detailed in the implementing regulation, 12 CFR 567.10. This document does not discuss the HOLA capital provisions and implementing regulations that are addressed in Handbook Section 120 Capital Adequacy.

\* To be well capitalized, association also cannot be subject to a higher capital requirement imposed by OTS.

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## Notice of Capital Category and Mandatory and Discretionary Operating Restrictions

OTS deems that savings associations have received notice of their capital category as of the date they file a Thrift Financial Report (TFR) or when OTS transmits a final report of examination (ROE). An association must also notify OTS of any event that results in the lowering of a PCA capital category within 15 days of the material event that caused the decreased capital (12 CFR § 565.3(c)(2)). In addition, OTS should provide written notice of an association's reclassified PCA status after receipt of a TFR, with the transmittal of a ROE, or upon learning of an event that results in a reclassification in capital category. The notice from OTS should include the mandatory and any discretionary operating restrictions (discussed below) applicable to associations in the designated category (see Chart 1 - PCA Categories). The restrictions are effective immediately upon the earlier of being deemed to have notice or receiving written notice of a capital category reclassification.

PCA requires OTS to apply progressively more significant restrictions on an association's operations as its capital category falls. PCA mandates the imposition of two restrictions once an association falls below the well capitalized category. First, no association can make a capital distribution or pay certain management fees if it results in its becoming undercapitalized. Second, the FDIC restricts associations from receiving brokered deposits unless they meet the well capitalized definition. The remaining mandatory operating restrictions apply to associations in the undercapitalized (or below) category.

For associations at the undercapitalized level and below, the additional mandatory operating restrictions include the following, found at 12 CFR § 565.6:

- Restricting capital distributions and certain management fees.
- Restricting asset growth.
- Limiting the ability to make acquisitions, branch, or enter new lines of business without prior agency approval.
- Compliance with a capital restoration plan submitted by the association.
- Requiring that OTS monitor the condition of the association.

All mandatory restrictions are effective immediately upon receiving or being deemed to have received notice of being less than well capitalized.

In addition to the mandatory restrictions, the PCA regulations provide OTS with authority to apply a wide range of discretionary remedies. Some of these provisions allow for directing changes in management should an association fall into the significantly undercapitalized level. OTS can mandate the election of a new board of directors, dismiss current directors and members of senior management, and require the hiring of certain qualified employees (subject to OTS approval) deemed necessary for safe and sound operations (12 USC 1831o(f)(2)(F); 12 CFR §§ 565.6 and 565.9). Other discretionary remedies include restrictions or bans on certain types of lending, limits on bonuses, prior approval of certain contracts, and other restrictions that OTS deems appropriate.

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If an association remains critically undercapitalized for ninety days, OTS must appoint a receiver or a conservator, or take such other action approved by the FDIC. (Capital failure as defined under the PCA statute is just one of the grounds for placing an association under a conservator or receiver.)

Even when savings associations are well capitalized or adequately capitalized under the PCA statute and regulations, OTS may exercise other authority to restrict an association's operations when capital levels are not commensurate with its balance sheet risk. OTS may use Individual Minimum Capital Requirements, Part 570 Compliance Plans, Supervisory Agreements, and/or Cease and Desist Orders.

### Capital Restoration Plan

In addition to the mandatory and discretionary operating restrictions, the FDIA requires all savings associations below adequately capitalized to submit a capital restoration plan (Capital Plan) within forty-five days of their receiving notice or being deemed to have notice of becoming undercapitalized. This section discusses the contents and approval of a Capital Plan in detail.

OTS regulations explain the timing, content, and approval standards for Capital Plans at 12 CFR § 565.5. The agency may alter the timing with proper cause.

Pursuant to agency policy, the Capital Plan must explain in detail the proposed strategy for becoming, at a minimum, adequately capitalized and for accomplishing the association's overall objectives. The plan should include:

- A detailed discussion of the following information:
  - The steps the association will take to become adequately capitalized, including underlying assumptions and proposed strategies.
  - Methodologies for forecasting the disposition of problem assets and the levels of expected charge-offs.
  - Any substantial changes in assets and liabilities.
  - The types and levels of activities in which the association plans to engage.
  - Strategies to control operating expenses, interest-rate risk, credit risk, and other significant risk exposures.
- Quarterly financial projections that generally follow the TFR, extending four quarters beyond the date the association becomes adequately capitalized. The projections should show the following information:
  - Progressively higher capital levels for complying with adequately capitalized standards.
  - Levels of core and net earnings.
  - Any capital infusions (specific steps must be taken within six months of becoming undercapitalized).

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— Compliance with applicable statutory or regulatory restrictions and OTS policies.

The association must base its projections on the following realistic assumptions and rates:

- Current Treasury rates and the implied interest rate forecast embedded in the existing yield curve for Treasury securities, with spreads over Treasuries on incremental assets and liabilities consistent with prevailing market spreads.
- Prepayment rates that reflect the market's consensus estimate for similar mortgage loans.
- Loan origination rates using recent experience and taking into consideration current national and regional economic conditions.
- The association may use OTS's quarterly updates on interest rates. The association can request a copy from the OTS Regional Office shortly after each quarter-end.
- A standard form of guarantee and assurance from all controlling companies, as required under 12 USC 1831o. In a tiered holding company structure, each controlling company must provide a standard form of guarantee and assurance signed by a majority of the board of directors or a duly authorized official. The guarantee does not supersede any existing capital maintenance agreements. A copy of the standard form can be obtained from the Chief Counsel's Office.
- A commitment in the Capital Plan to provide the Regional Director with quarterly variance reports comparing actual results to projected targets established in the Capital Plan within 30 days (or sooner if the association drops another PCA Capital category) following the close of each calendar quarter. OTS will condition approval of the plan upon submission of these variance reports. Failure to file required variance reports may result in enforcement action including civil money penalties. Material variances are grounds for terminating a Capital Plan approval.

After receipt of the Capital Plan, OTS has 60 days to review the contents and decide whether to approve or deny. If the association is critically undercapitalized, the FDIC will conduct a joint review of the proposed Capital Plan. By statute, 12 USC 1831o(e)(2), each agency must consider the following factors in determining whether to approve the plan:

- Does the Capital Plan specify the following information:
  - The steps proposed by the association to become adequately capitalized and the anticipated capital levels for each quarter contained in the plan.
  - How the association will comply with the restrictions and requirements under the FDIA.
  - The types and levels of activities that the association proposes to engage in, and such other information OTS may require.
- Has the association based its Capital Plan on realistic assumptions and is it likely to succeed in restoring the association's capital?

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- Does the Capital Plan demonstrate that the plan will not appreciably increase the association's exposure to risk (including credit, interest-rate, and other types of risk)?
  - Does each controlling company of the undercapitalized association:
    - Guarantee that the association will comply with the plan until adequately capitalized (on average) during four consecutive quarters?
    - Provide appropriate assurances of performance?

### PCA Directive

Whether or not OTS approves the Capital Plan, OTS regulations mandate issuing a directive to take prompt corrective action (12 CFR § 565.7 (PCA Directive)).

If the Regional Director approves the Capital Plan submitted by the association then it becomes the basis for the PCA Directive along with any mandatory or discretionary operating restrictions applicable to the association (as discussed above). If the Regional Director determines that the association's Capital Plan is not acceptable or it fails to file one, the PCA Directive becomes the basis for imposing the mandatory and discretionary restrictions and directing the steps necessary to either increase capital to acceptable levels or otherwise move the association toward resolution.

The sequence for issuing the PCA Directive is as follows:

- Within 15 days of reviewing and either approving or denying the association's Capital Plan, OTS will issue a "Notice of Intent to Issue a PCA Directive" providing the association with a copy of the proposed PCA Directive and allowing the association 14 calendar days to respond. OTS may shorten the 14-day period if the association's financial condition, or other circumstances, warrants.
- The notice of intent should state either that OTS is proposing to issue the directive in conjunction with approval of the Capital Plan, or that the association has not submitted an acceptable Capital Plan under the standards of PCA. It should also state that OTS has issued the Directive to carry out the purpose of PCA to resolve the association's problems at the least possible long-term loss to the deposit insurance fund.
- After reviewing the association's response to the proposed PCA Directive, OTS should make any appropriate revisions.
- Within the 15 days of issuing the Notice of Intent, OTS should provide the association with the "Stipulation and Consent to the Issuance of a PCA Directive" for signature by the association's board of directors.
- Upon receipt of an executed "Stipulation and Consent," OTS should then issue a final PCA Directive that requires compliance with the mandatory PCA sanctions and any discretionary PCA restrictions deemed appropriate. OTS may issue an immediately effective PCA Directive even if

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the association declines to execute the “Stipulation and Consent.” OTS can make the Directive effective upon issuance, or within a specified amount of time thereafter.

- In unusual circumstances, where immediate effectiveness of the PCA Directive is crucial, OTS may issue a PCA Directive without prior notice. To do so, OTS must document that immediate effectiveness is necessary to achieve the purpose of PCA. When we issue an immediately effective PCA Directive, the association has 14 calendar days to submit a written appeal and OTS has 60 days to decide whether or not to modify the PCA Directive. The OTS’s PCA regulation permits shortening of the 14-day response period if the financial condition of the association or other relevant circumstances warrants. The shortened period should allow sufficient time to make a meaningful response (12 CFR § 565.7). OTS should document in the official file when it shortens the response period.

### PCA Reclassifications

In certain situations, the statute allows OTS to reclassify a well capitalized association as adequately capitalized or subject an association to the supervisory actions applicable to the next lower capital category (together, “reclassification”).

OTS may reclassify a well capitalized association as adequately capitalized or may subject an adequately capitalized or undercapitalized association to the supervisory actions applicable to the next lower capital category if OTS determines that the savings association is in an unsafe or unsound condition or OTS deems the savings association to be engaged in an unsafe and unsound practice and not to have corrected the deficiency (12 USC 1831o(g); 12 CFR § 565.8). Once OTS determines that a capital category reclassification is appropriate, all of the mandatory and any appropriate discretionary restrictions for that capital category apply to the association.

Before reclassifying an association’s PCA capital category, OTS must specify its grounds for doing so and serve the association with a Notice of Intent to Reclassify. The Notice should include the following items:

- A statement of the association’s capital measures and capital levels and the proposed reclassified capital category;
- The reasons for reclassification of the association; and
- The date that the association may file a written appeal of the proposed reclassification and a request for a hearing, which shall be at least 14 calendar days from the date of service of the notice unless OTS determines that a shorter period is appropriate in light of the financial condition of the savings association or other relevant circumstances.

In the written response, an association may request an informal hearing and if it desires to present oral testimony or witnesses rebutting the reclassification the association shall include a request to do so with the request for an informal hearing (12 CFR § 565.8(a)(5)(6)). An association that has been reclassified can petition OTS for a PCA category upgrade once it has successfully rectified the unsafe and unsound conditions. An association’s failure to file a written response with OTS within the prescribed timeframe

shall constitute the association's consent to the reclassification and a waiver of the opportunity to respond.