Enhanced Framework for Supervising the U.S. Operations of Foreign Banking Organizations

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Section 2000.1

Foreign banking organizations ("FBOs") conduct an extensive and diverse business in the United States. Consistent with economic efficiency and national treatment, FBOs are free to conduct their U.S. activities through a variety of legal entities. Banking activities are conducted primarily through branches or agencies licensed by the individual states or by the Comptroller of the Currency and, to a lesser extent, through banks chartered by those banking supervisory authorities and through special-purpose banking corporations chartered by the states and the Federal Reserve. Some of these banking entities also are insured and therefore subject to the oversight of the Federal Deposit Insurance Corporation. Non-banking activities are authorized by the Federal Reserve pursuant to the Bank Holding Company Act and the International Banking Act. In addition, the Federal Reserve shares supervisory responsibility with other regulatory agencies for FBOs with respect to the business they conduct within the United States, including representative offices. As a result, FBOs are subject to a number of state and federal statutes, and various aspects of their operations are supervised and regulated by both state and federal banking supervisory authorities.

In order to better coordinate and further enhance the supervision of the U.S. activities of FBOs, the banking supervisory authorities that have supervisory and examination powers over the U.S. operations of FBOs have developed a program encompassing the supervisory principles and processes relating to FBOs, which is summarized in the following sections.

OVERVIEW

The strength-of-support assessment (SOSA) provides a general framework for evaluating and assimilating significant financial and managerial information related to individual foreign banking organizations (FBOs) in order to assign a two-component SOSA. The FBO assessment provides information to the supervisory agencies that is taken into account in reaching decisions regarding the scope and frequency of examinations and other appropriate supervisory initiatives. The assessment also provides a basis for the more efficient utilization of supervisory resources.

The first component of the SOSA addresses whether any factors relating to the ability of the FBO to meet its U.S. obligations warrant special monitoring of the FBO's U.S. operations. This component is a reflection of the overall financial viability of the FBO as well as several external factors such as the degree of supervision the FBO receives from its home country supervisor. This component is based on a scale of "A" through "E" with "A" representing the lowest level of supervisory concern and "E" representing the highest.

Factors considered in assigning the first component include a review of the FBO's financial condition and prospects, the system of supervision in the FBO's home country, the record of home country government support of the banking system or other sources of support of the FBO, and any transfer risk concerns. In assigning this component, all relevant factors are weighed and evaluated. Standards and criteria for this component, including the five possible strength-of-support indicators, are discussed in greater detail below.

The second component of the SOSA, which is utilized on an as-needed basis, identifies whether there are any factors that raise questions about the ability of the FBO to maintain adequate internal controls and compliance procedures at its U.S. offices, irrespective of the overall financial condition of the FBO. If any such control risks are apparent, an asterisk is placed next to the letter component of the SOSA.

Factors considered in assigning the asterisk include the FBO's managerial and operational record and whether current activities such as a recent merger, significant other expansion or changes in operations, or reported control problems at non-U.S. operations pose a potential risk to the U.S. operations. The factors considered for this component also are discussed below. Specific standards or criteria for the second component of the SOSA are not discussed because the purpose of this component is to indicate whether any such concerns exist, a determination that is largely judgmental in nature and not readily quantified. For this reason, the asterisk is used rather than an alpha or numeric symbol which would incorrectly imply differing degrees of such concerns.

All SOSAs are for *internal supervisory use only* and are not disclosed to the general public or to FBO's management, either in the United States or at the head office or to the home country supervisor(s). If deemed appropriate, any specific concerns raised through the assessment process, rather than the assessment itself, will be communicated directly to the FBO's management and home country supervisor(s), particularly if those concerns lead to supervisory follow-up action with regard to the FBO's U.S. operations.

SOSA INDICATORS

There are five possible indicators for the first component of the SOSA:

Assessment of A—The FBO has a financial profile that is regarded as strong by both home country peer and international standards. It has superior risk-based capital ratios,[1] more than ample access to U.S. dollar funding, and, if rated by any of the ratings agencies, is accorded one of the two highest market or investment rating categories. Supervision by the home country supervisory agency or agencies is conducted on a comprehensive basis, covering the worldwide

1. Risk-based capital ratios based on Basle or EC criteria are available for most banks. For those banks not providing such ratios, judgments related to the adequacy of capital are based on the ratio of equity capital to total assets.

operations of the FBO and its affiliates.[2] The home country has a good record of supervising financial institutions and dealing with problem institutions, and transfer risk is not an issue of concern. The FBO is an unquestioned source of strength to its U.S. operations.

Assessment of B—The financial profile and outlook pose a low risk that the FBO will be unable to support its U.S. operations. The FBO is viewed as investment grade or equivalent, capital ratios are above internationally accepted minima, and access to U.S. dollar funding is readily available; however, financial factors are not as strong as those of institutions with an assessment of A. The FBO is subject to a significant degree of supervision of its overall operations by the home country supervisor(s) and the country has a good record for dealing with problems in the local financial system. Transfer risk factors are generally consistent with those of FBOs with an assessment of A. An FBO whose financial profile is consistent with a B assessment could be assigned an assessment of C or lower if its home country has a supervisory system that is lacking in significant respects or significant transfer risk considerations exist.

Assessment of C—The current operating performance of the FBO and its immediate financial outlook, although not posing significant concerns about the ability of the organization to honor its U.S. liabilities, may warrant more than normal review based on such factors as the lack of an investment grade rating, capital ratios below internationally accepted minima, or other factors that are considered less than adequate by international standards. While the FBO currently may not meet all international financial standards, the home country has demonstrated an ability and willingness to support the FBO or similar financial institutions.

Conversely, the financial profile of the FBO may appear to warrant a stronger rating; however, supervision by the home country regulators is lacking in significant respects or significant transfer risk considerations exist.

2. This covers instances in which a determination regarding comprehensive, consolidated supervision has already been made by the Federal Reserve Board or where Board staff, based on available information, are prepared to make a positive recommendation to the Board with regard to comprehensive, consolidated supervision.

Assessment of D—Significant financial or supervisory weaknesses are apparent such that imposition of asset maintenance requirements on the U.S. branches and agencies should be considered. The FBO may be expected to continue as a going concern due primarily to government support, ownership, or other significant factors, although resource constraints, transfer risk considerations, operating structure, or other factors may place important limitations on that support. Conversely, the financial profile, based on available information, may imply a higher assessment, but home country supervision is deemed to be substantially or wholly deficient, or there are significant transfer risk concerns.

Assessment of E—Due to a seriously deficient financial profile and/or poor operating practices and the absence of any sufficient supervisory oversight and support, there is a strong possibility that the FBO will be unable to honor its U.S. obligations in the near future or is otherwise considered to present a hazard to U.S. financial markets.

SOSA FACTORS

Determining whether an individual FBO has the internal or external resources to provide the necessary financial or managerial support to its U.S. operations depends to a great extent upon its financial condition, operating record, and general outlook. A good financial condition combined with capable management is generally sufficient to ensure that support. However, the degree of certainty about the ability of an FBO to provide any necessary financial support may be limited by weaknesses in its home country supervisory system or a significant degree of transfer risk associated with its major operations. These two factors also may influence the home country's record of support for its financial institutions.

Accordingly, the first component of the SOSA considers four major factors: (a) the financial profile of the FBO based on its present financial condition and outlook, including capital ratios and access to U.S. dollar liquidity; (b) the FBO's home country banking supervision system; (c) the demonstrated capabilities of the home country in dealing with banking problems; and (d) the degree of transfer risk associated with the FBO's home country and any other countries in which the FBO has major operations.

All assessment factors are considered as a whole in assigning the first component of the SOSA. None of the four principal factors are assigned a separate ''rating'' or are considered a discrete component of the final assessment.

Financial Profile

The financial profile of the FBO is based on the institution's current condition and future prospects. A review of financial condition is based on the level and trend in financial performance indicators relating to the FBO's capital, profitability and asset quality. These indicators should be evaluated in the context of peer performance and knowledge of the FBO's home country financial system and accounting policies and practices.[3] The financial outlook should consider a broad range of external and internal factors, such as the home country banking system, the FBO's political and economic environment, its market position, risk profile, ownership, and management.

Generally, the FBO's short-term and long-term market ratings are good indicators of its financial outlook. An FBO with the highest market ratings should be able to demonstrate a strong financial condition and outlook. The FBO would likely be assigned an A assessment if other factors are consistent with the assessment. Notwithstanding the significance of market ratings, the FBO's financial profile and resultant assessment should not be based on market ratings alone. Rather the ratings should serve as a reference point for the independent assessment of the institution, because market ratings may not always reflect the most current view of the FBO or the supervisory authorities may have information not directly or indirectly available to the market. For example, examination findings of the U.S. operations could raise questions about the FBO's overall operations and management that could lead to a SOSA lower than that indicated by the FBO's market ratings. However, any significant difference between the assessment and market ratings should be fully analyzed and justified.

3. While recognizing that in many cases knowledge of this nature will take time to develop, it is particularly important because financial disclosure varies among countries. For this reason, meetings with head office management and the home country supervisors of FBOs are useful sources of information.

System of Home Country Supervision

A review of the home country supervisory system is essential to ensure that the FBO is subject to an appropriate level of supervision of its global operations. In assigning an FBO'S SOSA, the review of the system of home country supervision should concentrate on its general policies and how the supervisory framework applies in practice to the individual FBO. In this context, the mere presence of a home country supervisor is not considered sufficient.

The FBO's home country supervisory system should be evaluated based on those general principles and practices that ensure regulatory monitoring over the FBO's principal operations and activities, including those outside the home country. These general supervisory principles and practices usually include some level of periodic reporting, on-site and/or off-site review, prudential guidelines (including capital adequacy requirements), and supervisory enforcement powers. Effective regulatory systems may take many forms; however, the system of any country should ensure that the internationally active banks operating under that system are subject to a sufficient level of supervision.

Supervisory systems may also vary with respect to the type of institution. Therefore, the analysis of the supervisory system should evaluate actual regulatory practices for the individual FBO. This assessment will be based largely on the information that has been accumulated over time by the U.S. banking supervisory agencies. It is expected that this assessment will be enhanced as additional information on other supervisory systems is obtained through improved contacts and informational exchange.

Record of Home Country Support

Related to home country supervision is the matter of the home country's record of ensuring the solvency of its financial institutions, particularly those that operate internationally. The record of support varies by country with respect to structure, coverage of banks, and resources. Such support may be either direct or indirect in nature and may be widespread or only applicable to banking institutions with specific characteristics.

Some countries are able to take whatever steps are necessary to support their banks unequivocally while others will have a more limited degree of support for their banks due to legal restrictions or financial constraints. These factors should be reviewed, giving particular emphasis to past performance and an assessment of the country's resources.

Level of Transfer Risk

Transfer risk, which relates to the FBO's ability to access U.S. dollars, is an essential factor in determining whether the FBO can support its U.S. operations. For some FBOs, transfer risk is increased due to heavy debt servicing or other financial restraints relating to the home country, which often leads to exchange controls and hard currency restrictions. As a result, these FBOs may be limited in providing necessary support to their U.S. operations.

The assessment of transfer risk for individual countries is uniformly handled by U.S. regulators through the Interagency Country Exposure Review Committee (ICERC). These ICERC assessments can therefore be used in determining the SOSAs. For those countries not evaluated by ICERC, the assessments of transfer risk will made in the same manner as conducted by ICERC.

Generally, FBOs from countries rated substandard or worse would be accorded an assessment of no better than C. However, a high level of transfer risk associated with the FBO's home country could be mitigated by other considerations that clearly indicate that the FBO has broad access to U.S. dollars.

Other Factors

Determining whether an FBO poses any managerial or operational control risks to its U.S. operations can be influenced by a broad range of factors that are generally more subjective than those discussed under the first component of the SOSA. Any such risks, both actual and potential, which do not directly relate to the ability of an FBO to meet its obligations as discussed earlier, should be denoted by placing an asterisk beside the FBO's letter assessment. The nature of these risks should be discussed separately in the FBO evaluation.

One example of such control risks is an FBO that otherwise has a SOSA of A or B but may be experiencing certain operational problems, not necessarily in the United States. The FBO may be undergoing extensive expansion into new markets or products that over time could pose a strain on its financial and managerial resources. The FBO also could be experiencing well-publicized internal control problems at offices outside the United States. Although these control problems would not necessarily affect the ability of the FBO to pay its obligations, they may be symptomatic of larger control problems that also might exist in the U.S. offices. Any such concerns should be explored to the extent possible, particularly as they may influence the examination plan for the FBO's U.S. operations.

GENERAL SUPERVISORY IMPLICATIONS

As discussed earlier, one of the principal goals of the SOSA is to identify those FBOs that may pose risks to their U.S. operations or to U.S. financial markets due to financial, operational, or other concerns at the FBO as a whole. The SOSA serves to categorize all FBOs conducting banking operations in the United States and to highlight those FBOs warranting higher levels of supervisory attention with respect to their U.S. operations. This assessment may influence the examination plan and potential supervisory follow-up actions for the FBO's U.S. operations.

An FBO's SOSA is taken into consideration in setting the examination plan for the FBO's U.S. operations. The examination plan considers any issues raised in the assessment process and addresses them accordingly. For example, the U.S. operations of FBOs whose assessments are marked by an asterisk may have examinations that specially target operational or management areas. The FBO's SOSA is also a factor in determining whether the FBO will be subject to a simultaneous examination.

The FBO's SOSA also is considered in implementing supervisory follow-up action for the U.S. operations. Generally, an assessment of C or worse would imply a level of concern that would subject the FBO's U.S. offices to at least periodic monitoring of their due to/due from positions. Any additional supervisory steps, such as imposing an asset pledge or asset maintenance requirement, would be implemented largely based on the condition and nature of the U.S. operations. An FBO accorded an assessment of D or worse indicates a higher level of concern with some presumption of asset maintenance regardless of the condition of its U.S. operations.

As with all such supervisory follow-up actions, these steps are considered and implemented based on the general criteria for applying supervisory follow-up actions in the context of the FBO's SOSA. Supervisory follow-up action can be modified based upon a number of criteria. It is stressed that no automatic supervisory program is mandated as part of the FBO SOSA. Furthermore, an assessment of A or B generally would imply little if any concern relating to the ability of the FBO to meet its obligations. If an FBO does raise liquidity or solvency concerns, the FBO should not be accorded an assessment of A or B.

Suggested guidelines for supervisory follow-up action for each assessment category are as follows:

A or B Assessment—Normally, any supervisory follow-up action for FBOs with a SOSA of A or B is applied only if warranted by the condition of the U.S. operations. Supervisory measures generally would not relate to liquidation concerns. As such, asset maintenance usually would not be required for branches and agencies of these FBOs; however, supervisory actions would be undertaken, if necessary, to resolve any significant deficiencies in risk management, operations and internal controls, or compliance at any of the U.S. offices.

C Assessment—The FBO's SOSA is reviewed at least annually. The due to/due from position is closely monitored and any substantial due from position is fully analyzed for risk implications. If warranted by the condition of the combined U.S. operations or the asset quality at the U.S. offices of such an FBO, asset maintenance would be considered for branches and agencies, and U.S. subsidiary banks could be required to operate at capital levels above the minima.

D Assessment—There is a strong presumption of asset maintenance for branches and agencies of an FBO in this category, and U.S. bank subsidiaries should operate at strong capital levels. The FBO is more closely monitored and its assessment may be subject to review at least semi-annually.

E Assessment— The FBO will be placed under continuous surveillance and reporting as warranted. Termination proceedings for the U.S. operations of such an FBO will be considered under applicable regulatory guidelines.

DEVELOPING THE SOSA

The FBO's SOSA is developed annually through a process that involves all U.S. supervisors that have licensing, chartering, or examining responsibilities over the FBO's U.S. operations. The process includes an analysis of available information on the financial condition of the FBO within the context of the home country financial system, the banking supervisory system, the record of the authorities in preventing or successfully dealing with banking system problems, and transfer risk considerations. The FBO evaluations are based on information compiled by all of the relevant U.S. banking supervisory agencies.

Information obtained by any of the banking supervisory agencies relating to individual FBOs, their home country financial systems, supervisory systems and accounting policies should be transmitted to the Federal Reserve, which will assume responsibility for organizing and maintaining a database for this information. This database is available to all of the relevant U.S. banking supervisory agencies.

All of the relevant state and federal banking supervisory agencies, whenever possible, will obtain information for the database, especially as it relates to the individual FBOs, the financial systems within which they primarily operate and the supervisory systems in the different countries. This information will help to keep the database as current as possible and is developed primarily through discussions with the U.S. and head office managements of the FBOs as well as the home country supervisor(s).

PRIMARY PRODUCTS

The information in the database is used to develop three primary products, each of which summarizes information in the database and provides the supporting data for the SOSA. These three products are: (1) an evaluation of the financial condition of the FBO, (2) a review of the home country financial system, and (3) a review of significant home country accounting policies and practices.

Evaluation of the Financial Condition of the FBO

Normally, the FBO evaluation is drafted by the Federal Reserve each year. The initial source of information for the evaluation is the FR Y7 report as well as any external sources that are readily available (e.g. periodicals and services). Over time, as the database becomes more developed, many additional sources of information will be utilized.

The individual Reserve Banks responsible for drafting FBO evaluations produce a schedule at the beginning of each year showing the approximate date that the draft evaluation and recommended SOSA for each FBO will be circulated for comments. This schedule is based primarily on the fiscal year-end of the FBO (and consequently the date the FR Y7 report is received), the extent and overall condition of the FBO's combined U.S. operations, and the prior SOSA of the FBO. This schedule is distributed to all of the state and federal agencies participating in this joint program along with the name of a contact person at each Reserve Bank. The other agencies, as well as the other Reserve Banks, may request, through the assigned contact person, that an FBO evaluation in any given year be given a higher priority than the schedule indicates.

The draft evaluation and the proposed SOSA is circulated for comments within the Federal Reserve System and to all federal and state supervisory agencies involved in supervising the FBO. Each party reviews the draft and comments, if necessary. In addition, the analyst who prepared the draft will be available to answer questions regarding the draft. If the initial review of the draft indicates differences in view regarding the proposed assessment that can not be resolved informally, a meeting of the relevant banking supervisory agencies could be called by any supervisory agency to discuss the SOSA of the FBO. While it is expected that a consensus assessment will result from this process, individual agencies retain the right to exercise all statutory authorities available to them to meet their supervisory concerns.

The finalized evaluation is sent to all of the supervisory agencies involved in the supervision of the U.S. operations of the FBO. The evaluations and assessments normally are reviewed annually. The evaluations will be revised in the interim only if information is obtained by any of the U.S. supervisory agencies that is significant enough to change the SOSA, either positively or negatively.

These evaluations are kept strictly confidential by each of the agencies, in part to ensure that the sharing of information between the agencies for purposes of analyzing the condition of the FBO and assigning its SOSA does not violate state or federal regulations.

Review of Home Country Financial System

As mentioned above, a database containing information on the financial system of each country with bank representation in the United States is maintained by the Federal Reserve, using its own sources and information submitted by the other supervisory agencies. This information is made available to all of the agencies. In addition, the Federal Reserve provides, in a uniform format, reviews summarizing information on the home country financial system, the nature of banking supervision and the country's record in dealing with banking problems.[4] These reviews are updated whenever any of the supervisory agencies obtain significant information regarding the financial system of the particular country. The database includes all such reviews prepared by the Federal Reserve and any provided by the other supervisory agencies.

Review of Home Country Accounting Practices

The database also contains information on significant accounting policies and practices in other countries and is utilized to develop reviews of such practices. These reviews are developed by the Federal Reserve utilizing information

4. These reviews are produced based on a schedule provided by the Reserve Banks. The schedules give priority to those countries that have a major banking presence in the United States or are experiencing significant problems within the home country financial system. The draft is provided to the other agencies for their comments. The analyst who prepared the draft is available to answer questions regarding the draft.

derived from the same sources as used for the review of the home country financial system as well as from general accounting information provided in the FR Y7 report. These reviews are updated whenever any significant changes occur in accounting policies or practices.

OVERVIEW

This segment of the program is designed to provide a more efficient, rational, and uniform approach to supervising the U.S. operations of foreign banking organizations (FBOs), particularly those that operate in the United States through numerous entities and across multiple jurisdictions. In order to ensure coordination of supervisory efforts and avoid duplication, the U.S. banking supervisory agencies communicate with each other to a greater extent regarding their examination plans, examination results, and, where applicable, their proposed supervisory follow-up actions. In addition, the Federal Reserve assesses annually the combined U.S. operations of each FBO, based largely on input from and discussions with the examining agencies.

EXAMINATION SCHEDULING AND DEVELOPMENT OF EXAMINATION PLANS

FBSEA requires that each U.S. branch and agency of an FBO be subject to one safety and soundness examination in each twelve month period. More frequent examination may be warranted in certain situations.[1]

To ensure coordination, the licensing and insuring agencies provide the local Federal Reserve Bank with a copy of their preliminary examination schedule for the coming year for all U.S. offices of an FBO for which the agency anticipates conducting an examination. The Federal Reserve uses these schedules, along with the preliminary examination schedules of the various Reserve Banks, to derive a draft comprehensive examination schedule for all U.S. operations of individual FBOs.

The draft schedule is provided to each involved agency in order to permit all of the examining agencies to review their own schedules in conjunction with those of the other agencies. In addition, where necessary, an interagency scheduling meeting takes place each year to determine the scope and timing of examinations of FBOs that are to be conducted on a more coordinated basis. The Federal Reserve finalizes the comprehensive examination schedule and provides it to all of the supervisory agencies.

For FBOs that conduct all or substantially all of their U.S. operations through entities licensed or chartered by one banking supervisory agency, the timing of the annual examination is established by the licensing authority. In agreement with the individual states, the Federal Reserve and, for insured branches, the FDIC, share the burden of conducting the annual examinations of state-licensed branches and agencies. In those years that the Federal Reserve or FDIC conduct the examination, the timing will be established by that agency.

FBOs which operate in the United States through multiple offices often will have all offices examined using the same ‘‘as of’’ financial statement date. This provides the supervisory agencies with increased information on the interrelationships among the various offices and can enhance the examination of individual offices and the FBO’s overall U.S. operations. These examinations are conducted by the various agencies.

Sometimes, certain activities of a branch are functionally managed or operationally performed at the branch being examined, but are booked at another office of the FBO, either in the U.S. or offshore. It is not uncommon for one branch to generate, or be responsible for loans, trading assets, or deposits that are ultimately booked at another office. Similarly, it also is not uncommon for a branch to perform certain operations such as electronic data processing, accounting, financial reporting, or credit administration on behalf of another office of the FBO. Even when a U.S. branch performs limited operational functions for a related office, examiners should evaluate whether the branch has sufficient records and controls in place to execute the delegated responsibilities. If there is insufficient information to evaluate the nature of and the performance of the U.S. branch with respect to the business relationship with another office of the FBO, examiners should cite this deficiency in the report of examination as a matter that requires immediate attention.

1. Under legislation passed in 1996, branches and agencies that meet certain size and other criteria may be examined once in every 18 month period. Those criteria currently are under development and further guidance will be issued.

SR 96-36 provides detailed guidance on how to review duties performed by one branch on the behalf of another. Essentially, a branch performing duties on behalf of another office of the FBO should have adequate policies, procedures, and documentation to clearly delineate the oversight, operational, and control responsibilities of the branch. There should be adequate risk management processes, operational controls, and compliance programs covering all activities for which the branch has responsibility. The examination treatment under the ROCA rating system for activities conducted by a U.S. branch on behalf of another office of the FBO should be the same as for activities conducted by the branch for its own book, except for the evaluation of asset quality. In rating asset quality, the examiner should only evaluate assets that are on the books of the U.S. branch. However, examiners should be mindful of the general quality of assets being generated by the U.S. branch and booked elsewhere so as to be alert to any pattern of booking low quality assets outside the U.S. or any other situations that might indicate problems in risk management or operational controls.

EXAMINATION PLAN

Subsequent to the examination scheduling process, detailed examination plans are developed, exchanged and coordinated among the examining agencies. Each state and federal supervisory agency participating in this program is committed to developing, to the extent possible, examination plans for individual offices of FBOs that they plan to examine based primarily on the following:

- findings and scope of previous examinations;
- the results of any off-site surveillance;
- the latest assessment of the combined U.S. operations of the FBO and the role of the office in the context of the FBO’s overall U.S. business activities;
- results of meetings with both U.S. and head office management of the FBO, and the home country supervisor(s); and,
- the evaluation of the FBO and the SOSA assigned.

A comprehensive examination plan (‘‘Exam Plan’’) is developed annually for each FBO with banking offices licensed by more than one supervisory agency and/or with significant U.S. non-banking activities. The Federal Reserve drafts the comprehensive Exam Plan based on the individual examination plans prepared by the different state and federal supervisory agencies for each office to be examined. These examination plans should be developed after the regulatory agency has completed its most recent examination of the FBO entity subject to its supervision. The plan should be incorporated into the confidential section of the examination report. After conferring with other participating banking supervisory agencies, the scope or timetable of an examination, as set out in the annual comprehensive Exam Plan, may be altered in the event there are impediments to completing an examination as originally planned.

IMPLEMENTING THE ANNUAL EXAMINATION PLAN

The Federal Reserve coordinates the sharing of information throughout the examinations of FBOs with multi-state operations. Because of the differing starting dates and lengths of individual examinations, most examinations are completed by participating banking supervisory agencies at different times. Consequently, an important part of this program is the sharing of critical examination findings throughout the process. The U.S. supervisory agencies have committed to advising those agencies responsible for examining other U.S. offices of the FBO of any *critical* examination findings prior to the exit meeting for that examination.

The Federal Reserve, in its statutory role as umbrella authority with responsibility for overall U.S. operations, confers with the examining agencies to determine if its participation in any of the examiner closeout meetings is warranted. Such participation typically is appropriate in the event there are systemic weaknesses detected in the U.S. operations or problems exist that are so significant as to affect the rating of the overall U.S. operations. In those instances where a Federal Reserve Bank has conducted the examination, that Reserve Bank confers with the licensing agency to determine if the participation of that agency is warranted. However, the normal presumption is that the banking supervisory agency that conducted the examination also will conduct the closeout meeting without participation by non-examining agencies.

The agency responsible for the examination of any office in a given year is also responsible for completion of the examination and preparation of the examination report for that entity. In the case of joint examinations, the examining agencies strive to issue only one report of examination for that office of the FBO. The supervisory agency that conducted the examination of an individual office of an FBO also is responsible for the distribution of the transmittal letter and examination report.

Supervisory actions that affect only one office of an FBO also normally are entered into solely by the licensing authority, unless the action resulted from an examination conducted by the FDIC or the Federal Reserve. In these cases the action is undertaken by the examining agency or, at the option of the licensing authority, on a joint basis with that authority. Actions that apply to the overall operations of an FBO are entered into by the Federal Reserve and those licensing or insuring agencies that have offices affected by the supervisory action and wish to enter into such an action with the office they license.

ASSESSMENT OF COMBINED U.S. OPERATIONS AND ASSIGNMENT OF A RATING

An important component of this program is the integration of individual examination findings into an assessment of an FBO's entire U.S. operations. This assessment provides the FBO and the U.S. supervisory agencies with a view of the overall condition of the U.S. operations, and helps put into context the strengths and weaknesses of individual offices. It also highlights supervisory concerns regarding any problems that are pervasive in the U.S. operations of the FBO.

The Federal Reserve conducts an annual assessment of the combined U.S. operations and prepares a "Summary of Condition" for all FBOs with U.S. offices supervised by more than one agency. The summary includes an assessment of all risk factors, including (1) all elements of the ROCA rating system, (2) quality of risk management oversight employed by all levels of management in the FBO's U.S. operations, and (3) the examinations of all vehicles of the FBO conducted during the year. The Summary of Condition leads to the assignment of a single-component rating between 1 and 5 for the combined U.S. operations.

The Summary of Condition is drafted by the Federal Reserve which provides a copy of the draft and proposed rating to each supervisory agency with examination authority over an office of the FBO in order to make certain that information obtained from these agencies was correctly interpreted.

Once the Summary of Condition is finalized, the Federal Reserve provides a copy, including the rating, to the Chief Executive Officer at the head office of the FBO. The Summary of Condition and the rating serve as a starting point in drafting the Exam Plan for the next year.

In arriving at the rating for the combined U.S. operations of the FBO, all of the FBO's U.S. vehicles are considered; however, this rating is not based merely on an arithmetic average of the examination ratings of the vehicles examined. The strengths or weaknesses exhibited within individual entities are evaluated based on the size and importance of the entity relative to the FBO's entire U.S. operations, and the materiality and extent of the weaknesses.

The five ratings are defined as follows:

Combined Rating of 1—The overall operations are fundamentally sound in every respect. They cause no supervisory concern and require only normal supervisory attention.

Combined Rating of 2—The combined U.S. operations operate in a basically sound manner, but may have modest weaknesses that can be corrected by management in the normal course of business. They do not require more than normal supervisory attention.

Combined Rating of 3—Overall U.S. operations are weak in risk management, operational controls, and compliance, or have numerous asset quality problems that in combination with the condition of the FBO cause supervisory concern. U.S. and/or head office management may not be taking the necessary corrective actions to address weaknesses. This rating may also be assigned when either risk management, operational controls, or compliance is individually viewed as unsatisfactory. Generally, these operations raise supervisory concern and require more than normal supervision to address their weaknesses.

Combined Rating of 4—The combined U.S. operations have a significant volume of serious weaknesses. Serious problems or unsafe and unsound banking practices or operations exist, which have not been satisfactorily addressed or resolved by U.S. or head office management. These operations require close supervisory attention and surveillance monitoring and a definitive plan for corrective action by head office management.

Combined Rating of 5—The combined U.S. operations have so many severe weaknesses or unsafe and unsound conditions that they require urgent restructuring by head office management.

This composite assessment serves to apprise the various U.S. supervisory authorities of the condition of all the U.S. entities of individual FBOs. These agencies can then factor the information that they obtain from the Summary of Condition and the composite assessment into their supervision of the U.S. entities under their jurisdiction.

Rating System for U.S. Branches and Agencies of Foreign Banking Organizations

Effective date July 1997

Section 2003.1

The rating system for U.S. branches of FBOs is a management information and supervisory tool designed to assess the condition of a branch and to identify significant supervisory concerns at a branch in a systematic and consistent fashion. The rating system (ROCA) has been revised from the previous rating system of asset quality, internal controls, and management (AIM), to better assess the condition of a branch within the context of the FBO, of which it is an integral part, and to pinpoint the key areas of concern in a branch office.

For evaluation purposes, the rating system divides a branch's overall activities into three individual components: risk management, operational controls, and compliance. These components represent the major activities or processes of the branch that may raise supervisory concern. The rating system also provides for a specific rating of the quality of the branch's stock of assets as of the examination date.

COMPOSITE RATING

The overall or composite rating indicates whether, in the aggregate, the operations of the branch may present supervisory concerns and the extent of any concerns. While the individual component ratings are taken into consideration in arriving at the branch's overall assessment, the composite rating should not be merely an arithmetic average of the individual components. The examiner should assign and justify in the report a composite rating using definitions provided below as a guide.[1]

The composite rating is based on a scale of one through five in ascending order of supervisory concern. Thus, one represents the lowest level of supervisory concern while five represents the highest level. The five composite ratings are defined as follows.

Composite Rating 1

Branches in this group are strong in every respect. These branches require only normal supervisory attention.

Composite Rating 2

Branches in this group are in satisfactory condition, but may have modest weaknesses that can be corrected by branch management in the normal course of business. Generally, they do not require additional or more than normal supervisory attention.

Composite Rating 3

Branches in this group are viewed as fair due to a combination of weaknesses in risk management, operational controls, and compliance, or asset quality problems that, *in combination with* the condition of the FBO or other factors, cause supervisory concern. In addition, branch and/or head office management may not be taking the necessary corrective actions to address substantive weaknesses. This rating may also be assigned when risk management, operational controls, or compliance is individually viewed

1. Assessment of asset quality is an integral part of any examination; however, under certain circumstances, it may be appropriate to give the individual asset quality rating component greater or lesser weight in arriving at an overall composite rating. In ensuring the protection of branch creditors, an important factor is the strength of the FBO. As the financial strength of the FBO weakens, it becomes increasingly important to look to the quality of the assets booked in the United States as the source of protection for local creditors, and, at a certain point, asset maintenance should be imposed. Similarly, where the FBO is strong, and the need to look to local assets for protection of creditors seems remote, the relative weighing of the asset quality component in the overall evaluation diminishes.

It also should be recognized that different offices of the FBO can be assigned widely different roles in the FBO's overall strategy. Thus, an individual office that books very few loans, but is otherwise poorly managed should not be given undue credit for having good asset quality. Alternatively, a branch that is designated to hold problem assets generated by other offices of the FBO, in order to better manage the workout process, should not be penalized, so long as the FBO has the ability to support the level of problem assets.

Finally, it should be recognized that asset quality tends to be a ''trailing'' indicator of branch performance. In instances where risk management systems are weak, but problem assets are currently nominal, it is realistic to assume there will be future deterioration in asset quality. By the same measure, management should be given credit in the overall evaluation where the causes of past asset quality problems have been corrected.

as unsatisfactory. Generally, these branches raise supervisory concern and require more than normal supervisory attention to address their weaknesses.

Composite Rating 4

Branches in this group are in marginal condition due to serious weaknesses as reflected in the assessments of the individual components. Serious problems or unsafe and unsound banking practices or operations exist, which have not been satisfactorily addressed or resolved by branch and/or head office management. Branches in this category require close supervisory attention and surveillance monitoring and a definitive plan for corrective action by branch and head office management.

Composite Rating 5

Branches in this group are in unsatisfactory condition due to a high level of severe weaknesses or unsafe and unsound conditions and consequently require urgent restructuring of operations by branch and head office management.

DISCLOSURE

Following approval of the rating by appropriate senior supervisory officials at the examining agency, the numeric ratings for all components as well as the overall composite rating should be disclosed in the open, summary section of the examination report. This also applies when conducting meetings with senior management. In disclosing the rating, its meaning should be explained clearly using the appropriate composite rating definition. The report should also make it clear that the rating is part of the overall findings of the examination and is thus confidential. Any rating disclosed or discussed at an examination closeout meeting should be held out by the examiner-in-charge to be tentative.

COMPONENT EVALUATIONS

Similar to the composite rating, the individual rating components are evaluated on a scale of one to five, where one represents the lowest level of supervisory concern and five represents the highest. Each component is discussed below followed by a description of the individual performance ratings.

Risk Management

Risk is an inevitable component of any financial institution. Risk management, or the process of identifying, measuring, and controlling risk, is therefore an important responsibility of any financial institution. In a branch, which is typically removed from its head office by location and time zone, an effective risk management system is critical not only to manage the scope of its activities but to achieve comprehensive, ongoing oversight by branch and head office management. In the examination process, examiners will therefore determine the extent to which risk management techniques are adequate (i) to control risk exposures that result from the branch's activities and (ii) to ensure adequate oversight by branch and head office management and thereby promote a safe and sound banking environment.

The primary components of a sound risk management system are a comprehensive risk assessment approach; a detailed structure of limits, guidelines, and other parameters used to govern risk taking; and a strong management information system for monitoring and reporting risks.

The process of risk assessment includes the identification of all the risks associated with the branch's balance sheet and off-balance-sheet activities and grouping them into appropriate risk categories. These categories broadly relate to credit, market, liquidity, operational, and legal risks.[2] All major risks should be measured explicitly and consistently by branch management; risks should also be reevaluated on an ongoing basis as underlying risk assumptions relating to economic and market conditions vary and as the branch's activities change. The branch's expansion into new products or business lines should not outpace proper risk management or supervision by head office. Where risks cannot be explicitly measured, manage-

2. While operational risks are identified as part of the branch's overall risk assessment process, the effectiveness of the branch's operational controls is separately evaluated under ROCA.

ment should demonstrate knowledge of their potential impact and a sense of how to manage such risks.

Risk identification and measurement are followed by an evaluation of the tradeoff between risks and returns to establish acceptable risk exposure levels, which are stated primarily in the branch's lending and trading policies subject to the approval of head office management. These policies should give standards for evaluating and undertaking risk exposure in individual branch activities as well as procedures for tracking and reporting risk exposure to monitor compliance with established policy limits or guidelines.

Head office management has a role in developing and approving the branch's risk management system as part of its responsibility to provide a comprehensive system of oversight for the branch. Generally, the branch's risk management system, including risk identification, measurement, limits or guidelines, and monitoring should be modeled on that of the FBO as a whole to provide for a fully-integrated risk management system.[3]

In assigning the risk management rating, examiners should evaluate the current, ongoing situation and concentrate on developments since the previous examination. The rating should not concentrate on past problems, such as those relating to the current quality of the branch's stock of assets, if risk management techniques have improved significantly since those problems developed.[4]

More specifically, in rating the branch's risk management procedures, examiners should consider the following.

- The extent to which the branch is able to manage the risks inherent in its lending, trading, and other activities, specifically its ability to identify, measure, and control these risks.
- The soundness of the qualitative and quantitative assumptions implicit in the risk management system.
- Whether risk policies, guidelines, and limits at the branch are consistent with its lending, trading, and other activities; management's experience level; and the overall financial strength of the branch and/or the FBO.
- Whether the management information system and other forms of communication are consistent with the level of business activity at the branch and sufficient to accurately monitor risk exposure, compliance with established limits, and sufficient to enable the head office to monitor the real performance and risks of the branch.
- Management's ability to recognize and accommodate new risks that may arise from the changing environment, and to identify and address risks not readily quantified in a risk management system.

For example, in the lending area, a branch is expected to have (1) experienced lending officers, an effective credit approval and review function, and, where appropriate, credit workout personnel; (2) a credit risk evaluation system that is adequate in assessing relative credit risks; (3) branch officer lending limits, lending guidelines, and portfolio policies consistent with the abilities of branch personnel and the financial expertise and resources of the FBO; (4) a system that identifies existing and potential problem credits, a method for assessing the likely impact of those credits on existing and future profits, and procedures for accurately informing head office of the credit quality of the portfolio and possible credit losses; and (5) procedures for assessing the impact on the portfolio of specific or general changes in the business climate.

A rating of 1 indicates that management has a fully-integrated risk management system that effectively identifies and controls all major types of risk at the branch, including those from new products and the changing environment. This assessment, in most cases, will be supported by a superior level of financial performance and asset quality at the branch. No supervisory concerns are evident.

A rating of 2 indicates that the risk management system is fully effective with respect to almost all major risk factors. It reflects a responsiveness and ability to cope successfully with existing and foreseeable exposures that may arise in carrying out the branch's business plan.

3. For a more detailed overview of the risk management process in trading operations, refer to the Federal Reserve's *Trading Activities Manual*.

4. Thus, for example, the change in the level of problem assets since the previous examination is normally more important than the absolute level of problem assets. At the same time, a loan portfolio that has few borrowers experiencing debt service problems does not necessarily indicate a sound risk management system because weak underwriting standards may make the branch vulnerable to credit problems during a future economic downturn.

While the branch may have residual risk-related weaknesses, these problems have been recognized and are being addressed by the branch and/or head office. Any such weaknesses will not have a material adverse affect on the branch. Generally, risks are being controlled in a manner that does not require additional or more than normal supervisory attention.

A rating of 3 signifies a risk management system that is lacking in some important measures. Its effectiveness in dealing with the branch's level of risk exposures is cause for more than normal supervisory attention, and deterioration in financial performance indicators is probable. Current risk-related procedures are considered fair, existing problems are not being satisfactorily addressed, or risks are not being adequately identified and controlled. While these deficiencies may not have caused significant problems yet, there are clear indications that the branch is vulnerable to risk-related deterioration.

A rating of 4 represents a marginal risk management system that generally fails to identify and control significant risk exposures in many important respects. Generally, such a situation reflects a lack of adequate guidance and supervision by head office management. As a result, deterioration in overall performance is imminent or is already evident in the branch's overall performance since the previous examination. Failure of management to correct risk management deficiencies that have created significant problems in the past warrants close supervisory attention.

A branch rated 5 has critical performance problems that are due to the absence of an effective risk management system in almost every respect. Not only are there a large volume of problem risk exposures, the problems are also intensifying. Management has not demonstrated the capability to stabilize the branch's situation. If corrective actions are not taken immediately, the operations of the branch are severely endangered.

Operational Controls

This component assesses the effectiveness of the branch's operational controls, including accounting and financial controls. The assessment is based on the expectation that branches should have an independent internal audit function and/or an adequate system of head office or external audits as well as a system of internal controls consistent with the size and complexity of their operations. In this regard, internal audit and control procedures should ensure that operations are conducted in accordance with internal guidelines and regulatory policies and that all reports and analyses provided to the head office and branch senior management are timely and accurate.

The rating of operational controls should include the following.

- The adequacy of controls and the level of adherence to existing procedures and systems. (These are separate but related factors.)
- The frequency, scope, and adequacy of the branch's internal and external audit function, relative to the size and risk profile of the branch, and the independence of the internal audit function from line management.
- The number and severity of internal control and audit exceptions.
- Whether internal control and audit exceptions are effectively tracked and resolved in a timely manner.
- The adequacy and accuracy of management information reports. This assessment should be based primarily on whether reports and analyses are sufficient to properly inform head office management of the branch's condition on a timely basis, and whether there are sufficient procedures to ensure the accuracy of those reports.
- Whether the system of controls is regularly reviewed to keep pace with changes in the branch's business plan and laws and regulations.

A branch that is rated 1 has a fully comprehensive system of operational controls that protects against losses from transactional and operational risks and ensures accurate financial reporting. Branch operations are fully consistent with sound market practices. The branch also has a well-defined and independent audit function that is appropriate to the size and risk profile of the branch. No supervisory concerns are evident.

A rating of 2 may indicate some minor weaknesses, such as the presence of new business activities where some modest control deficiencies exist, but which management is addressing. Some recommendations may be noted. Overall, the system of controls, including the audit function, is considered satisfactory and effective in maintaining a safe and sound branch operation. Only routine supervisory attention is required.

A rating of 3 indicates that the branch's system of controls, including the quality of the audit function, is lacking in some important respects, particularly as indicated by continued control exceptions and/or substantial deficiencies in or failure to adhere to written policies and procedures. As a result, more than normal supervisory attention is required.

A branch that is rated 4 signifies that the system of operational controls has serious deficiencies that require substantial improvement. In such a case, the branch may lack control functions, including those related to the audit function, that meet minimal expectations; therefore, adherence to bank and regulatory policy is questionable. Head office management has failed to give the branch proper support to maintain operations in accordance with U.S. norms. Close supervisory attention is required.

A branch that is rated 5 lacks a system of operational controls to such a degree that its operations are in serious jeopardy. The branch either lacks or has a wholly deficient audit function. Immediate substantial improvement is required by branch and head office management, along with strong supervisory attention.

Special audit procedures are required when both the O component and the composite rating are 3 or worse. If both the O component and the composite rating are 3, the special audit procedures may be performed by the internal audit function if, and only if, the audit function is considered satisfactory. If the internal audit function is less than satisfactory, or if both the O component and composite rating are 4 or worse, then an external audit is required. An external audit also is required if the internal auditors had performed the special audit procedures following the previous examination, and the O and composite ratings are again assigned a 3 rating. As significant internal control weaknesses in the operations of one office may be an indication of systemic weaknesses in other branches as well, the special audit procedures may be applied to other U.S. offices of the FBO. SR 96-27 provides additional guidance regarding these special audits.

Compliance

In addition to maintaining an effective system of operational controls, branches should also demonstrate compliance with all applicable state and federal laws and regulations, including reporting and special supervisory requirements. To the extent possible given the size, risk profile and organizational structure of the branch, these responsibilities should be vested in a branch official or compliance officer whose function is separate from line management. Branch management should also ensure that all appropriate personnel are properly trained in meeting regulatory requirements on an ongoing basis. The scope of the branch's audit function also should ensure that the branch is meeting all applicable regulatory requirements.

Accordingly, the branch's level of compliance should be rated based on the following factors.

- The level of adherence to applicable state and federal laws and regulations and any supervisory follow-up actions.
- The effectiveness of (i) written compliance procedures and (ii) training of line personnel charged with maintaining compliance with regulatory requirements.
- Management's ability to submit required regulatory reports in a timely and accurate manner.
- Management's ability to identify and correct compliance issues.
- Whether the internal audit function checks for compliance with applicable state and federal laws and regulations.

A branch accorded a rating of 1 demonstrates an outstanding level of compliance with applicable laws, regulations, and reporting requirements. No supervisory concerns are evident.

A rating of 2 indicates that compliance is generally effective with respect to most factors. Compliance monitoring and related training programs are sufficient to prevent significant problems. Minor reporting errors may be present, but they are being adequately addressed by branch management. Only normal supervisory attention is warranted.

A branch that is rated 3 has deficiencies in management and training systems that result in an atmosphere where significant compliance problems could and do occur. Such deficiencies could include a lack of written compliance procedures, no system for identifying possible compliance issues, or a substantial number of minor or repeat violations or deficiencies. More than normal supervisory attention is warranted.

A rating of 4 indicates that compliance matters are not given proper attention by branch and head office management and close supervisory attention is warranted. The lack of an effective compliance program, including an ongoing training program, may be evident along with a failure to meet significant regulatory requirements and/or significant, widespread inaccuracies in regulatory reports.

A rating of 5 would signal that attention to compliance matters is wholly lacking at the branch to the extent that immediate supervisory attention is warranted.

Asset Quality

Generally, asset quality is evaluated to determine whether a financial entity has sufficient capital to absorb prospective losses and, ultimately, whether it can maintain its viability as an ongoing entity. The evaluation of asset quality in a branch does not have the same result because a branch is not a separately capitalized entity. Instead, a branch relies on the financial and managerial support of the FBO as a whole.

Nonetheless, the evaluation of asset quality is important both in assessing the effectiveness of credit risk management and in the event of a possible liquidation of a branch. However, as indicated above, a branch is not strictly limited by its own internal and external funding sources in meeting solvency and liquidity needs. The ability of a branch to honor its liabilities ultimately is based upon the condition and level of support from the FBO, *a concept that is integral to the FBO supervision program.*

This concept states that if the condition of the FBO is satisfactory, the FBO is presumed to be able to support the branch with sufficient resources on a consolidated basis. As a result, the assessment of asset quality in such circumstances would not in and of itself be a predominant factor in the branch's overall assessment, if existing risk management techniques are satisfactory. If, however, support from the FBO is questionable, the evaluation of asset quality should be carefully considered in determining whether supervisory actions are needed to improve the branch's ability to meet its obligations on a stand-alone basis. In cases where a branch is subject to asset maintenance, it is expected that asset quality issues will be addressed by disqualifying classified assets as eligible assets.

The quality of the branch's stock of assets is evaluated based on the following factors. *Generally, credit administration concerns should be addressed in rating risk management.*

- The level, distribution, and severity of asset and off-balance-sheet exposures classified for credit and transfer risk.[5]
- The level and composition of nonaccrual and reduced rate assets.

A branch rated 1 has strong asset quality.

A branch rated 2 has satisfactory asset quality.

A branch rated 3 has fair asset quality.

A branch rated 4 has marginal asset quality.

A branch rated 5 has unsatisfactory asset quality.

5. The various state and federal agencies may differ in terms of specific practices and methodologies used to implement the above guidelines. For further guidance in this area, examiners should consult with their respective agencies.

Risk-focused examinations emphasize effective planning and scoping in order to customize examinations to the size and activities of the institution and to concentrate examiner resources on areas that expose the institution to the greatest degree of risk. In addition, under a risk-focused approach, the resources directed to assessing an organization's management are generally increased, while the degree of transaction testing may be reduced in order to minimize the regulatory burden.

Transaction testing includes the reconciliation of internal accounting records to financial reports (in order to evaluate the accuracy of account balances), the comparison of day-to-day practices to the office's policies and procedures (in order to assess compliance with internal systems), and all other supervisory testing procedures, such as the review of the quality of individual loans and investments. Risk-focused examinations still require an appropriate level of transaction testing to verify (1) the adequacy of, and adherence to, internal policies, procedures, and limits; (2) the accuracy and completeness of management reports and financial records; and (3) the adequacy and reliability of internal control systems. However, under a risk-focused examination approach, the degree of transaction testing should be reduced when internal risk management processes are determined to be adequate or risks considered minimal.

Generally, advance notification of an examination is given to enable branch management to have the necessary information available for examiners when they arrive on-site. This practice results in significant savings in time and personnel resources. However, surprise or nonroutine examinations may be conducted at any time at the examining agency's discretion.

PURPOSE OF PRE-EXAMINATION PREPARATION

Pre-examination planning results in more effective examinations that are focused on risks particular to the specific institution and thus minimizes regulatory burden. Further, such planning facilitates close coordination with other state and Federal banking agencies and allows information requests to be better tailored to the specific institutions.

RISK ASSESSMENT

In order to focus procedures on the areas of greatest risk to the branch, a risk assessment should be performed in advance of the on-site work. The risk assessment process highlights both the strengths and the vulnerabilities of the institution and provides a foundation from which to determine the procedures to be conducted during an examination. Risk assessments entail the identification of the financial activities in which a banking organization has chosen to engage, the determination of the types and quantities of risk, and the consideration of the quality of the management and control of these risks. At the conclusion of the risk assessment process, a preliminary supervisory strategy for the institution and each of its major activities can be formulated. Those activities that are most significant to the organization's risk profile or that have inadequate risk management processes or rudimentary internal controls represent the highest risks to the institution and should undergo the most rigorous scrutiny and testing.

Identifying the significant activities of an institution is the first step in the risk assessment process. These activities may be identified through the review of prior examination and inspection reports and workpapers, surveillance and monitoring reports generated by the Board and Reserve Bank staff, regulatory reports, and other relevant supervisory material. Once significant activities have been identified, the types and quantities of risks to which these activities expose the institution should be determined. This allows identification of the high risk areas that should be emphasized during the examination. The types of risk which may be encountered individually or in various combinations are credit, market, liquidity, operational, legal, or reputational. These risk types are discussed further in Section 3000.1 of this manual.

The quantity of risk can be determined by a number of factors. For example, in order to assess the quantity of credit risk in loans and commitments, the level of past due loans, internally classified or watch list loans, nonperforming loans, and concentrations of credit to particular industries or regions should be considered. In addition, the examiner should consider the trends in special mention and classified loans and historic chargeoff levels.

Once the types and quantities of risk in each activity have been identified, a preliminary assessment of the process in place to identify, measure, monitor, and control these risks should be completed. Sound risk management will vary from branch to branch, but generally include four basic elements. These are: (1) active senior management oversight, (2) adequate policies, procedures, and limits, (3) adequate risk measurement, monitoring, and management information systems, and (4) comprehensive internal audits and controls.

Ordinarily the pre-examination preparation is performed by the examiner-in-charge or designee and one or more assistants. Time requirements for this preparation may vary considerably depending upon the size, complexity, and condition of the branch being examined. The timing should allow overall scheduling efficiency and should consider such factors as the number and experience of participating personnel, geographic location of the branch, and the results of previous examinations. Scheduling factors may result in the pre-examination preparation being performed from many weeks before the start of the examination to the week immediately preceding the examination.

ASSIGNMENT AND SUPERVISION OF PERSONNEL

Early review allows the examiner-in-charge the greatest flexibility in determining the number of examining personnel needed and any special expertise required.

The examiner-in-charge must be able to prioritize critical categories of the examination and determine the optimum timing of simultaneous activities. Budgeting and allocating human resources should include the following considerations:

- Assignment of examiners based on their skills/expertise and examination objectives.
- Assignment of priorities to avoid duplication of effort and ensure timely completion of the examination.
- Coordination with other regulatory agencies that may be conducting a joint, concurrent, or related office examination.
- Assignment of examining personnel in a manner to maintain an even workload throughout the examination.

GENERAL GUIDELINES FOR PRE-EXAMINATION PREPARATION

Because the primary purpose of the pre-examination preparation is to determine examination objectives and scope, only general guidelines for the procedures to be performed can be given. Accordingly, the procedures that follow may be modified to fit the specific circumstances encountered. General guidelines for pre-examination preparation include:

- Reviewing the examination strategy/annual examination plan developed by the appropriate supervisory authorities.
- Reviewing examination manuals, programs, and regulatory letters applicable to the examination.
- Reviewing all other available analyses prepared by the coordinating Reserve Bank and other supervisory agencies.
- Reviewing all available regulatory reports, including the Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks (FFIEC 002) and the Country Exposure Report (FFIEC 019).
- Reviewing the branch's strategic or business plan, if available. This plan, provided by the branch, can be useful in examination planning, as it may indicate new or discontinued services that could affect the scope and direction of the examination. The plan can also serve as a reference between examinations. The plan usually contains goals and prospects for the branch over the next business period, indicating target markets and the expected level of profitability and other performance standards to be achieved.
- Reviewing the following list of branch services and products to determine their importance to the examination:
  - — Deposit services: checking, automatic funds transfer, telephone transfer;
  - — Credit services: commercial loans, overdraft banking, installment loans, mortgage lending, letters of credit, bills discounted;
  - — EDP services;
  - — Securities trading and off-balance sheet activities, including foreign exchange;
  - — Fiduciary activities; and
  - — Private banking.
- Reviewing all related examination and visitation reports, correspondence, enforcement

actions, minutes, and memoranda of significance.

- Coordinating with other pertinent regulatory agencies or units, particularly in the case of special examinations resulting from novel or unusual situations. Determining which related organizations are to be examined and the extent of the procedures to be performed.
- Completing personnel assignments and coordinating with assisting personnel regarding any preliminary procedures that are to be performed.
- Determining the cut-off line or the appropriate statistical sampling technique to be used for performing risk asset review. Note any unusual considerations that may affect the establishment of the factors.
- Reviewing and customizing the First Day Letter before presentation to branch management; early presentation permits timely completion of bank-prepared information.

Upon completion of the pre-examination preparation, the scope of the examination should be established and a planning memorandum should be developed. Accomplishing the foregoing tasks before starting the examination will provide for an efficient examination, consistent with established objectives.

DETERMINING THE SCOPE OF THE EXAMINATION

Full-scope examinations under a risk-focused approach are not comprised of a fixed set of routine procedures. Rather, the procedures that must be performed to fulfill the objectives of a full-scope examination must be adjusted depending on the circumstances of the institution being evaluated. At a minimum, however, full-scope examinations should include sufficient procedures to reach an informed judgement on the risk management, operational, and compliance factors rated under ROCA.

If necessary, the examiner-in-charge should meet with the principal branch officers before the start of the examination to determine the breadth of their individual responsibilities. The examiner-in-charge should determine at this meeting whether any important developments have occurred since the previous examination or if any planned or probable events are expected in the near-term. Arrangements should be made with branch personnel as to the level of their assistance required during the examination.

Discussions should be held with any examiners offering specialized assistance during the examination, for example, consumer affairs, EDP, or audit, to determine the scope of their review and the inclusion of those results within the context of the overall examination report, if so planned.

At this point in time, the scope of the examination should be developed so as to facilitate the development of a First Day Letter applicable to the branch being examined.

PREPARATION OF A SCOPE MEMORANDUM

Once the examination planning and risk assessment processes are completed, a scope memorandum should be prepared. A scope memorandum provides a detailed summary of the supervisory strategy for an institution and assigns specific responsibilities to examination team members. A scope memorandum should be tailored to the size and complexity of the institution, should define the objectives of each examination, and generally should include:

- Name and location of entity to be examined.
- Results of previous examination.
- Objectives of the examination.
- Identification of the risks to be assessed.
- Scope of the examination/nature and depth of coverage.
- An overview of the branch's management structure.
- Summary of the branch's activities.
- Summary of earnings and other performance information to date.
- Summary of the structure and business strategy/plan of the branch.
- Balance sheet and contingency/memoranda items.
- Administrative issues.
- Allocation of assigned personnel resources.
- Business components and support functions.
- Workpaper and report of examination requirements.

DEVELOPING THE FIRST DAY LETTER

Once the scope memorandum is completed, the examiner-in-charge can develop the First Day Letter, which should be delivered to branch management in a timely manner, before the start of the examination. Upon presentation of the First Day Letter, the examiner should ensure that management understands what is being requested and how to avoid duplication of effort through the use of information that may already be generated by the branch's own management information systems.

The examiner-in-charge must ensure that branch personnel are fully aware of how the information is to be prepared, when the information is required, and the need for accuracy and completeness.

A risk-focused review of a loan portfolio is one of the most important elements of an examination. Credit reviews are an examiner's primary means for evaluating the effectiveness of internal loan review and credit-grading systems, determining that credit is being extended in compliance with internal policies and credit standards, ascertaining a branch's compliance with applicable laws and regulations, and judging the safety and soundness of the branch's lending and credit administration functions. Examiners must select for review a sample of loans[1] that is sufficient in size and scope to enable them to reach reliable conclusions about the branch's overall lending function. The specific details of selecting the sample is subject to the examiners's discretion, based on the level of risk perceived at the institution.

Sampling enables the examiner to draw conclusions regarding the condition of the entire loan portfolio and selected off-balance-sheet items by reviewing only a selected portion of outstanding credit facilities. Thus, such techniques economize on the use of examination resources and allow examiners to devote more of their time and efforts to other areas of examination interest.

Generally, a judgmental sampling technique is used for reviewing credit facilities. This technique enables examiners to evaluate the portfolio by reviewing a desired percentage of all loans and appropriate off-balance-sheet items over preselected cut-off amounts. In addition to the judgmental sampling approach, statistical sampling techniques can also be valid methods for evaluating credit portfolios. Two statistical sampling techniques that may be selectively implemented during on-site examinations are attribute sampling and proportional sampling. Attribute sampling is used in certain branches that have formal loan review programs; proportional sampling is used in branches without such internal credit review programs.

In statistical sampling, the examiner applies sampling techniques to the design, selection, and evaluation of samples by employing the concepts of probability. Use of these concepts eliminates (or at least minimizes) biases by satisfying a condition that each item in the population must have an equal or otherwise determinable probability of being included in the examined portion. By satisfying that condition, statistical sampling provides the examiner with a quantitative measure of risk that can be controlled at a level that is tolerable to the examiner. Statistical sampling techniques may be implemented only in those branches that were found to be in financially sound condition at the latest examination and only in those branches where it is determined that the systems and controls are appropriate for implementing such techniques. Moreover, if during the examination where statistical sampling is being used, the examiner determines that the sample results are unsatisfactory or the condition of the branch has deteriorated since the previous examination, the traditional judgmental sampling technique must be implemented.

The following is a description of the two recommended statistical sampling techniques:

ATTRIBUTE SAMPLING

The objective of attribute sampling is to use a sample, within specified reliability limits, to determine the validity of the branch's internal credit review program. The reliability limits are determined by the examiner who formulates a hypothesis about the branch's credit review program when evaluating its policies, practices, and procedures with regard to extensions of credit. The sample population consists of all loans and appropriate off-balance-sheet items between certain dollar parameters, except for credit facilities reviewed under the Shared National Credit Program and facilities to identified problem industries, which are reviewed separately during the examination. The lower dollar parameter is an amount that the examiner deems sufficient to achieve the desired coverage of the portfolio and is selected in much the same manner as a cut-off line is chosen in judgmental sampling. The upper dollar parameter is an amount over which all credit facilities must be reviewed because of the significant effect each could have on the branch's condition. Credit

1. For the purposes of this section, the term "loans" includes all sources of credit exposure arising from loans and leases including interbank placements, investment securities, and banker's acceptances. This exposure also includes credit-related off-balance-sheet items such as standby letters of credit, loan commitments, and risk participations in acceptances. Credit exposures arising from trading and derivatives activities are not generally included.

facilities are selected from the sample population by using a random digit table.

When the selected credit facilities are reviewed, the examiner compares the findings with those of the branch's credit review program. An error exists if the examiner's criticism of a particular credit is significantly more severe than the branch's findings. If the error rate in the sample is beyond the reliability limits that the examiner is willing to accept, all credit facilities over the appropriate cut-off line will be reviewed. If the examiner is satisfied with the sample results, the branch's internal classifications may be accepted for all criticized loans within the sample population. Even when the branch's classifications are deemed acceptable by the examiner, any loans reviewed and found to be in error will be appropriately classified in the report.

PROPORTIONAL SAMPLING

Generally speaking, the procedures for proportional sampling are similar to those followed for attribute sampling. The examiner formulates a hypothesis about the quality of the examined branch's credit administration based upon an analysis of its loan policies, practices, and procedures with regard to extensions of credit. Additionally, the branch is asked to provide a problem credit list, without grading the credit facilities. The examiner's findings are compared to that list. The objective of this sampling technique is to determine whether management can identify all the criticizable credit facilities in its portfolio. In proportional sampling, every credit in the sample population is given an equal chance of selection proportionate to its size; therefore, the larger the credit, the more likely it will be selected for review.

As in attribute sampling, the examiner specifies the desired precision of the sample, i.e., that the true error rate in the branch's problem credit list should be contained within a certain range of values. As a control measure, sample precision is set to represent a specified percentage of the branch's net assets. A statistical error occurs whenever the examiner criticizes a credit not previously identified by the branch. If the error rate is higher than expected, the examiner may review all credit facilities over selected cut-off lines, which are determined by using the same criteria used for line selection in judgmental sampling. If the sample results indicate an error rate within expectations, then the examiner may accept the branch's problem credit list as being representative of the quality of the population of credits from which the sample was taken. The examiner will then review each credit on the problem list over the selected cut-off lines to determine the amounts that should be classified.

For detailed procedures on how to implement both attribute and proportional sampling techniques, examiners should contact appropriate regulatory agency staff.

The primary goal of workpapers is to strengthen the examination process by providing a clear recounting of the many tasks performed during an examination. Workpapers, their purpose, their quality, and organization are important to the supervisory process because the workpapers support the information and conclusions contained in the related report of examination. Accordingly, they could include, but are not necessarily limited to: risk-focused scope memorandum (as discussed in section 2010), examination procedures and verifications, memoranda, schedules, questionnaires, checklists, abstracts of branch documents, analyses prepared or obtained by examiners, and a summary memorandum for each component. To this end, the workpapers should achieve the following objectives:

- Organize the material assembled during an examination to facilitate review and future reference;
- Aid the examiner in efficiently conducting the examination;
- Document the policies, practices, procedures, and internal controls of the branch;
- Provide written support of the examination procedures performed during the examination;
- Indicate why certain steps or procedures were eliminated or deemed unnecessary;
- Document the results of testing and formalize the examiner’s conclusions; and,
- Substantiate the assertions of fact or opinion contained in the report of examination.

They also are useful as:

- A tool for the examiner-in-charge to use in planning, directing, and coordinating the work of the other examiners;
- A means of evaluating the quality of the work performed;
- A confirmation that the work recommended by the annual examination plan was performed as specified;
- A guide in estimating future personnel and time requirements; and
- A record of the procedures used by the branch to assemble data for reports to supervisory authorities.

WORKPAPER DOCUMENTATION

Each individual workpaper should include a workpaper coversheet, scope, and conclusion.

Workpaper Coversheet—A workpaper coversheet should provide the following information:

- Office name and location;
- Workpaper title;
- Examination date and work performance date;
- Initials of preparer and initials of the assigned reviewer;
- Name and title of person or description of records that provided the information for the workpaper; and
- An index number identifying the workpaper and facilitating organization of the workpaper files.

Scope—This should address the activities performed in order to examine the particular area, including the nature, timing, and extent of testing in the application of examination and audit procedures as well as the examiner’s evaluation of and reliance on internal and external audit procedures and compliance testing of internal controls. To the extent that this information is contained in other workpapers, such as the risk-focused scope memorandum, a reference to the appropriate workpaper will be sufficient. Because of the risk-focused nature of examinations, an explanation should be provided in the scope section of the workpapers explaining why the particular scope was chosen for a specific area or function. The workpapers also should contain an explanation as to why certain steps or examination procedures were eliminated or deemed unnecessary. This information is necessary in order to ensure that an effective audit trail is documented in the workpapers detailing the reasons for the scope chosen.

Conclusion—This summarizes the findings both positive and negative, and lists any recommendations made by examiners. Each workpaper summary is consolidated into the applicable component(s) rating conclusion memorandum.

ORGANIZATION OF WORKPAPERS

To promote efficiency and help ensure that all applicable areas of an examination have been considered and documented, examiners should use an indexing system to organize workpaper files. A general outline or index of all examination areas provides a basis for organization to which a numbering or other sequential system can be assigned and applied to each workpaper file.

When all workpapers pertinent to a specific area of the examination have been completed, the workpapers should be indexed and filed by each rating component. A component rating conclusion memorandum is then prepared for each of the ROCA components. This memorandum should include a list of workpapers completed, a summary of findings and conclusions, a recommended rating for the component, and any required corrective action to be recommended in the report.

CONTROL AND REVIEW

All examiners assigned to an examination should ensure that workpapers are controlled at all times while the examination is in progress. For example, when in the branch's offices, the workpapers should be secured at night and safeguarded during the lunch hour or at other times when no examining personnel are present in the immediate vicinity. It is essential to completely control confidential information provided by the branch. In addition, information relating to the extent of tests and similar details of examination procedures should not be made available to branch employees.

In cases where customary workpaper procedures are not practical, alternative procedures and the extent to which they are applied should be documented. The need for completeness requires that there be no open items, unfinished operations, or unanswered questions in the workpapers at the conclusion of the examination.

The clarity of workpapers should be such that an examiner or examining official unfamiliar with the work could readily understand them. Commentaries should be legible, concise, and support the examiner's conclusions. Descriptions of work completed, notations of conferences with branch management, conclusions reached, and explanations of symbols used should be free from ambiguity or obscurity. In addition, examining personnel should be instructed on workpaper standards and content to ensure that they will meet the quality standards of the regulatory agencies. When workpapers have the necessary qualities of completeness, clarity, conciseness, and neatness, a qualified reviewer may easily determine their relative value in support of conclusions and objectives reached. Incomplete, unclear, or vague workpapers may lead a reviewer to the conclusion that the examination has not been adequately performed.

REVIEW PROCEDURES

Experienced personnel must review all workpapers prepared during an examination. Usually, that review is performed by the examiner-in-charge, although in some cases, the examiner-in-charge may designate other experienced personnel to perform the review. The primary purposes of a review of workpapers by senior personnel are to determine that the work is adequate, given the circumstances, and to ensure that the record is sufficient to support the conclusions reached in the report of examination. The timely review and discussion of workpapers with the individual who prepared them is one of the more effective on-the-job training procedures.

Normally, the review should be performed as soon as practicable after the completion of each assignment. This review ideally occurs at the branch's office, so that, if additional information or work is required, the matter can be promptly attended to with a minimum loss of efficiency.

When the review of workpapers is completed, the reviewer should sign or initial the applicable documents. Although all workpapers should be reviewed, the depth and degree of review depends on factors such as:

- The nature of the work and its relative importance to the overall examination objectives.
- The extent to which the reviewer has been associated with the area during the examination.
- The experience of the examiners who have carried out the various operations.

Examiner judgment must be exercised throughout the review process.

WORKPAPER RETENTION

Examiners should consult with their respective agency for further guidance on workpaper retention guidelines.

Supervisory follow-up actions are implemented to ensure that appropriate corrective actions are taken in a timely manner to resolve any supervisory concerns that exist with respect to a branch. Generally, supervisory action is initiated based upon the results of an on-site examination. Action may be initiated, however, in response to concerns developed through various supervisory monitoring programs or through the review of other available information.

Because branches are subject to supervision by their federal or state licensing authority, branches may be subject to supervisory follow-up actions by all of these supervisory authorities. In most cases, however, if concerns are limited to one branch of the foreign banking organization, supervisory follow-up action will be the responsibility of the examining agency or agencies. If problems are apparent in other branches of the foreign banking organization, the various supervisory authorities will coordinate the development of the supervisory action plan for the institution.

INFORMAL AND FORMAL SUPERVISORY ACTIONS

As a general rule, informal and formal supervisory action should be considered when normal follow-up procedures and other more routine measures, such as formal discussions with a branch's local or head office management, have failed to resolve supervisory concerns. This practice is consistent with the treatment of domestic banking organizations and is based on the expectation that all banking institutions operating in the United States are expected to operate in a safe and sound manner and in compliance with applicable U.S. laws and regulations. Accordingly, when supervisory concerns are identified, corrective action should be initiated by branch or head office management as soon as possible. In this regard, examiners should communicate to the management of the branch throughout the course of the examination and at its close, both the problems identified and the actions recommended to correct those problems.

Generally, an informal supervisory action is appropriate when supervisory concerns have been identified that, while not overly serious in nature, do warrant some type of remedial action undertaking with the foreign banking organization. Such concerns may be isolated in one branch or may be evident in other branches of the foreign banking organization. In either case, the action is entered into with the foreign banking organization and the affected U.S. branch or branches; it involves a mutually agreed upon understanding between the foreign banking organization and the supervisory agency or agencies. The action generally lists and describes how specific objectives are to be achieved, including timeframes for achieving those objectives.

Informal enforcement actions that may be utilized for branches include the Commitment Letter and the Memorandum of Understanding.

A Commitment Letter is a document that contains specific written commitments to take corrective action in response to problems or concerns identified by the supervisory agency or agencies. A Commitment Letter is not a binding legal document; however, failure to meet the commitments in the letter will provide strong evidence of the need for more formal supervisory action.

A Memorandum of Understanding is a more formally designed action, though still not a binding legal document, that incorporates even greater specificity concerning the measures being taken to resolve problems than found in a Commitment Letter. A Memorandum of Understanding suggests a higher level of supervisory concern over that of a Commitment Letter. It generally must be signed by senior officials from the head office.

Formal supervisory actions are appropriate in instances where supervisory concerns have risen to a level where stronger or more immediate action is necessary to ensure that corrective actions are taken and fully implemented. These actions are authorized by statute and noncompliance has a legal liability, i.e. violators can be subject to additional enforcement actions, such as the assessment of civil money penalties.

Formal enforcement actions include the Cease and Desist Order, including a Temporary (Emergency) Cease and Desist Order, and the Written Agreement. Cease and desist action may be initiated when there is a finding that an offender is engaging, has engaged, or may engage in an unsafe or unsound practice in conducting the business of the institution. An action may also be deemed necessary due to a finding that the offender is violating, has violated, or may violate a law, rule, or regulation, or any condition imposed in writing, for example, by the Board of Governors in connection with the granting of any application or written agreement.

In the event that a violation of law, rule, or regulation, or the undertaking of an unsafe or unsound practice meets certain criteria, a temporary (emergency) cease and desist order may be issued. This order may also be issued if it is determined that the institution's books and records are incomplete or that the institution's financial condition or the details or purpose of any transaction cannot be determined through the normal supervisory process. The temporary order may require the same corrections as an order issued either on consent or after the full administrative process. Its advantage is that it is effective immediately upon service on the entity or individual. A hearing must be held within 30–60 days, during which time the temporary order stays in effect. Within 5–10 days of the service of the temporary order, the subject may appeal to a U.S. District Court for relief from the order.

When circumstances warrant a less severe form of formal supervisory action, a *formal written agreement* may be used. Other enforcement tools that are applicable to branches include the imposition of civil money penalties, prohibition orders, and possibly termination.

CIVIL MONEY PENALTIES

Under provisions of the Financial Institutions Regulatory and Interest Rate Control Act of 1978 (FICA) (Pub. L. 95-630), the appropriate federal banking agency is authorized to assess civil money penalties for violations of any law or regulation or for violation of the terms of any written agreement, any final or temporary cease and desist order or any condition imposed in writing by a federal banking agency in connection with the granting of any application by the foreign banking organization. Civil money penalties may also be imposed, in certain cases, for engaging in unsafe and unsound practices (12 USC Section 1818). In addition, civil money penalties may be assessed against officers, directors, and other institution-affiliated parties for violations of any of the above situations.

In determining the appropriateness of initiating a civil money penalty assessment proceeding, the federal banking agencies may use a variety of relevant factors. For example, in assessing a civil money penalty, the Board of Governors is required to consider the size of the financial resources and good faith of the respondent, the gravity of the violation, the history of previous violations and such other matters as justice may require. (See FRRS, Section 3-1605.) Other regulatory agencies have their own guidelines. (See, for example, *OCC Policy and Procedures Manual*.)

Depending upon the regulatory agency involved, examiners may be responsible for the initial analyses of potential civil money penalties. Civil money penalties may be proposed for serious violations and for violations that, because of their frequency or recurring nature, show a general disregard for the law. After the examiner has reviewed the facts and decided to recommend a civil money penalty, he or she should contact the appropriate federal regulatory agency for advice on proper documentation and any other assistance.

ASSET MAINTENANCE

In cases where there is doubt concerning the ability of a foreign banking organization to continue to serve as a source of strength to its U.S. branch(es), supervisory action may have to be taken to safeguard the U.S. branch(es) and ensure that it can honor its liabilities to third parties. Under these circumstances, an asset maintenance requirement[1] of at least 105 percent material may be imposed on the individual branch.

Other actions that may be taken to address concerns of this nature regarding the foreign banking organization include: asset pledge requirements, increased capital equivalency deposits, restrictions on transactions with related

1. Asset maintenance means the maintenance of eligible assets in the United States covering a specified percentage of third party liabilities of a branch. In general, eligible assets are those for which there is a reasonable expectation of liquidation on a timely basis. When under an asset maintenance requirement, a branch must maintain a net due to related parties position at all times. Thus, the branch is prevented from providing net funding to other branches or the head office. For more specific information on the examination objectives and procedures relating to asset maintenance, refer to that section of the manual.

parties, funding limitations, growth limitations, and voluntary or involuntary termination of the branch.

In some cases, because of concerns about the financial condition of the foreign banking organization or circumstances in the home country that may adversely affect the foreign banking organization's U.S. operations, asset maintenance may be necessary even when the U.S. operations are in satisfactory condition. When the U.S. operations, of a foreign banking organization are in less than satisfactory condition, the severity of the problems in those operations, combined with the degree of concern over the solvency of the foreign banking organization, will be used to determine the appropriate combination of informal or formal supervisory action and asset maintenance requirement.

When an asset maintenance requirement is deemed necessary, the preferred way to implement such a requirement is by action of the appropriate licensing agency and the insurer through any means available, including mutual agreement, authorization under state law, or formal supervisory action. Asset maintenance may therefore be imposed regardless of whether it is a specific regulatory tool of the licensing authority. When multiple branches are involved, as a general principle, asset maintenance requirements will be defined to be applied in a consistent manner to all of the operations of the foreign banking organization.