

TABLE OF CONTENTS

	<u>Page</u>
Introduction	1
Understanding the Bank	1
Reliance on Internal Risk Assessments	2
Scope Memorandum	2
Preliminary Risk Assessment	3
Summary of the Pre-Examination Meeting	3
Summary of Audit and Internal Control Environment	3
Summary of Examination Procedures	4
Summary of Loan Review	4
Job Staffing	4
Use of the Examination Modules	4
Appendix-A (Sample Scope Memorandum)	
Appendix-B1 (Management and Internal Control Evaluation Module)	
Appendix-B2 (Loan Portfolio Management Module)	

Questions or comments concerning this handbook should be addressed to:

**Director, Division of Banking Supervision and Regulation
Board of Governors of the Federal Reserve System
Washington, D.C. 20551**

INTRODUCTION

In recent years, the Federal Reserve has introduced a number of programs aimed at enhancing the effectiveness of its supervisory process for community banks. Although effective risk management has always been central to safe and sound banking activities, it has become even more important as new technologies, product innovation, and the size and speed of financial transactions have changed the nature of banking markets. In response to these changing market realities, certain supervisory risk management processes have been refined, while others - in particular, those that have proven most successful in supervising banks under a variety of economic circumstances and industry conditions - have been retained.

The objective of a risk-focused examination is to effectively evaluate the safety and soundness of the bank, including the assessment of its risk management systems, financial condition, and compliance with applicable laws and regulations, while focusing resources on the bank's highest risks. The exercise of examiner judgment to determine the scope of the examination during the planning process is crucial to the implementation of the risk-focused supervision framework, which provides obvious benefits such as higher quality examinations, increased efficiency, and reduced on-site examiner time.

UNDERSTANDING THE BANK

The risk-focused supervision process for community banks involves a continuous assessment of the bank. The understanding of the bank developed through this assessment enables examiners to tailor the examination of the bank to its risk profile. Understanding the bank begins with a review of available information on the bank. In addition to examination reports and correspondence files, each Reserve Bank maintains various surveillance reports that identify outliers when a bank is compared to its peer group. The review of this information assists examiners in identifying both the strengths and vulnerabilities of the bank and provides a foundation from which to determine the examination activities to be conducted.

Contact with the organization is encouraged to improve the understanding of the institution and the market in which it operates. A pre-examination interview or visit should be conducted as a part of each examination. Such a meeting gives examiners the opportunity to learn about any changes to bank management, bank policies, strategic direction, management information systems, and other activities. Particular emphasis should be placed on learning about new products or markets into which the bank has entered. The interview or visit also provides examiner's with management's view of local economic conditions, an understanding

of the bank's regulatory compliance practices, its management information systems, and its internal/external audit function. In addition, Reserve Banks should contact the state banking regulator to determine whether they have any special areas of concern that should be focused on during the examination.

RELIANCE ON INTERNAL RISK ASSESSMENTS

Internal audit, loan review, and compliance functions are integral to a bank's own assessment of its risk profile. If applicable, it may be beneficial to discuss with the bank's external auditor the results of the most recent audit it has completed for the bank. Such a discussion gives the examiner the opportunity to review the external auditor's frequency, scope and reliance on internal audit findings. Examiners should consider the adequacy of these functions in determining the risk profile of the bank and the opportunities to reduce regulatory burden by testing rather than duplicating the work of these audit functions.

Transaction testing remains a reliable and essential examination technique for use in the assessment of an institution's condition. The amount of transaction testing necessary to evaluate particular activities generally depends on the quality of the bank's process to identify, measure, monitor, and control the activity's risk. Once the integrity of the management system is verified through testing, conclusions on the extent of risks within the activity can be based on internal management assessments of the risks rather than on the results of more extensive transaction testing by examiners. If, however, initial inquiries into the risk management system, or efforts to verify the integrity of the system, raise material doubts as to the system's effectiveness, then no significant reliance should be placed on the system and a more extensive series of tests should be undertaken to ensure that the bank's exposure to risk from a particular activity can be accurately evaluated.

SCOPE MEMORANDUM

The scope memorandum is an integral product in the risk-focused methodology as the memorandum identifies the central objectives of the on-site examination. The scope memorandum also ensures that the examination strategy is communicated to appropriate

examination staff. A sample scope memorandum is presented in Appendix - A. This document is of key importance, as the scope will likely vary from examination to examination. Examination procedures should be tailored to the characteristics of each bank, keeping in mind its size, complexity, and risk profile. Procedures should be completed to the degree necessary to determine whether the bank's management understands and adequately controls the levels and types of risk that are assumed. In addition, the memorandum should address the banking environment, economic conditions, and any changes that bank management foresees that could affect the bank's condition. A preliminary estimate of staffing required to perform the examination should also be prepared as part of the scope memorandum.

The key factors that should be addressed in the scope memorandum include:

Preliminary Risk Assessment

The risks associated with the bank's activities should be summarized and based on a review of all available sources of information on the bank, including but not limited to, prior examination reports, surveillance reports, correspondence files, and audit reports. The scope memorandum should include a preliminary assessment of the bank's condition and major risk areas that will be evaluated through the examination process.

Summary of the Pre-Examination Meeting

The results of the pre-examination meeting should be summarized with particular emphasis on the meeting results that affect examination coverage.

Summary of Audit and Internal Control Environment

A summary of the scope and adequacy of the audit environment should be prepared which may result in a modification of examination procedures initially expected to be performed. Activities that receive sufficient coverage by the bank's audit system can be tested through the examination process. Sufficient audit coverage could result in the elimination of certain procedures if the audit and internal control areas are deemed satisfactory.

Summary of Examination Procedures

Examination modules have been developed related to the significant areas reviewed during an examination. The modules are categorized as being primary or supplemental. The primary modules must be included in each examination. However, procedures within the primary modules can be eliminated or enhanced based on the risk assessment or the adequacy of the audit and internal control environment. The scope memorandum should specifically detail the areas within each module to be emphasized during the examination process. In addition, the use of any supplemental modules should be discussed.

Summary of Loan Review

Based on the preliminary risk assessment, the anticipated loan coverage should be detailed in the scope memorandum. In addition to stating the percent of commercial and commercial real estate loans to be reviewed, the scope memorandum should also identify which speciality loan references to the general loan module are to be completed. The memorandum should specify activities within the general loan module to be reviewed, as well as the depth of any speciality reviews.

Job Staffing

The staffing for the examination should be detailed. Particular emphasis should be placed on ensuring appropriate personnel are assigned to the high risk areas identified in the bank's risk assessment.

USE OF THE EXAMINATION MODULES

Standardized community bank examination modules have been jointly developed by the Federal Reserve and the FDIC. This automated format was designed to define common objectives for the review of important activities within community banks and to assist in the documentation of examination work. It is expected that full-scope examinations will include

examiners' evaluation of six critical areas that are necessary to determine the bank's CAMELS rating. To evaluate these areas, examiners must perform procedures tailored to fit the risk profile of the bank. The seven primary examination modules are:

- Capital Adequacy
- Earnings Analysis
- Loan Portfolio Management
- Liquidity Analysis
- Management and Internal Control Evaluation
- Securities Analysis
- Other Assets and Liabilities

In addition, a review of the bank's compliance with the Bank Secrecy Act (BSA) should be performed using the existing BSA handbook.

There are six supplemental modules that are available for use if any of these activities present significant risk to the bank. The supplemental modules are:

- Electronic Funds Transfer Risk Assessment
- International Banking
- Credit Card Merchant Processing
- Mortgage Banking
- Electronic Banking
- Related Organizations

In addition, there are ten Loan References (for specialized lending areas) included in the general Loan Portfolio Management module. The loan reference modules are:

- Construction and Land Development
- Commercial and Industrial Real Estate
- Residential Real Estate Lending
- Commercial and Industrial Loans
- Agricultural Lending
- Direct Lease Financing
- Floor Plan Loans
- Troubled Debt Restructuring
- Consumer and Check Credit
- Credit Card Activities

The modules establish a three-tiered approach for the review of a bank's activities. The first tier is the core analysis, the second tier is the expanded review, and the final tier is the impact analysis. The core analysis includes a number of decision factors which should be considered collectively, as well as individually when evaluating the potential risk to the bank. To assist the examiner in determining whether risks are adequately managed, the core analysis section contains a list of procedures that may be considered for implementation. Once the relevant procedures are performed, the examiner should document conclusions in the core analysis decision factors. Where significant deficiencies or weaknesses are noted in the core analysis review, the examiner is required to complete the expanded analysis for those decision factors that present the greatest degree of risk to the bank. On the other hand, if the risks are properly managed, the examiner can conclude the review and carry any comments to the report of examination.

The expanded analysis provides guidance to the examiner in determining if weaknesses are material to the bank's condition and if they are adequately managed. If the risks are material or inadequately managed, the examiner is directed to perform an impact analysis to assess the financial impact to the bank and assess whether any enforcement action is necessary.

The use of modules should be tailored to the characteristics of each bank based on its size, complexity, and risk profile. As a result, the extent to which each module should be completed will vary from bank to bank. One of the features included in the automated format for the modules allows examiners to select the appropriate procedures in the modules that address the area(s) of concern while eliminating unnecessary procedures. The degree of expected completion of the modules should be documented in the scope memorandum. Appendix - B1 provides the Management and Internal Control Evaluation module. The Loan Portfolio Management module is presented in Appendix - B2.

The individual procedures presented for each level are meant only to serve as a guide for answering the decision factors. Each procedure does not require an individual response and each procedure may not be applicable at every community bank. Examiners should continue to exercise discretion in deciding to exclude any items as unnecessary in the evaluation of the decision factors. Moreover, the listed procedures do not represent every possible factor to be considered during an examination. Examiners should reference the Commercial Bank Examination Manual or supervisory and administrative letters for additional guidance.

SCOPE MEMORANDUM

February 24, 2000

Bank: State Bank of North Dakota, Ayncity, North Dakota

Examination Date: March 1, 2000

Examiner in charge: Bob Doe

Prior examination CAMEL: 12232/2

SEER/CAEL ratings: SEER rating 2.06
CAEL rating 22M31/3

PRELIMINARY RISK ASSESSMENT

Credit risk appears to be modest as indicated by a low level of internal classifications. The latest internal classification represented 4.3% of capital on a weighted basis. In addition, past due loans represent a nominal 2.3% of outstandings. These indicators have remained relatively stable over the past several years. Market risk appears to be moderate. The bank monitors its position on a gap report. Limits are considered conservative, and the bank does not invest in high risk securities. Surveillance reports reflect a highly liquid position as evidenced by core deposit stability, a high volume of liquid securities, and limited borrowing activity.

The capital position is strong. Tier 1 leverage is 15.5% and historically asset growth has been manageable at less than 10% annually. The dividend payout ratio remains low. Earnings performance continues to lag peer group averages. The primary factors appear to be high overhead expenses and limited fee income. In addition, securities represent a high percentage of total assets, consequently asset yields trail peer comparison. The bank's return on average assets was .82% for 1999, below peer banks but comparable to previous years. Earnings are characterized by relatively stable margins. Interest expense has risen steadily due to increased pressure from competition for local deposits; however, the bank has been able to raise loan rates to compensate for the increase in interest expenses.

The bank has not been detailed on surveillance exception reports during the past year, with the exception of the below peer earnings performance. Other financial factors indicate a stable and satisfactory position.

SUMMARY OF PRE-EXAMINATION MEETING

A meeting was held on January 15, 2000 with President Dave Elvis. Informal conversations were also held with Ginny Rich and Greg Cook in the loan administration area. The bank has started a division to lend to small commercial borrowers and continues to be active in community outreach programs. Management also discussed plans to start issuing credit cards.

Due to problems associated with the purchase of one high-risk security, the bank has elected to continue to confine their future purchases to short-term U.S. Treasury and Agency issues, recognizing it will affect the bank's earnings performance. The strategic plan calls for moderate growth and a community orientation. The local economy is strong. There are six colleges located within five miles of the bank.

There have been no changes in top management; however, the bank recently hired Jane Drew to head a new commercial loan division focused on the needs of small companies.

SUMMARY OF AUDIT AND INTERNAL CONTROL ENVIRONMENT

The bank's internal auditor resigned within the past several months and has not been replaced. The bank has an internal controls routine that is performed by the audit staff or other responsible officers. For each area of review, specific functions to be performed are listed. It includes a frequency code indicating a review is performed daily, monthly, semi-annually or annually. However, a review of the list and the responsible personnel shows that some of the listed functions are not audits, but rather operating procedures. In addition, in a few areas supervisors are reviewing their own areas of responsibility which presents an apparent conflict of independence.

According to the President, the external CPA firm has been engaged to perform internal audit work and some limited loan review work. The engagement letter for

the current year had an audit schedule attached; however, no internal audit reports have been received by the bank.

The external audit scope was comprehensive and included direct verification of a sample of loans and deposits, a review of operational procedures and internal controls, a loan review, and analysis of reserve adequacy. The exceptions noted were relatively minor. There were no significant differences between the CPA's loan review and the bank's internal watch list.

SUMMARY OF EXAMINATION PROCEDURES

Loan Portfolio Management - Procedures will focus on policy considerations and the bank's approval process for the extension of small business loans. The loans extended under new Loan Officer Jane Drew will be selected for review. Validation procedures will be used to test the internal loan review system for appropriate classifications. In addition, the credit card loan loan reference will be performed to determine if management processes for the extension of these types of loans are appropriate.

Securities - A limited review will focus on the module's decision factors as the bank purchases only short-term U.S. Treasury issues mitigating any credit and market risk.

Management and Internal Control Evaluation - Efforts will focus on monitoring and adequacy of board oversight due to potential concerns surrounding the resignation of the internal auditor and the lack of true audits in certain functional areas. Also, given the venture into new product lines (small business and credit card loans), a review of the risk assessment for these activities will be performed to assess the planning process and practices.

Capital Adequacy - Given the satisfactory level of capital, the review will only focus on the ability of the bank to maintain the level given the current level of earnings. Review will focus on answering the decision factors.

Earnings - The procedures concerning the level and trend of overhead expenses and noninterest income will be reviewed as these two areas continue to be the contributing factors to the bank's weak earnings performance. Also, a review of the bank's deposit

pricing plan will be reviewed to determine the impact of rate changes. Of importance is management's plans to correct these weaknesses.

Liquidity - A limited review of liquidity should focus on the decision factors given the satisfactory level of performance and minimal risk detailed in the preliminary risk assessment.

Other Assets and Liabilities - Given the lack of reliance that can be placed on internal controls, an expanded analysis should be performed.

SUMMARY OF LOAN REVIEW

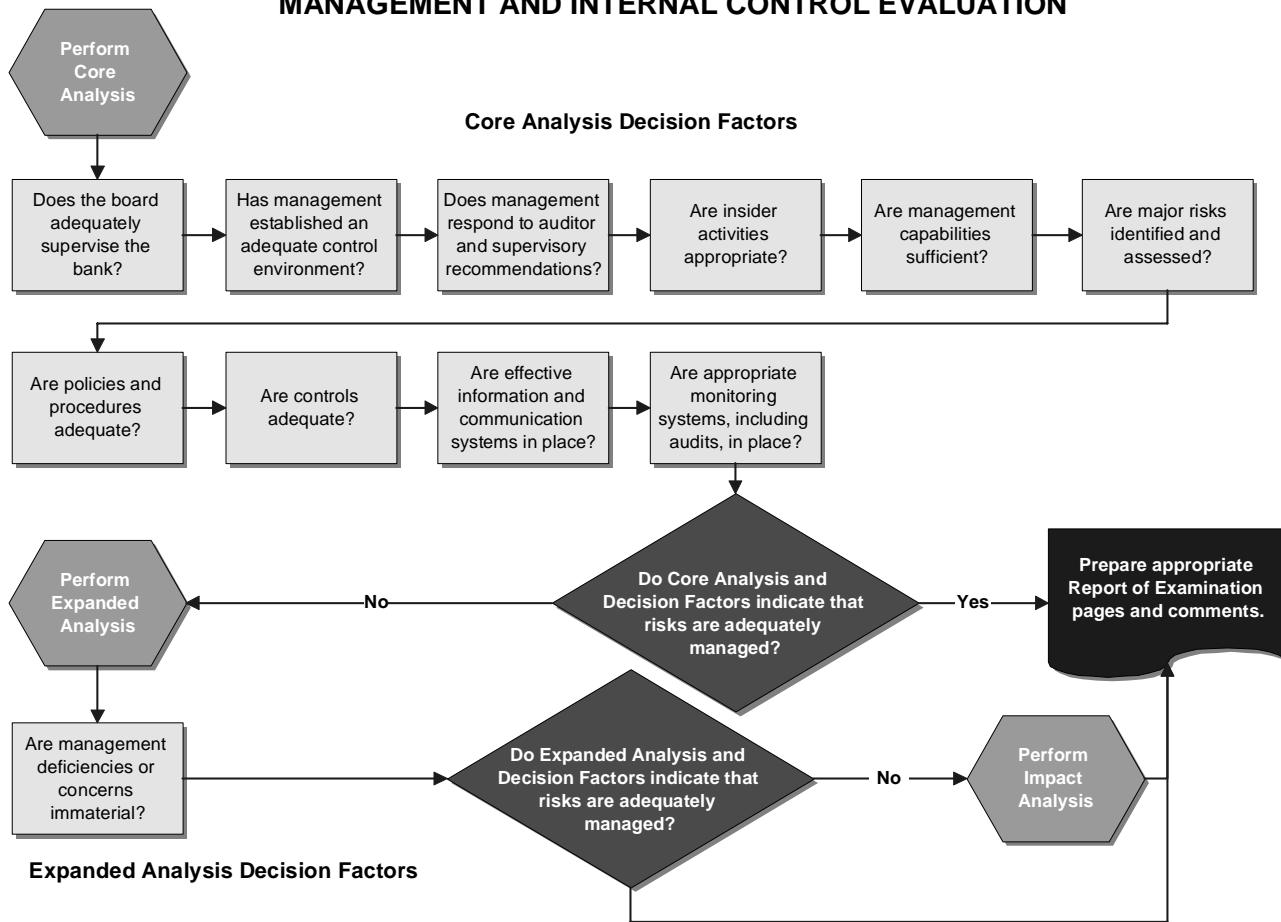
Approximately 60% of total loans were reviewed at the previous examination. Based on the risk assessment and the pre-examination meeting, we plan to start with 45% coverage at this examination. Included in this figure are the larger commercial loans and a significant volume of the loans generated by the new small loan division. We also plan to review the strategies and plans on the planned credit card venture. This level of review should serve to adequately test the bank's internal watch list which has historically been accurate.

Based on the preliminary cutoff, a total of 73 lines will be reviewed. This compares to 122 lines which were reviewed at the previous examination.

JOB STAFFING

Based on the reduced loan review and the modules to be completed, it is estimated that seven examiners will be needed for this one-week examination. Four of the examiners will work on the credit portion of the examination.

MANAGEMENT AND INTERNAL CONTROL EVALUATION



MANAGEMENT AND INTERNAL CONTROL EVALUATION

Evaluate the above-captioned function against the following control and performance standards. The Standards represent control and performance objectives to ensure the bank operates in a safe and sound manner and that the entity's objectives are carried out. Associated Risks represent potential threats to the bank if the standards are not achieved and maintained. The Standards are intended to assist examiners in analyzing important functions that may warrant additional review. All of the following Standards may **NOT** need to be considered at every bank. Conversely, these do **NOT** represent all of the control and performance standards needed for every bank. Examiners should continue to use their judgement when assessing risk.

STANDARDS	ASSOCIATED RISKS
MANAGEMENT AND CONTROL	
<ul style="list-style-type: none"> ▶ An independent board assigns responsibility, delegates authority, and establishes policies to provide a basis for accountability and control. ▶ Lines of authority and responsibilities of management and employees are clearly stated and understood by all personnel. 	<ul style="list-style-type: none"> ▶ The lack of independent oversight could result in a poor control environment. ▶ Inappropriate or deficient organizational structure may result in problems going uncorrected.
<ul style="list-style-type: none"> ▶ The board and executive management have the required knowledge, experience, and training to perform their duties. ▶ The board has a management succession plan, either formally or informally. 	<ul style="list-style-type: none"> ▶ An unqualified board and management team may be ineffective. ▶ Inadequate management succession and depth may disrupt the bank's operations and adversely impact its financial condition.
<ul style="list-style-type: none"> ▶ Management conveys the message that integrity and ethical values will be maintained. ▶ Management implements corrective actions recommended by auditors and supervisory authorities. 	<ul style="list-style-type: none"> ▶ Self-serving practices and conflicts of interest could impair the bank's reputation and increase its exposure to legal risks and losses.
<ul style="list-style-type: none"> ▶ Management conducts risk assessments to identify key business risks. ▶ Management adheres to reasonable risk-taking practices. ▶ Management maintains a system that effectively measures and monitors risks. 	<ul style="list-style-type: none"> ▶ Aggressive and uncontrolled risk-taking practices may increase the bank's exposure to risk. ▶ Internal controls may not be structured properly in areas of high risk. ▶ Capital, asset quality, earnings, and liquidity could be impaired by excessive risk.

STANDARDS	ASSOCIATED RISKS
<ul style="list-style-type: none"> ▶ The board uses an effective planning process and implements dynamic strategies. 	<ul style="list-style-type: none"> ▶ An inadequate planning process may result in poor performance and missed opportunities. ▶ Management may be inflexible to changes in economic, industry, and regulatory environments.
<ul style="list-style-type: none"> ▶ The board establishes control activities encompassing policies and implementation procedures that ensure management's directives are achieved. 	<ul style="list-style-type: none"> ▶ The lack of control activities may prevent the realization of the organization's objectives. ▶ The bank may be exposed to greater risk if adequate policies and procedures addressing key risks are not implemented. ▶ The board and management may be unaware of non-compliance and corrective measures may not be initiated.
<ul style="list-style-type: none"> ▶ A process is in place to ensure relevant information is identified, processed, and reported by information systems. ▶ Information is communicated in an effective manner throughout the organization. 	<ul style="list-style-type: none"> ▶ Insufficient or untimely information prevents individuals from performing their duties effectively.
<ul style="list-style-type: none"> ▶ Management, or a committee, provides the monitoring to ensure an effective system of internal controls, including compliance with laws, regulations, and policy statements. ▶ Management, or a committee, enforces policies and procedures. ▶ The board establishes an effective audit program. 	<ul style="list-style-type: none"> ▶ Ineffective monitoring could result in a poor internal control environment with a high probability of operating losses. ▶ Lack of policy and procedure enforcement could result in insufficient responses to problems and mismanagement of the bank. ▶ Operational weaknesses may not be found; financial or regulatory reporting may be unreliable; and compliance with laws, regulations and internal policies may be jeopardized.

CORE ANALYSIS

Consider the following procedures at each examination. Examiners are encouraged to exclude items deemed unnecessary. This procedural analysis does not represent every possible action to be taken during an examination. The references are not intended to be all-inclusive and additional guidance may exist. Many of these procedures will address more than one of the Standards and Associated Risks. For the examination process to be successful, examiners must maintain open communication with bank management and discuss relevant concerns as they arise.

IMPORTANT

The other examination modules contain specific procedures that will provide insight into management and internal controls in major risk areas. As such, the other examination modules **MUST** be completed prior to the overall assessment of management and internal controls. Coordinate procedures at the beginning of the examination to avoid duplication.

BOARD AND MANAGEMENT SUPERVISION

- ▶ Review board and committee minutes since the last examination as well as the most recent and year-end board packages to determine the extent and adequacy of board supervision. Document important details. Consider the following items:
 - Director attendance.
 - Changes in control since the prior examination.
 - Board independence from executive management.
 - Dominant control by a board member, shareholder, or management executive.
 - Significant changes in direction or activities of the bank.
 - Adequacy of management information systems.
 - Review and approval of policies.
- ▶ Determine changes in the bank's management or directorate since the last examination and review management succession plans. (*Note: This plan can be either formal or informal.*)
 - Assess compliance with Section 32 of the FDI Act, if applicable (Notification of changes in executive management).
 - Assess the impact of management changes on bank operations.
 - Obtain biographical information for new executive officers and directors.
- ▶ Determine if operational expertise is commensurate with the size, complexity, and risk profile of the bank.
- ▶ Determine management's or the board's reliance on external advisors or consultants.

CORE ANALYSIS

Control Environment (*Focuses on senior management's ability to establish a "tone from the top" regarding acceptable business practices, conflicts of interest, and expected behavior to ensure it is communicated and understood throughout the organization.*)

- ▶ Determine if management adequately addresses integrity in its code of conduct, ethics policy, and actions. Review and evaluate the following items:
 - Specific guidelines concerning conflicts of interest and periodic training, including acceptable and unacceptable business practices.
 - Suitable remedial action concerning departures from the policies.
 - Documentation concerning deviations from policies and documentation concerning remedial actions.
- ▶ Determine if management takes adequate corrective action to address recommendations by auditors and regulatory authorities.
- ▶ Determine whether individuals holding executive positions are qualified and fulfilling their duties.
- ▶ Determine whether the organizational structure is appropriate given the size and complexity of the bank.
- ▶ Determine if the board of directors minimizes operating management's ability to override policies and procedures through effective monitoring and enforcement of established guidelines.
- ▶ Review appropriateness of salary levels and compensation arrangements for both the board and executive management. Review the following areas:
 - Board approval of personnel compensation including individual salaries and benefits.
 - Approval of board members' compensation including individual fees and benefits.
 - Bank purchases of life insurance. (*Note: Regional Director Memorandum Transmittal No. 96-084 provides general guidelines provided by OCC Bulletin 96-51 that replaces OCC BC 249.*)
 - Golden parachute agreements. (*Note: Refer to Regional Director Memorandum Transmittal No. 96-026 and FIL-8-96 dated March 29, 1996, and February 16, 1996, respectively.*)
 - Incentive-based compensation.
 - If necessary, supporting documentation from the board regarding compensation practices at comparable institutions, based on such factors as asset size, geographical location, complexity, and risk profile of the bank.
- ▶ Determine if self-serving practices or conflicts of interest exist.

CORE ANALYSIS

- Determine if insiders have undue control over customer files and activities.
 - Determine if insiders are lending personal funds to customers or borrowers. (*Note: The first day letter may request various sources of information on insider transactions.*)
 - Assess if privileges or benefits given to insiders are commensurate with the services rendered.
 - Determine if any insiders are conducting excessive non-bank related business at the bank or are spending inordinate amounts of time away from the bank.
 - Determine if ORE was sold to insiders. If so, review the appropriateness of the transactions.
- ▶ Determine if changes in external auditors or legal counsel occurred and why.

Risk Assessment (*Considers external and internal factors that could impact achievement of the bank's objectives, identifies and analyzes risks, and provides a basis for managing and reacting to changing conditions.*)

- ▶ Review management's risk-taking practices. Assess management's capabilities in the following areas: loans; investments; asset and liability management; growth; nontraditional banking services; deposit structure, rates, and products; and any other areas.
- Determine if management's risk-taking practices are conservative, moderate, or aggressive.
 - Review the controls in place to mitigate any concerns regarding risk-taking practices.
 - Determine if there are any material changes in management's risk-taking practices. For example, changes could occur in the following areas: loans to new borrowers, loan portfolio mix, securities portfolio maturity distribution, new loan products, or asset growth.
- ▶ Determine if management plans effectively. Consider the following issues:
- Strategic plan, budget process, profit plan, and growth projections.
 - Individuals involved with the planning process.
 - Reasonableness of assumptions.
 - Method of comparing actual performance against objectives.
 - Frequency of revisions.
 - Research efforts of new strategic initiatives such as new products and investments, branch expansion, and acquisitions and mergers.

CORE ANALYSIS

- ▶ Determine if management assesses risks that influence the success or failure of established objectives. A formal or informal risk assessment should consider the following areas:
 - External sources of risk:
 1. Technology changes.
 2. Competitors' actions.
 3. Economic conditions.
 4. Political and regulatory conditions.
 - Internal sources of risk:
 1. Retention of key management.
 2. Availability of funds.
 3. Information systems.
 - The significance of the risks identified, the likely impact on the bank, and mitigating actions taken by management.
 - ▶ Determine if risks identified in the examination differ from risks identified by management.
 - ▶ Review the appropriateness of blanket bond insurance levels. Consider the following items:
 - Effectiveness of the bank's internal operations.
 - Amount of cash, securities, and negotiable items normally held.
 - Number, experience, and turn-over rate of personnel.
 - Trust activities.
 - Merchant credit card activities.
 - Data processing activities.
 - Previous fraudulent activities or claims.
 - ▶ Review coverage amounts of other policies including any excess employee fidelity policy.
 - If there are significant fidelity insurance claims determine the reasons.
- Control Activities** *(Encompasses a wide range of policies and the related implementation procedures that help ensure that management's directives are effected.)*
- ▶ Determine if bank policies, procedures, and practices are adequate for the size, complexity, and risk profile of the bank.
 - Review findings from other modules completed during the examination.

CORE ANALYSIS

- ▶ Determine whether control activities are in place to ensure adherence to established policies and review actions taken to address the related risks.
 - Review the findings from other modules completed during the examination.
- ▶ Determine whether management maintains an effective system of controls and safeguards for activities that expose the bank to risk. Consider the following issues:
 - Authorization requirements.
 - Joint custody arrangements.
 - Dual control.
 - Separation of duties.
- ▶ Determine whether the bank maintains off-premises storage of back-up files for all critical records.
- ▶ Determine if management files appropriate suspicious activity reports, if necessary. (*Note: Refer to FIL-69-95*).

Information and Communication (*Includes identifying, capturing, processing, and reporting information by information systems. This information must be communicated throughout the organization.*)

- ▶ Determine whether information systems are in place to identify and capture relevant internal and external information.
 - Assess if the systems are adequate in the higher risk areas.
 - Determine if the bank regularly reviews information systems output for accuracy.
- ▶ Evaluate whether communication of information is sufficient for personnel to carry out their responsibilities.
- ▶ Consider the accuracy of the Call Reports.
 - Review exceptions identified in the other modules.
 - Determine if the bank has a history of Call Report amendments.

CORE ANALYSIS

Monitoring *(Ensures appropriate procedures are in place to periodically evaluate the effectiveness of internal controls, to report deficiencies to appropriate personnel, and to modify policies and procedures.)*

- ▶ Determine if appropriate procedures are in place to monitor risk. Assess risk monitoring with respect to the following:
 - Identifying problem assets.
 - Determining adequacy of the ALLL.
 - Evaluating the risks in the securities portfolio.
 - Monitoring IRR.
 - Achieving strategic initiatives.
 - Pricing.

- ▶ Review the bank's internal audit program. *(Note: For banks with formal internal audit departments, the following procedures should be considered. For those banks with either no audit function or with limited audit activity, monitoring, as defined above, can be evaluated through the other modules.)*
 - Determine whether the audit function is sufficiently segregated from bank operations. Appropriate segregation is generally evidenced by the following items:
 1. The audit department is segregated from operations in the organizational structure.
 2. Audit staff is prohibited from performing any duties in lieu of operating personnel such as preparation of general ledger tickets, daily reconcilements, and dual control.
 3. Reporting procedures of the auditor are independent of the influence of operating personnel.
 4. The audit function reports directly to the board of directors and the audit committee, and the auditor periodically meets with them to review reports issued by the audit function.

 - Determine if there is a formal audit schedule in place to direct audit activities. The following are characteristics of a generally satisfactory plan:
 1. The audit schedule is reviewed and approved.
 2. All important bank functions and services are subject to audit.
 3. Audit procedures are updated as needed.
 4. The auditor periodically reports progress in completing the schedule to the board of directors.
 5. Starting dates and time intervals between audits are changed in order to avoid anticipation by those subject to audit.

 - Determine if audit records are adequate.
 1. A reasonable record retention schedule is maintained for audit records.
 2. Audit workpapers contain approval of significant deviations from audit procedures.
 3. Workpapers contain evidence that audit managers have reviewed the workpapers for findings and final conclusions.
 4. All significant and unresolved exceptions are noted in the workpapers and included in audit reports.
 5. Responsibility for maintaining the audit manual is assigned to appropriate staff.

CORE ANALYSIS

- Determine if the audit department's reporting procedures are adequate.
 1. The auditor submits formal reports to the board of directors or the appropriate committee regarding material weaknesses or other unsatisfactory matters.
 2. The board or appropriate committee supports the audit staff in resolving audit matters.
 3. Departmental managers commit to take specific actions to resolve matters noted in the audit reports.
 4. The audit reports include a summary of the effectiveness of controls in the department or function.
 5. The auditor maintains a formal record of all unresolved audit or regulatory exceptions and recommendations.
- Determine whether the audit staff's academic backgrounds and experience are sufficient for the size and complexity of the bank.

► Review the bank's external audit program.

- If the bank is covered by Part 363 of the FDIC Rules and Regulations, management is required to assess annually the effectiveness of its internal control structure and procedures for financial reporting and the bank's compliance with designated laws. Review the documentation maintained to determine if management adequately assesses the internal control structure and compliance with laws.
- In banks that have chosen not to obtain an external audit, the board of directors should document its reasons including whether the auditing program provides sufficient coverage of areas of potential concern or unique risk. The examiner should review the minutes describing the board's consideration of this audit issue at each examination. If, in the judgement of the examiner, additional external audit coverage is warranted, specific suggestions for addressing these areas should be recommended; however, the lack of an external audit will not automatically result in negative comment.
- Determine if the audit program is in compliance with Part 363, the Statement of Policy Regarding Independent External Auditing Programs of State Nonmember Banks, and the Statement of Policy Providing Guidance on External Auditing Procedures for State Nonmember Banks.

NOTES:

CORE ANALYSIS DECISION FACTORS

Evaluate Core Analysis results in this section for significance and to determine if an Expanded Analysis is necessary. Negative responses to Core Analysis Decision Factors may not require proceeding to the Expanded Analysis. Conversely, positive responses to Core Analysis Decision Factors do not preclude examiners from proceeding to the Expanded Analysis if deemed appropriate.

1. Does the board adequately supervise the affairs of the bank and provide for management depth and succession?
2. Has management established an adequate control environment throughout the organization?
3. Is management responsive to recommendations from auditors and supervisory authorities?
4. Are insider activities appropriate?
5. Are management capabilities sufficient for the type, size, and condition of the bank?
6. Are the major risks that influence the success or failure of the bank identified and assessed?
7. Are policies and procedures generally adequate given the size and complexity of the bank?
8. Are adequate controls in place to ensure adherence to bank policies and legal and regulatory requirements?
9. Are effective information and communication systems in place to enable personnel to carry out their duties?
10. Are appropriate systems, including audits, in place to monitor the activities of the bank?

REPORT OF EXAMINATION PRESENTATION:

- ▶ Discuss analysis, conclusions, and recommendations with the EIC and management prior to completing the following pages as needed:
 - Management/Administration.
 - Assessments as required on the Risk Management pages.
 - Directors and Officers-Confidential.

NOTES:

EXPANDED ANALYSIS

Generally, procedures used in this section should target concerns identified in the Core Analysis and Decision Factors. The flexible guidelines specified in the Core Analysis also apply here.

Note: The procedures outlined in the Expanded Analysis sections of other modules in aggregate represent the Expanded Analysis of management and internal controls. Consider the results and recommendations derived from those modules.

- ▶ Determine why an ethics policy has not been adopted. Obtain management's response to examiner recommendations.
- ▶ Determine the significance of insider abuses identified in the other modules.
- ▶ Determine why the bank does not have fidelity insurance and review the steps management is taking to mitigate the consequences of not having insurance coverage.

NOTES:

EXPANDED ANALYSIS DECISION FACTORS

The following questions will help to evaluate the significance and materiality of deficiencies or other specific concerns identified in the Core and Expanded Analyses.

1. Are management deficiencies or concerns immaterial?

- Does management have the ability and commitment to implement corrective measures to effectively address deficiencies or concerns?

REPORT OF EXAMINATION PRESENTATION:

NOTE: Only prepare supplemental pages that support examination comments and conclusions.

- ▶ Discuss analysis, conclusions, and recommendations with the EIC and management prior to completing the following pages as needed:
 - Those pages listed in the Core Analysis Decision Factor section.
 - Violations of Laws and Regulations.
 - Examination Conclusions and Comments.
 - Matters Requiring Board Attention.
 - Confidential-Supervisory Section.

NOTES:

IMPACT ANALYSIS

This section helps to evaluate the impact of deficiencies identified in the Core and Expanded Analyses and Decision Factors on the bank's overall condition. This section also directs the examiner to consider possible supervisory actions.

- ▶ Determine whether management deficiencies or suspicious activities have resulted or could result in increased asset quality problems, deteriorated earnings, decreased capital protection, or undue risk to the bank.
- ▶ Consider whether an informal or formal enforcement action is warranted, such as an MOU, a Cease and Desist Order, or a removal action. Advise the Field Office Supervisor and the Regional Office on the nature of supervisory concerns.

CIVIL MONEY PENALTIES

- ▶ Prepare recommendations for Civil Money Penalties, if appropriate. The FDIC manual details specific instances in which CMPs may be assessed. *(Note: Examiners should no longer refer to the FDIC's authority to impose civil money penalties in the reports of examination. Refer to RD Memo Transmittal Number 93-94).*
 - Complete the CMP matrix (contained in the Manual and the FDIC icon) for fineable violations, unsafe and unsound practices, or breach of fiduciary duties. The matrix should be prepared whenever an examiner is considering a penalty. The interagency statement of policy sets forth thirteen factors to consider when determining whether civil money penalties should be imposed:
 1. Evidence that the violation or pattern of violations was intentional or committed with a disregard of the law or the consequences to the institution.
 2. The frequency or recurrence of violations and the length of time the violation has been outstanding.
 3. Continuation of violation after the respondent becomes aware of it, or its immediate cessation and correction.
 4. Failure to cooperate with the agency in effecting early resolution of the problem.
 5. Evidence of concealment of the violation, or its voluntary disclosure.
 6. Any threat of or actual loss or other harm to the institution, including harm to public confidence in the institution, and the degree of any such harm.
 7. Evidence that participants or their associates received financial or other gain, benefit, or preferential treatment as a result of or from the violation.
 8. Evidence of any restitution by the participants in the violation.
 9. History of prior violations, particularly where similarities exist between those and the violations under consideration.
 10. Previous criticism of the institution for similar violations.
 11. Presence or absence of a compliance program and its effectiveness.
 12. Tendency to create unsafe or unsound banking practices or breach of fiduciary duty.
 13. The existence of agreements, commitments, or orders intended to prevent the subject violation.
- ▶ CMP recommendation should only be considered if it meets the test of gravity after considering the above 13 points and when any one of the following criteria is present:
 - The bank suffers a substantial financial loss as a result of the violation.

IMPACT ANALYSIS

- The violation is willful, flagrant, or otherwise evidences bad faith on the part of the bank or individual involved in the violation.
 - An insider (or associate) directly or indirectly involved in the violation materially benefited from the transaction.
 - Previous supervisory means have not been effective in eliminating or deterring violations.
- ▶ If the examiner decides to recommend CMPs, the following procedures should be implemented:
- Consult with the Regional Office to determine the documentation necessary to support the violation and the CMP recommendation.
 - Prepare a memorandum to the appropriate Regional Director addressing the 13 points and specifying the recommendation.
 - Include the home mailing addresses for all directors and any other individuals involved in a fineable violation in the confidential pages.
 - Discuss the violations with management, but, if necessary to discuss CMPs, limit discussions to the criteria used to determine whether to assess a penalty.
 - Examiners should not discuss penalties regarding Section 8 matters. If questioned, discussions should be limited to stating that CMPs can be assessed for noncompliance with an order. (*Note: Only the Regional Director can determine compliance with a Section 8 Order.*)
 - If the violation involves financial gain to an insider or financial loss to the bank, examiners should attempt to quantify the amount of loss. The violation writeup should include the monetary amount and method of calculation. If the amount can not be determined, the examiner should include the reason why.
 - Copy evidence supporting the violations and retain in field office files in a separate labeled folder apart from the regular workpapers.

SUSPICIOUS ACTIVITY REPORTS

- ▶ Notify the Regional Office of suspected activities and actions taken.
- ▶ Discuss the possibility of administrative and enforcement actions with executive management and the board of directors. If suspicious activity is discovered, and the Regional Office concurs, examiners should report the discovery of the suspicious activity and any related apparent violations to the bank's board of directors.
- Examiners should present the facts giving rise to the apparent violation, but avoid any conclusions as to guilt or innocence of any particular individuals.
 - Remind the board of the regulatory requirements to report apparent violations promptly to law enforcement agencies and the Regional Director.

IMPACT ANALYSIS

- ▶ Determine if management has or will file Suspicious Activity Reports (SARs). *(Note: Examiners should generally bring apparent criminal activities to management's attention for reporting by the bank. Under certain situations, it may not be appropriate to notify bank officials.)*
- ▶ Prepare an SAR if the report submitted by the bank is deemed inadequate or the suspected criminal conduct has not been reported by the bank and the examiner believes it is best for the FDIC to prepare the report. *(Note: Refer to RD memo 96-027 for guidance on preparing and submitting SARs to the interagency SAR system. An SAR prepared and entered into the SAR system by the bank does not prevent examiners from making a more detailed report. SARs should be completed when the examiner first obtains evidence to support a belief that a crime has been committed. Do not wait until the examination concludes.)*
- ▶ Each field office should have a SAR manual and related software. If the FDIC is preparing the SAR, examiners should prepare the report using the software and submit it to the Regional Director.
 - Attach copies of documents that prove or support the suspected criminal violations.
 - Segregate and store additional supporting documents.
- ▶ If authorized by the Regional Director, the examiner may communicate the details of a criminal referral directly to the FBI or the US Attorney's office.

REPORT OF EXAMINATION PRESENTATION:

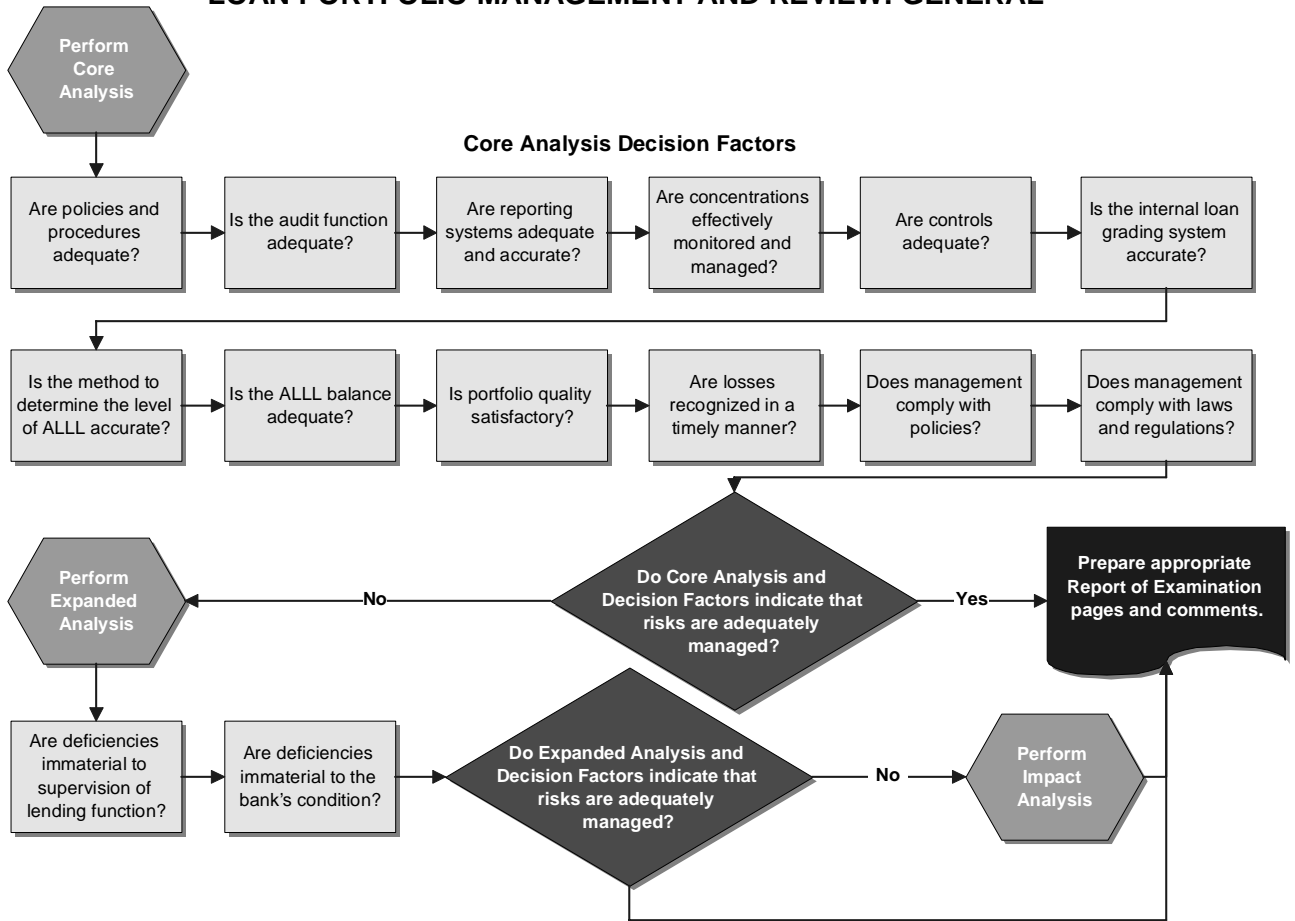
NOTE: Only prepare supplemental pages that support examination comments and conclusions.

- ▶ Discuss analysis, conclusions, and recommendations with the EIC and management prior to completing the following pages as needed:
 - Those pages listed in the Expanded Analysis Decision Factor section.

IMPACT ANALYSIS

NOTES:

LOAN PORTFOLIO MANAGEMENT AND REVIEW: GENERAL



LOAN PORTFOLIO MANAGEMENT AND REVIEW: GENERAL

Evaluate the above-captioned function against the following control and performance standards. The Standards represent control and performance objectives to ensure the bank operates in a safe and sound manner and that the entity's objectives are carried out. Associated Risks represent potential threats to the bank if the standards are not achieved and maintained. The Standards are intended to assist examiners in analyzing important functions that may warrant additional review. All of the following Standards may **NOT** need to be considered at every bank. Conversely, these do **NOT** represent all of the control and performance standards needed for every bank. Examiners should continue to use their judgement when assessing risk.

STANDARDS

ASSOCIATED RISKS

NOTE: References to lending policies and loan functions in this section include off-balance sheet lending activities. Analysis of lending functions must consider off-balance sheet lending activities.

MANAGEMENT AND CONTROL

▶ The board establishes adequate lending policies, procedures, and operating strategies.

▶ Inadequate lending policies and procedures expose the bank to greater credit, interest rate, liquidity, and other risks.

▶ Lending objectives are not consistent with the bank's overall goals.

▶ Management adheres to and supports policies regarding conflicts of interest and insider dealing.

▶ Public confidence and funding sources may be lost if guidelines are not followed.

▶ Violation of policies, procedures, rules and regulations, and criminal statutes result.

▶ The lending area is adequately staffed for planned objectives, and personnel are knowledgeable and competent for the size and nature of the bank's lending functions.

▶ Poorly administered loans may cause greater portfolio risk.

▶ Insufficient knowledge impedes management's ability to adapt to changes in economic conditions, technology, products, etc.

▶ Unqualified lenders may inadequately underwrite and analyze credits.

▶ The potential for loan losses and poor financial performance increases.

▶ Management may be unable to monitor lending activities effectively.

▶ Inadequate staffing could result in insufficient collection activity and monitoring.

STANDARDS	ASSOCIATED RISKS
<ul style="list-style-type: none"> ▶ A knowledgeable and independent board of directors and committees of the board supervise the affairs of the bank. 	<ul style="list-style-type: none"> ▶ Unqualified management ineffectively monitors and controls lending activities. ▶ Concentrated authority in the lending area could create ineffective checks and balances. ▶ The potential for self-serving practices and conflicts of interest increases. ▶ The board may not develop and enforce accountability and performance standards.
<ul style="list-style-type: none"> ▶ Management assigns prudent lending authorities to officers and committees. 	<ul style="list-style-type: none"> ▶ The potential for over-lending to individuals and industries heightens. ▶ Certain loan officers may not be experienced enough to originate large or high-risk loans. ▶ The lack of lending authorities impedes loan officer accountability and oversight.
<ul style="list-style-type: none"> ▶ Management identifies and analyzes relevant risks. 	<ul style="list-style-type: none"> ▶ Inadequate analysis could result in excessive credit risk. ▶ Loan pricing may not reflect risks. ▶ Lending objectives may not be achieved.
<ul style="list-style-type: none"> ▶ Procedures exist to identify and react to changing economic, industry, and regulatory environments. 	<ul style="list-style-type: none"> ▶ Management may violate new or revised regulations. ▶ Economic changes may cause unfavorable financial performance. ▶ Concentrations of credit could deteriorate. ▶ Rapid and uncontrolled growth may occur.
<ul style="list-style-type: none"> ▶ Loan information systems provide management with relevant information. 	<ul style="list-style-type: none"> ▶ Ineffective information systems could lead to uninformed business decisions, inappropriate reaction to external influences or internal results, and lost opportunities. ▶ Poor communication could result in inadequate accountability and oversight of lending personnel.

STANDARDS	ASSOCIATED RISKS
<ul style="list-style-type: none"> ▶ Loan committee meets regularly to review and approve loans. 	<ul style="list-style-type: none"> ▶ Lack of direction and oversight may cause imprudent lending decisions and increase credit risk.
<ul style="list-style-type: none"> ▶ Management performs effective and timely evaluations of loan portfolio quality and conformance with established lending policies. 	<ul style="list-style-type: none"> ▶ Unauthorized high-risk loans could go undetected. ▶ Losses might not be easily traced to the responsible department or individual. ▶ Underwriting controls could break down and lending practices depart from established corporate policies and procedures.
<ul style="list-style-type: none"> ▶ Management follows an appropriate method for determining the level of the Allowance for Loan and Lease Losses (ALLL). 	<ul style="list-style-type: none"> ▶ The ALLL could be inadequate to absorb estimated losses in lending activities, including off-balance sheet lending activities.
<ul style="list-style-type: none"> ▶ Internal reviews and audits discuss deficiencies in the lending function, and reports are provided directly to senior management and the board. 	<ul style="list-style-type: none"> ▶ Identification, communication, and correction of deficiencies may be inadequate.
<ul style="list-style-type: none"> ▶ Management has established adequate internal controls for its lending operation. 	<ul style="list-style-type: none"> ▶ Weak controls may increase the bank's exposure to errors and omissions. ▶ Inadequate controls increase the potential for fraud and abuse.
<ul style="list-style-type: none"> ▶ Controls exist to ensure adherence to accounting standards. 	<ul style="list-style-type: none"> ▶ Failure to use proper accounting could result in material misstatement of income and capital levels.
PERFORMANCE	
<ul style="list-style-type: none"> ▶ Bank officers comply with established guidelines and policies. 	<ul style="list-style-type: none"> ▶ Officers may originate unauthorized loans.
<ul style="list-style-type: none"> ▶ Internal loan review functions accurately identify loan problems. 	<ul style="list-style-type: none"> ▶ Failure to detect existing and emerging loan problems could result in escalating problem assets.
<ul style="list-style-type: none"> ▶ Management recognizes losses in a timely manner. 	<ul style="list-style-type: none"> ▶ Deferred loan losses overstate current period earnings. ▶ Understated losses could result in inaccurate financial reports.

STANDARDS	ASSOCIATED RISKS
<ul style="list-style-type: none"> ▶ The overall quality of the loan portfolio is satisfactory. 	<ul style="list-style-type: none"> ▶ Sub-quality loans increase loan losses and operating expenses and can erode capital. ▶ Officers spend an inordinate amount of time collecting and monitoring loans.
<ul style="list-style-type: none"> ▶ Loan operations meet profit targets. 	<ul style="list-style-type: none"> ▶ The net interest margin may be reduced.
<ul style="list-style-type: none"> ▶ Credit files contain timely and accurate documentation. 	<ul style="list-style-type: none"> ▶ Incomplete documentation impedes management's ability to properly analyze borrowers' creditworthiness. ▶ Undetected loan problems and financial weaknesses delay successful workout agreements. ▶ Improperly perfected liens and missing documentation hinder efforts to foreclose or repossess collateral.
<ul style="list-style-type: none"> ▶ The bank complies with all laws and regulations related to the lending function. 	<ul style="list-style-type: none"> ▶ Intentional and continuing violations could result in costly penalties and increased supervisory oversight. ▶ Regulators, shareholders, and customers may lose confidence in the bank and its executive management.
<ul style="list-style-type: none"> ▶ The ALLL adequately protects against the risks inherent in the bank's loan portfolio and off-balance sheet lending activities. 	<ul style="list-style-type: none"> ▶ An insufficient ALLL results in an overstated capital position and earnings. ▶ An under-funded ALLL results in inaccurate financial reports to shareholders and regulators. ▶ Loan losses might exhaust the ALLL and erode capital.

CORE ANALYSIS

Consider the following procedures at each examination. Examiners are encouraged to exclude items deemed unnecessary. This procedural analysis does not represent every possible action to be taken during an examination. The references are not intended to be all-inclusive and additional guidance may exist. Many of these procedures will address more than one of the Standards and Associated Risks. For the examination process to be successful, examiners must maintain open communication with bank management and discuss relevant concerns as they arise.

IMPORTANT

References to lending policies and loan functions in this section include off-balance sheet lending activities. Analysis of lending functions must consider off-balance sheet lending activities.

- ▶ Review prior examination reports, pre-examination memorandum, and file correspondence for an overview of any previously identified lending deficiencies.
- ▶ Review interim internal and external audit reports, and assess the adequacy of the audit scope.
- ▶ Review remedial actions taken by management to correct audit and examination deficiencies. (*Note: Disseminate information to examiners responsible for specialty lending areas.*)
- ▶ Discuss with management any planned changes in lending philosophy, portfolio composition, new products, pricing strategies, etc. Determine if current and planned lending strategies are consistent with the bank's overall strategic plan.
 - ▶ Review loan committee minutes for completeness, any identified lending problems, and consideration of approved exceptions to established lending policies including off-balance sheet lending activities.

POLICY CONSIDERATIONS

- ▶ Determine if lending policies, procedures, and practices are adequate for the lending activities of the bank.
 - Evaluate the frequency and timeliness of reviews and updates by the board of directors.
 - Determine the adequacy of guidelines established for financial analysis including borrower equity, borrower liquidity, and borrower cash flow and income.
 - Determine if policies include the following broad areas of concern:
 1. General fields of lending in which the bank will engage and the kinds or types of loans within each general field.
 2. Lending authority of each loan officer.
 3. Lending authority of a loan committee or executive committee.
 4. Responsibility of the board of directors in reviewing, ratifying, or approving loans.
 5. Guidelines under which unsecured loans will be granted.
 6. Guidelines for rates of interest and the terms of repayment for secured and unsecured loans.

CORE ANALYSIS

7. Limitations on the amount advanced in relation to the value of the collateral and documentation required by the bank for each type of secured loan (Part 365 - Real Estate Lending Standards).
8. Guidelines for obtaining and reviewing appraisals of real estate or other collateral as well as for ordering reappraisals.
9. Maintenance and review of complete and current credit files on each borrower.
10. Appropriate and adequate collection procedures including, but not limited to, actions to be taken against borrowers who fail to make timely payments.
11. Limitations on the maximum volume of loans in relation to total assets.
12. Guidelines for purchased loans.
13. Limitations on the extension of credit through overdrafts.
14. Description of the bank's normal trade area and circumstances under which the bank may extend credit outside the area.
15. Guidelines which address the goals for portfolio mix and risk diversification and cover the bank's plans for monitoring and taking appropriate corrective action on any existing concentrations.
16. Guidelines addressing the bank's loan review and grading system ("Watch list").
17. Guidelines addressing the bank's review of the Allowance for Loan and Lease Losses.
18. Guidelines for adequate safeguards to minimize potential environmental liability.
19. Guidelines regarding loans to insiders.
20. Guidelines for all current lending products.

► Review the bank's loan approval process.

• Determine if loan presentations include an adequate analysis of the following items:

1. Loan purpose.
2. Repayment source.
3. Collateral.
4. Background of borrower.
5. Principals and management.
6. Financial information including balance sheet and income statement.
7. Financial projections.
8. Industry and economic outlooks.
9. Cash flows.
10. Borrowing and deposit histories.
11. Loan structure and terms.
12. Loan covenants.

► Ascertain if the loan review policies are adequate for the size and complexity of the bank.

• Verify that the loan review policies meet the following objectives:

1. To promptly identify loans having potential credit weaknesses, and appropriately classify loans with well-defined credit weaknesses that jeopardize repayment so that timely actions can be taken and credit losses minimized.
2. To project relevant trends that affect the collectibility of the portfolio and isolate potential problem areas.
3. To provide essential information to determine the adequacy of the ALLL.
4. To assess the adequacy of and adherence to internal credit policies and loan administration procedures, and to monitor compliance with relevant laws and regulations.

CORE ANALYSIS

5. To evaluate the activities of lending personnel.
6. To provide senior management and the board with an objective and timely assessment of the overall quality of the loan portfolio.

- Verify that updates to the “watch list” are performed in a timely manner.
- ▶ Consider providing a written summary of key provisions in the lending policies for examiners reviewing loans.
- ▶ Determine if executive management and loan officers are aware of established lending policies and practices.
- ▶ Determine the accuracy of loan reports produced for the board and executive management.
- ▶ Review management’s procedures to prevent, detect, and respond to lending policy exceptions.
- ▶ Review the details of any lending incentive compensation programs. Determine if amounts distributed agree to what was approved by the board of directors.
- ▶ Determine if lending officers’ skills are commensurate with their lending responsibilities. Possible ways of measuring skill levels include the following items:
 - Review lending area job descriptions.
 - Review individual resumes.
 - Evaluate the expertise of lending officers during loan discussions.
- ▶ Determine the extent and adequacy of training and continuing education provided to lending personnel.
- ▶ Evaluate the business experience of loan committee members. Determine if members are independent and qualified to function effectively.

PORTFOLIO ANALYSIS

- ▶ Validate the composition of the loan portfolio by type and dollar volume by reviewing the bank’s Call Report workpapers and account reconciliations. Determine specialty lending areas and assign responsibility for completing appropriate reviews. Refer to individual specialty Loan References for additional guidance.
- ▶ Review overdraft, large items, and uncollected funds reports for possible check kiting or other irregular activity. Pay particular attention to overdrafts of bank insiders and insiders of other banks.

CORE ANALYSIS

- ▶ Determine the adequacy of subsidiary loan record reconciliations to the general ledger. Consider the following items:
 - Frequency of reconciliations.
 - Disposition of reconciling amounts.
 - Separation of duties. (Reconciliations should not be performed by persons responsible for posting or who handle cash or official checks.)
- ▶ Review the accuracy of accounting for loans sold and participations. Consider partial sales and recourse arrangements.
- ▶ Determine if controls exist over loan closings and disbursements. Consider the following issues:
 - Documentation is complete and appropriate waivers are obtained before loans are funded.
 - Use of documentation waivers is not excessive.
 - Funds are disbursed in accordance with loan terms.
- ▶ Ascertain if items held in suspense accounts clear in a timely manner.
- ▶ Confirm the amount of off-balance sheet lending activities that management expects to fund. (*Note: Provide this information to examination personnel reviewing liquidity.*)
 - Verify if commitments are limited in amount, cover a specific period of time, and indicate the conditions that must be satisfied before draws will be honored.
- ▶ Evaluate the current level and trend of past due ratios for each type of credit.
- ▶ Calculate all applicable lending limits, and determine how the bank aggregates related credits and tests for conformity to lending limits.
- ▶ Analyze growth trends by total and loan type, and determine if actual data satisfactorily mirrors budgeted growth plans.
- ▶ Validate the bank's internal loan review system and assigned classification ratings. Also evaluate any documentation exception reports and written classification summaries. Evaluate frequency and timeliness of reports to the board of directors. (*Note: Preliminary sampling at this level should be sufficient to judge the accuracy of the internal loan review system without becoming so large that examiners duplicate efforts established by banks with satisfactory internal reviews. An inaccurate internal loan review system will result in expanded loan sampling.*)

CORE ANALYSIS

To properly measure the accuracy of the internal loan review, examiners should evaluate a cross section of loans by type, size, and severity of classification.

- Sample “watch list” loans and assess if management’s ratings are accurate. When developing the sample consider the following:
 1. Credits representing the greatest inherent risk to the bank (for example, commercial, commercial real estate).
 2. Severity of the internal classification.
 3. Multiple credit types and categories.
 4. Loans to industries or groups affected by adverse economic trends.
 5. Loans to facilitate the sale of bank assets or loan collateral. (Ensure compliance with SFAS 66 and APB 21.)
 - Sample loans **not** on the watch list to validate the internal loan review process, considering the following:
 1. Previously classified and Special Mention loans.
 2. Significant overdue and nonaccrual loans.
 3. Loans to insiders, their related interests, and affiliates.
 4. Significant newly extended credits since the previous examination.
 5. New types of loans.
 6. Loans originated by each loan officer and loan officers with unusually high loss ratios.
 7. Other significant credits as determined by the EIC, including loans to industries or groups affected by adverse economic trends.
 8. Loans to facilitate the sale of bank assets or insider assets or loan collateral.
 9. Loans at a seasonal low point that could represent large credits when fully drawn.
- ▶ Review any loans to out-of-territory borrowers who also have large deposits. Determine if the loans were offered at favorable loan terms as a result of the large deposit relationship.
 - ▶ Review any transactions where broker’s fees are paid from the proceeds of related loans instead of being paid directly by the bank as a cost of obtaining the funds.
 - ▶ Evaluate the extent to which loan renewals and extensions are used to maintain otherwise underperforming loans current.
 - ▶ Determine the bank’s practices regarding capitalization of interest.
 - ▶ Evaluate management’s procedures for limiting risk in concentrations of credit by industry, type, person, etc.
 - ▶ Determine if the bank effectively manages environmental risk.

CORE ANALYSIS

- ▶ Determine if the bank's financial analysis of borrowers is adequate in relation to the size and complexity of the debt.
 - Review financial analysis for appropriate financial ratios, trends, cash flow history, and projections sufficient to determine the financing needs and repayment capacity of the borrower.
 - Assess whether the bank's review evaluates important items such as salaries, fees, dividends, notes and accounts receivable, and notes and accounts payable, including those to insiders.
 - Determine whether significant balance sheet and income statement changes are properly explained and whether the bank identifies and reviews contingent liabilities.
 - Evaluate the bank's comparison of actual results to projected performance.
 - Consider the prospects for support from any financially responsible guarantors, with emphasis on excess liquidity, cash flow, and demonstrated willingness to honor guaranty agreements.
- ▶ Determine if the bank is tracking borrowers' compliance with financial and reporting covenants.
- ▶ Determine if the bank maintains adequate documentation. Consider the following items:
 - Certificate of good standing.
 - Financial statements. (Balance sheet, income statement, cash flow).
 - Certified borrower resolutions authorizing the loan or guaranty and collateral attachment.
 - Guaranty forms.
 - Documentation of title to assure proper lien position.
 - Evidence of proper collateral attachment and public filing. (Security agreement or real estate lien instrument and properly filed financing statement (UCC-1) or other form of recordation in public files).
 - Evidence of insurance.
- ▶ Determine if underwriting practices are acceptable. Consider the following items:
 - Loans have adequate credit and collateral documentation.
 - Pricing, recourse provisions, and loan to value requirements reflect underlying credit risk.
 - The purpose of the borrowing is identified.
 - Terms are consistent with officer, committee, and board approvals.
 - Debt amortization and maturity consider the timing and duration of borrower cash flows.
 - Additional advances to an existing loan are supported by evidence that the loan will be repaid.

CORE ANALYSIS

- Renewals, extensions, and refinancings have reliable repayment sources and repayment schedules are reasonable.
- ▶ Determine if the proper level of approval is documented.
- ▶ Discuss individual loans with management and loan officers when appropriate.
- ▶ Assign classifications to credits reviewed from the above samples, and evaluate the internal loan classifications for accuracy. *(Note: If the internal grading system is reliable, use the bank's data for preparing appropriate report pages, for determining the overall level of classifications, and for providing supporting comments regarding the quality of the loan portfolio. If internal classifications are overly conservative, examiners should make adjustments as deemed appropriate.)*

ALLOWANCE FOR LOAN AND LEASE LOSSES (ALLL)

IMPORTANT

Primary guidance is found in the Interagency Policy Statement on the Allowance for Loan and Lease Losses dated December 21, 1993.

- ▶ Evaluate the bank's method for determining the adequacy of the ALLL, including all binding commitments to lend. *(Note: Refer to SFAS 114.)*
 - Determine if management maintains an adequate ALLL, after deducting all portions of the portfolio classified Loss, considering the sum of the following items:
 1. For loans and leases classified Substandard or Doubtful, all estimated credit losses over the remaining effective lives of these loans.
 2. Estimated credit losses on loans and leases not adversely classified.
 3. Amounts for estimated losses from transfer risk on international loans.
 - Evaluate the frequency of the bank's ALLL evaluation process. *(Note: ALLL evaluations must be done on at least a quarterly basis.)*
 - Determine if management's analysis is conservative so that the overall ALLL appropriately reflects a margin for the imprecision inherent in most estimates of expected credit losses. In carrying out their responsibility for maintaining an adequate ALLL, the board of directors and management are expected to implement the following procedures:
 1. Ensure that the bank has an effective loan review system and controls.
 2. Ensure that management promptly charges off loans, or portions of loans, that are uncollectible.
 3. Ensure that the bank's method is based on a comprehensive, adequately documented, and consistently applied analysis of the bank's loan and lease portfolio. The methods should consider all significant factors that affect the collectibility of the portfolio and supports the range of credit losses estimated by the process.

CORE ANALYSIS

- Determine if the complexity and scope of the bank's ALLL evaluation process, loan review system, and other relevant controls are appropriate given the size of the bank and its lending activities.
 - Determine if the bank relies primarily on analyzing its various loan categories, including significant credits, on an individual basis.
 - Examine the factors that management uses in estimating credit losses.
 - Determine if management considers any factors that are likely to cause estimated credit losses to differ from historical loss experience:
 1. Changes in lending policies and procedures, including underwriting standards and collection, charge-off, and recovery practices.
 2. Changes in national and local economic business conditions and developments, including the condition of various market segments. (*Note: Credit loss and recovery experience may vary significantly depending upon the business cycle.*)
 3. Changes in the nature and volume of the portfolio.
 4. Changes in the experience, ability, and depth of lending management and staff.
 5. Changes in the trend of the volume and severity of past due and classified loans, and trends in the volume of nonaccrual loans, troubled debt restructurings, and other loan modifications.
 6. Changes in the quality of the bank's loan review system and the degree of oversight by the bank's board of directors.
 7. The existence and effect of any concentrations of credit, and changes in the level of such concentrations.
 8. The effect of external factors such as competition and legal and regulatory requirements.
 - Determine if documentation is maintained to support the adequacy of the ALLL.
- ▶ Evaluate the overall level of the ALLL for reasonableness.
- If the bank's internal loan review system and method for determining ALLL adequacy is accurate, compare the bank's result to the current ALLL balance.
 - Consider reviewing applicable UBPR ratios as a check for reasonableness.

APPRAISAL REVIEWS

- ▶ When reviewing compliance with appraisal regulations (Part 323), determine if the board has approved a list of appraisers. This list is typically contained as part of the loan or appraisal policy.
- Spot check licenses or certifications to verify authenticity. (License terms depend on state law.)
 - Ensure management has confirmed whether or not appraisers are currently licensed or certified to operate in the states in the bank's lending area.
- ▶ If an appraisal is required under Part 323 (refer to specific regulation to determine requirements), evaluate the appraisal to ensure compliance with the regulation.

CORE ANALYSIS

VIOLATIONS REVIEW

The following procedures cover assessing compliance with common regulations relating to loan and lease reviews. The descriptions are brief overviews, and if an examiner suspects an apparent violation, he/she should reference the applicable regulations and state laws.

Extensions of Credit that Exceed a Bank's Legal Loan Limit

- ▶ Review the loan trial balance, particularly the large borrower list, to determine if any borrowing relationships exceed the bank's statutory lending limit.

Extensions of Credit to Insiders *(Note: Examiners should use the Rules and Regulations as their primary guidance regarding Regulation O issues.)*

- ▶ Review extensions of credit originated to insiders since the previous examination. Determine if extensions of credit meet the requirements of Regulation O. Consider the following items:
 - The adequacy of bank records identifying insiders, their interests, and related transactions.
 - The accuracy and completeness of board minutes and insider information provided by management.
 - Approvals for insider transactions, including terms, credit worthiness, and prior approval.
 - Conformity to Regulation O lending limits.
 - Overdraft history.
 - Cash items held for insiders or their related interests.
 - Disclosure statements submitted by executive officers reporting indebtedness to correspondent banks.

Loans Collateralized by Securities

- ▶ Review compliance with applicable state laws that govern extensions of credit secured by own bank stock.
- ▶ If the bank extends credit for the purpose of purchasing or carrying margin stock, ensure compliance with the Federal Reserve's Regulation U. (If the stock is secured directly or indirectly by margin stock, Regulation U is applicable.)

Notes:

CORE ANALYSIS DECISION FACTORS

Evaluate Core Analysis results in this section for significance and to determine if an Expanded Analysis is necessary. Negative responses to Core Analysis Decision Factors may not require proceeding to the Expanded Analysis. Conversely, positive responses to Core Analysis Decision Factors do not preclude examiners from proceeding to the Expanded Analysis if deemed appropriate.

Note: Consider off-balance sheet activities and contingent liabilities.

1. Are loan policies and procedures adequate for the bank's current and anticipated areas of lending?
2. Does the audit function adequately cover lending activities?
3. Are reporting systems for the lending function adequate and accurate?
4. Are loan concentrations effectively monitored and managed?
5. Are controls adequate?
6. Is the bank's internal grading system accurate?
7. Is the method used to determine the level of ALLL accurate?
8. Is the ALLL balance adequate?
9. Is loan portfolio quality satisfactory?
10. Are loan losses recognized in a timely manner?
11. Does management generally comply with the above policies and procedures?
12. Does management comply with applicable laws and regulations?

REPORT OF EXAMINATION PRESENTATION

- ▶ Discuss analysis, conclusions, and recommendations with the EIC and management prior to completing the following pages as needed:
 - Appropriate items on the Risk Management pages.
 - Comments for the Asset Quality page.
 - Summary of Items Subject to Adverse Classification and Special Mention.
 - Consider including any classified item write-ups that management disagrees with.
 - Comments for the Management/Administration page.

Notes:

EXPANDED ANALYSIS

Generally, procedures used in this section should target concerns identified in the Core Analysis and Decision Factors. The flexible guidelines specified in the Core Analysis also apply here.

POLICIES AND PROCEDURES

- ▶ Investigate why the lending and loan review policy or procedure deficiencies identified in the Core Analysis exist. Discuss with management its response to examiner recommendations. *(Note: The Core Analysis reveals what the deficiencies are, whereas the Expanded Analysis is focused on the circumstances causing the deficiencies and management's ability to implement corrective action.)*

Possible reasons for policy deficiencies may include the following circumstances:

- Management overlooked these issues.
 - Management is unfamiliar with prudent loan and loan review guidelines and procedures.
 - Management is unwilling to create or enhance policies and procedures.
- ▶ If poor compliance with policies and procedures exist, determine the reasons. Possible reasons are detailed below:
 - Poor internal communication of policy and procedures or subsequent revisions.
 - Lack of awareness of policy existence.
 - Disregard for established policies.
 - Misunderstanding of policy or procedures.
 - ▶ Determine if management commits to and supports proper controls and monitoring to ensure policy and procedures are followed in the future. Determine if proposed controls, if any, are reasonable.

REPORTING SYSTEMS

- ▶ Research the inaccuracies or inadequacies in the loan reporting systems to determine the underlying cause.
- ▶ Determine if exception reports portray extensions, renewals, and other changes in customer account status which are produced and reviewed by operating management.
- ▶ Consider confirming a sample of participations purchased and sold.

CONCENTRATIONS

- ▶ Investigate the reasons that information systems do not adequately identify and properly aggregate concentrations of credit or related credits (industry and common borrower).

EXPANDED ANALYSIS

- ▶ Consider expanding the sample of loans (including off-balance sheet activities) within the industry concentration(s), particularly if concerns exist about concentration size, management, or adverse economic trends.

CONTROLS

- ▶ If internal loan reconcilements are inadequate, perform loan account reconcilements.
- ▶ Determine if management gives proper attention to out-of-balance conditions and does not charge off or close out small balances without investigation.
- ▶ Evaluate the ability of loan records to provide satisfactory audit trails that allow for the tracing of transactions from initiation to disposition.
- ▶ Consider tracing loan proceeds for a sample of loans including large and unusual credits and ascertain the adequacy of the disbursement controls.
- ▶ Determine if loan terms and other information on new loans is checked for accuracy and verified against loan trial reports.
- ▶ Determine if it requires two employees to effect a status change in a customer account record.
- ▶ Determine if source documents supporting loan modifications are supported by proper authorizations.
- ▶ Determine if supervisory overrides or approvals are required to perform the following functions:
 - Processing payments on loans and leases in the process of foreclosure or other legal action.
 - Waiving late charges or other penalties.
- ▶ Determine if loan officers are prohibited from processing loan payments.
- ▶ Determine if receiving and releasing collateral to borrowers and posting entries in the collateral register are performed by different employees and if appropriate records are maintained.
- ▶ Determine if collateral receipts exist and identify each item retained by the bank.
- ▶ Determine if negotiable collateral is held under dual control.

EXPANDED ANALYSIS

- ▶ Determine if discount, interest, commission, and fee computations are compared or tested to initial records by employees who cannot originate entries.
- ▶ Determine the extent of collateral attachment problems.
- ▶ Determine if the bank is identified as loss payee on collateral insurance coverages.
- ▶ Determine if tickler systems for insurance, taxes, and collateral filings are adequate.
- ▶ Determine if officers and employees are prohibited from holding blank signed notes in anticipation of future borrowings.
- ▶ Determine if paid and renewed notes are canceled and promptly returned to customers.
- ▶ Determine if charged-off notes are adequately segregated and controlled.
- ▶ Determine if loan charge-offs are approved in writing and reported to the board or appropriate committee.
- ▶ Determine if the record of charged-off loans is maintained by a person other than the one who has custody of the notes or receives payment.
 - Determine if the record is reconciled to the actual notes at least annually.
- ▶ Determine if subsidiary payment records and files for serviced loans are adequately segregated and identifiable.
- ▶ Review reciprocal situations where loans to bank insiders are sold to other institutions and loans to insiders of other institutions are purchased.

PORTFOLIO QUALITY

- ▶ Expand loan sampling (including off-balance sheet activities) in order to assess loan quality and gain an understanding of credit deficiencies.
- ▶ Sample consumer loans if significant deficiencies were noted in underwriting or administration.
- ▶ Review participation agreements for terms and conditions.

EXPANDED ANALYSIS

- ▶ Consider if there are any informal repurchase agreements between participants by reviewing participation repurchase history.
- ▶ Determine why loan losses are not recognized in a timely manner. Reasons for not recognizing losses in a timely manner include the following items:
 - Lack of identification.
 - Loss deferral motivated by earnings performance.
 - Loss deferral motivated by poor financial condition.

ALLOWANCE FOR LOAN AND LEASE LOSSES (ALLL)

NOTE: Many of the factors necessary to determine an appropriate level of the ALLL may have already been reviewed within the PORTFOLIO ANALYSIS section. Coordinate procedures with other team members to avoid unnecessary duplication.

- ▶ Determine an appropriate ALLL level.
 - Consider comparing the reported ALLL (after the deduction of all loans, or portions thereof, classified Loss) against the sum of the following amounts: *(Note: Refer to interagency policy statement on the ALLL dated December 21, 1993.)*
 1. 50 percent of the portfolio that is classified Doubtful.
 2. 15 percent of the portfolio that is classified Substandard.
 3. For the portions of the portfolio that have not been adversely classified (including those loans designated Special Mention), estimated credit losses over the upcoming twelve months (based on the institution's average annual rate of net charge-offs experienced over the previous two or three years on similar loans, adjusted for current conditions and trends).
 - Determine if the ALLL is sufficient to cover all of the following risks:
 1. Any losses on loans accorded Loss classifications (in whole or in part) that have not yet been charged off.
 2. Estimated probable losses for all loans accorded Doubtful classifications (without partial Loss classification).
 3. Estimated probable losses for all remaining adversely classified loans (without partial Loss or Doubtful classification).
 4. Other problem loans (either individually or in pools).
 5. Estimated probable losses for the remaining categories of loans in the portfolio.
 6. Supplemental amount for unidentified loan portfolio losses.
 - Consider the bank's loan loss history in aggregate and by loan type.
 1. Calculate the average loan loss history for the past five years using gross loan losses to average total loans. (Data available from latest year-end UBPR).
 2. Evaluate any aberrations in a specific year, and make adjustments needed for current conditions to arrive at a realistic average.
 3. Consider migration analysis.
 - Consider the average reserve coverage of non-performing loans by state, rating, and charter. *(Note: Provided by the Regional Office on a quarterly basis.)*

EXPANDED ANALYSIS

- Consider the historical average of loan loss reserves to nonperforming loans for all banks in the region and nation. (*Note: Refer to the FDIC quarterly Banking Profile. Reserve coverage of nonperforming loans is typically higher for sound loan portfolios than those where problems exist.*)
- Estimate the potential loss exposure in classified and Special Mentioned loans.
- Consider the following factors to determine an appropriate percentage for nonclassified loans: (*Note: If the bank uses a formula approach to determine reserve adequacy, it may be feasible to use the internal formula in arriving at the reserve requirements for nonclassified loans even though the overall system may be considered inadequate.*)
 1. Degree of board or committee involvement, oversight, and control.
 2. Expertise, training, and adequacy of loan staff.
 3. Adequacy of loan policy and adherence to policy requirements.
 4. Effectiveness of collection procedures.
 5. Adequacy of renewal and extension policies.
 6. Adequacy of charge-off policies.
 7. Effectiveness of internal loan review function.
 8. Adequacy of appraisal procedures.
 9. Maintenance and analysis of financial information.
 10. Adequacy of documentation (other than financial information).
 11. Capitalization of interest.
 12. Over reliance on collateral values.
 13. Composition of the loan portfolio. (It may be appropriate to use different percentages for consumer, residential and commercial real estate, and commercial loans.)
 14. Existence of self-dealing and insider transactions.
 15. Level of classified loans and trend over past few examinations.
 16. Level and trend of internally identified loan problems.
 17. Level and trend of overdue and nonaccrual loans.
 18. General economic considerations (local, state, regional, national).
 19. Growth trends.
 20. Entry into new areas of lending.
 21. Extent of out-of-territory lending.
 22. Adequacy of follow-up systems, etc.
 23. Existence of off-balance sheet items (loan commitments, letters of credit).

VIOLATIONS

- ▶ Determine the cause of the violation or contravention to FDIC Statements of Policy and responsible party or parties. Consider the following items.
 - Lack of familiarity with laws, regulations or policy statements.
 - Negligence.
 - Misinterpretation.
 - Willful disregard and noncompliance.

EXPANDED ANALYSIS

- ▶ Discuss violations with management and gain commitments to correct infractions.

Notes:

EXPANDED ANALYSIS DECISION FACTORS

The following questions will help to evaluate the significance and materiality of deficiencies or other specific concerns identified in the Core and Expanded Analyses.

1. Are deficiencies immaterial to the supervision of the lending function?
 - Are deficiencies in loan policies and procedures easily corrected or insignificant?
 - Are exceptions to established lending policies approved by the board or immaterial?
 - Are violations unintentional, technical, and easily corrected?
2. Are deficiencies immaterial to the bank's condition?
 - Do loan concentrations represent minimal overall risk to the institution?
 - Will capital, earnings, and liquidity remain at satisfactory levels despite the volume of adversely classified loans?
 - Will capital and earnings remain satisfactory after the Allowance for Loan and Lease Losses is funded to an adequate level?

REPORT OF EXAMINATION PRESENTATION:

NOTE: Only prepare supplemental pages that support examination comments and conclusions.

- ▶ Discuss analysis, conclusions, and recommendations with the EIC and management prior to completing the following pages as needed:
 - Those pages listed in the Core Analysis Decision Factors section.
 - Loans and Lease Financing Receivables.
 - Items Subject to Adverse Classification.
 - Items Listed for Special Mention.
 - Assets with Credit Data or Collateral Documentation Exceptions.
 - Analysis of Loans Subject to Adverse Classification.
 - Concentrations.
 - Extensions of Credit to Directors, Officers, Principal Shareholders, and Their Related Interests.
 - Internal Routine and Controls.
 - Violations of Laws and Regulations.
 - Examination Conclusions and Comments.
 - Matters Requiring Board Attention.

EXPANDED ANALYSIS DECISION FACTORS

Notes:

IMPACT ANALYSIS

This section helps to evaluate the impact of deficiencies identified in the Core and Expanded Analyses and Decision Factors on the bank's overall condition. This section also directs the examiner to consider possible supervisory actions.

- ▶ Determine the impact of lending deficiencies on the institution's capital, earnings, and liquidity, and assess the future impact on the institution if these deficiencies continue.
- ▶ Determine the impact of an under-funded ALLL on the bank's capital accounts.
- ▶ Determine the need for direct confirmation of loan accounts. As needed, consult with the Field Office Supervisor and Regional Office.
- ▶ Determine the need for administrative and enforcement actions, formulate specific recommendations, and advise the Field Office Supervisor and the Regional Office on the nature of the supervisory concerns.
- ▶ Discuss the possibility of administrative and enforcement actions with executive management and the board of directors.
- ▶ Investigate the circumstances and facts surrounding apparent violations, prepare recommendations for Civil Monetary Penalties, Reports of Apparent Crime, and removal action under Section 8 when necessary.

REPORT OF EXAMINATION PRESENTATION:

- ▶ Discuss analysis, conclusions, and recommendations with the EIC and management prior to completing the following pages as needed:
 - Those pages listed in the Expanded Analysis Decision Factors section.

Notes: