

# RESCINDED

## Regulatory Bulletin RB 37-68

Handbook: **Examination**  
Subject: **Administration**

This rescission does not change the applicability of the conveyed document. To determine the applicability of the conveyed document, refer to the original issuer of the document.



Sections: **060, 070**

### **Examination Scheduling, Scoping, and Management Ratings: Developing, Assigning, and Presenting**

**Summary:** This Regulatory Bulletin transmits revised Examination Handbook Sections 060, Examination Scheduling, Scoping, and Management, and 070, Ratings: Developing, Assigning, and Presenting. These revised Handbook sections also incorporate applicable information currently in Section 040. We delete Section 040 from the Examination Handbook with the issuance of this bulletin. We also rescind RB 37-32 dated February 27, 2009; RB 37-14 dated March 13, 2006; and RB 37-4 dated November 30, 2004 with the issuance of this bulletin.

*For Further Information Contact:* Your Office of Thrift Supervision (OTS) Regional Office or the Examination Programs Division of the OTS, Washington, DC. You may access this bulletin at our web site: <http://www.ots.treas.gov>.

*Regulatory Bulletin 37-68*

#### **SUMMARY OF CHANGES**

OTS is issuing revised Examination Handbook Sections 060, Examination Scheduling, Scoping, and Management, and 070, Ratings: Developing, Assigning, and Presenting. Change bars in the margins of the Handbook sections indicate revisions. Both sections include new language to emphasize that examiners should not disclose proposed examination ratings during the exit meeting. We also added a new procedure to the examination programs that requires review of the Matters Requiring Board Attention and Corrective Actions from the three or four previous reports of examination. In addition, we summarize the other substantive changes below:

#### **060 Examination Scheduling, Scoping, and Management**

- Added a discussion to re-emphasize the importance of an on-site examination at the principal locations of higher risk lines of business of an association.
- Added Matters Requiring Board Attention and corrective actions for previous three or four examinations to the list of items to review offsite.
- Revised Appendices A, B, and C; and added new Appendix D – Exception Sheet.

## Regulatory Bulletin 37-68

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### 070 Ratings: Developing, Assigning, and Presenting

- Included discussion of trust comments and ratings, when applicable.
- Revised the guidance for the compliance comment and the Earnings comment.
- Revised discussion to highlight the importance of communicating with all savings association boards following a comprehensive examination, regardless of composite rating.
- Changed requirement to disclose ratings at exit conferences.

*Thomas A. Barnes*

—Thomas A. Barnes  
**Deputy Director**  
**Examinations, Supervision, and Consumer Protection**

## Examination Scheduling, Scoping, and Management

The Office of Thrift Supervision (OTS) conducts comprehensive examinations to thoroughly assess each saving association's risk profile and produces one report of examination (ROE) addressing safety and soundness (S&S), compliance and, when applicable, trust department operations. (See the Trust and Asset Management Handbook for guidance.) OTS also recently enhanced the comprehensive ROE to include a risk assessment summary matrix to document the quantity of risk, quality of risk management, aggregate risk, and direction of risk. (See [CEO Memo 369](#), dated October 8, 2010.)

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### LINKS

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

Key considerations in a comprehensive examination:

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

The comprehensive examination process includes the PERK PAC, which makes available S&S and Compliance information schedules in addition to schedules and questionnaires for specialty areas.

This Handbook Section addresses examination strategy and objectives, examination scheduling on 12- and 18-month cycles, scoping and planning, and examination management. This section also provides guidance for intervening state, Limited, Eligibility, and Joint OTS/FDIC examinations.

## EXAMINATION STRATEGY AND OBJECTIVES

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

*Timely* examinations ensure that the agency stays abreast of changes in the condition or management of an association. OTS must schedule a full scope, on-site examination of each insured depository institution within the appropriate timeframe for that institution. An efficient examination eliminates multiple reviews of the same area for different purposes by combining safety and soundness and compliance reviews of the same areas such as lending or deposits.

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

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

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

The goal of the comprehensive examination process is to conduct an examination that reviews the compliance and the CAMELS component areas. Based upon the findings in each of these areas, the examination team should be able to make an overall assessment of the association in terms of the risk management and compliance management functions, as well as the adequacy of management and staff.

## SCHEDULING EXAMINATIONS

OTS must conduct a full-scope, on-site examination of every savings association once during each 12-month period. OTS may conduct a full-scope, on-site examination of a savings association once during each 18-month period if the association meets the conditions below. You may conduct a limited examination under certain conditions. (See the discussion of Comprehensive Limited Examinations at the end of this Handbook Section.)

A full-scope examination, according to the statute, means that you conduct an on-site examination and rate all CAMELS components. You may conduct certain examination procedures offsite. (See the

discussion of Off-Site Examination Procedures later in this section.) For comprehensive examination purposes, OTS conducts the Compliance review as part of a full-scope examination except as noted below under Intervening State Examinations.

OTS measures the 12-month and 18-month cycles from the “close date” of the last examination to the “start date” of the next examination. The “close date” is the date OTS transmits the Report of Examination (ROE) to the association.

## **12-month Cycle**

By conducting examinations annually, you increase the chances of discovering problems and resolving them early. Regional offices may conduct full-scope, on-site examinations more often than prescribed by statute.

All de novo savings associations are subject to the 12-month examination cycle. The 12-month examination cycle should continue until management demonstrates its ability to operate an association in a safe and sound manner and satisfies all conditions imposed at the time of approval.

## **18-month Cycle**

An 18-month examination cycle applies to insured savings associations with total assets of less than \$500 million that meet the following criteria in 12 CFR § 563.171:

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

Revert to the 12-month examination cycle if any of the following triggering events occur:

- An enforcement action.
- An acquisition or change in control.
- A change in asset size to \$500 million or more.

- A downgrade in PCA rating.
- A downgrade to a 3 or worse in the CAMELS composite rating, the Compliance rating, or Management component rating.

If a triggering event occurs in any of the following time frames at an association that otherwise meets all of the criteria for an 18-month examination interval, you must conduct a full-scope examination within the appropriate interval:

<b>If the triggering event occurs....</b>	<b>Then start the next exam...</b>
Within 9 months of the “close” date of the prior full-scope exam	No later than 12 months from the close of the last full-scope exam.
Between 9 and 12 months since the close of the last full-scope exam	Within 90 days.
Twelve or more months since the close of the last full-scope exam	Within 90 days, but no later than 18 months from the close of the last full-scope exam.

Conversely, if an association under a 12-month examination interval becomes eligible for an expanded interval, the regional office may immediately expand the interval to 18 months.

## Intervening State Examinations

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

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

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

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

- The previous Compliance rating was 1 or 2.

- Off-site monitoring shows no material change in the association's risk profile.
- The association corrected any previous compliance deficiencies.

## EXAMINATION SCOPING AND PLANNING

### Scoping an Examination

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

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

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

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

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

Scoping consists of three stages:

- Reviewing pre-examination information.
- Conducting management interviews.
- Developing a preliminary risk assessment.

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

## ***Review Pre-examination Information***

Generally, the EIC begins the scoping process offsite, before the start of the examination, leveraging off work performed by regional staff responsible for monitoring and updating the Electronic Continuing Examination Folder (ECEEF) and Regulatory Profiles, prior exams and work papers, and relevant Preliminary Examination Response Kit (PERK) materials.

A sample of items to review offsite include the following:

### **Agency Information**

- The ECEF, (including Quarterly Monitoring Reports (QMRs)), and, if applicable, the Regulatory Profile for the association.
- Results of regional off-site monitoring.
- OTS financial reports including the Thrift Financial Report (TFR) and the Uniform Thrift Performance Report (UTPR).
- Prior savings association, compliance, and holding company work papers and recommendations.
- The Matters Requiring Board Attention and corrective actions from the previous three or four ROEs.
- Correspondence covering significant matters involving the association that transpired between exams.
- Other correspondence and internal memoranda involving the association.
- Application information – conditions of approval and major applications filed.
- Documentation on supervisory and enforcement actions.
- Consumer complaints filed with OTS since the last examination.
- Suspicious Activity Reports and Currency Transaction Reports.
- CRA Wiz/ HMDA data.

### **PERK Information**

- PERK documents completed by association management before the start of the examination for information related to the following:



- Changes in operations.
- Changes in technology risk, systems and controls.
- Board meetings.
- Internal and external audits.
- Compliance self-assessments.
- Responses and corrective actions to exams and audits.
- Significant changes in outsourcing or vendor relationships.

## **General Data**

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

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

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

## ***Conduct Management Interviews***

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

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

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

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

## ***Risk Assessment***

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

Using pre-examination information and management interviews allows the EIC to formulate an initial assessment of:

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

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

## **Selecting Examination Programs and Procedures**

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

You may expand the depth of review of any given area as additional facts surface that necessitate a more comprehensive review.

Use programs and questionnaires as appropriate, but only to the extent necessary to address the scope and support the examination conclusions. Programs provide guidance necessary to support examination findings and ROE comments.

The EIC should use the Examination Scope Worksheet in [Appendix B](#) to indicate the examination programs to complete on an examination. In many circumstances, you will not need all or even a majority of the programs. Discuss the scope of the examination with the Field Manager (FM) or Assistant Regional Director (ARD) and document their concurrence on the worksheet. Before the start of the examination, the EIC will prepare a scoping memorandum, signed by the FM or ARD, that sets forth the initial risk assessment and exam programs. Retain a copy for the work papers.

For example, if your review of the policies, structure, administration, and results of the association's internal asset review program reveals that the program is sufficient and the results are accurate, you may place a greater reliance on the association's internal review. The risk that the association is not adequately reviewing and classifying its assets would be low, so more detailed examination procedures would generally not be necessary.

When using this risk-focused examination approach, use sound professional judgment to ensure that the depth of review is sufficient to accurately assess the association's condition, but is not excessive. For further information regarding the examination program and the three levels of review, refer to [Examination Handbook Section 010](#), Handbook and Program Use.

## EXAMINATION MANAGEMENT

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

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

### EIC Responsibilities

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

- **Examination planning, organization, and implementation:** The EIC is responsible for scoping the examination, setting the examination objectives, communicating the examination

objectives to the examination team, and ensuring that the exam team meets the examination objectives.

- **Assignments and job monitoring:** The EIC must determine the expertise necessary to perform certain aspects of the examination and make assignments accordingly. The EIC is responsible for realizing the maximum efficiency from conducting coordinated safety and soundness and compliance reviews consistent with the examination's scope. Depending on the size of the job, the EIC may delegate certain management responsibilities to assistants for efficiency and to improve upon administrative and management skills of assistants.
  - Assign priorities to examination tasks and determine optimal use of comprehensive reviews across exam programs. Maximize efficiency by assigning one assistant to conduct or coordinate interrelated S&S and compliance programs to avoid duplication of effort whenever feasible.
  - Brief the examination team members on their respective assignments, including their participation in examination segments that will involve comprehensive reviews across exam programs. Provide them with the necessary information and resources to conduct their assignments efficiently.
  - Explain the preliminary risk assessment and scoping relevant to each assistant's assignment. Discuss the effect of information developed during the exam on the association risk profile, possible changes to the scope, opportunities for conducting comprehensive reviews across exam programs, and the ability to meet assignment deadlines throughout the examination. Adjust assignments as warranted by these considerations.
  - Consider completing the Examination Scope Worksheet in [Appendix B](#) when assigning tasks and budgeting examination hours. The EIC specifies the areas to review on the examination considering the scope. As needed, you may add any activities not included on the worksheet.
  - Monitor the progress of the examination to achieve examination objectives in a timely manner and to identify early adjustments to the scope, staffing, and completion date. The EIC should notify a supervisor as soon as adjustments to scope or other events may affect scheduling or the completion date. The supervisor might consider staff reassignment from other jobs, if necessary.
- **Prepare Report of Examination:** Incorporate program findings and conclusions, edit comments and finalize the ROE. Compile, index and file work papers. Properly record necessary exam data and regulatory violations in agency systems.
- **Serve as the primary communications link:** The EIC is the focal point for communications on significant matters. Assistants, association personnel, and regional office staff must all know how to communicate information and when to share information. During

the examination, it is important that only one responsible individual provide answers to significant items. The EIC should coordinate this in case questions arise.

- Examiners should communicate any significant changes to the scope and the reasons for them with examiners involved in the different examination areas. Share significant findings and conclusions to avoid duplicating efforts.
- When the FDIC or a state banking department participates in an examination, maintain close communication with FDIC regulatory authorities and appropriate state regulatory authorities. See the discussion of OTS/FDIC Joint Examinations Process later in this Handbook Section.
- Early in the examination, the EIC should discuss with the President/CEO, or with a designated association representative, some of the administrative aspects of the examination, including:
  - ✓ Time frames for receiving requested information.
  - ✓ The availability of the examiners to answer questions from the staff preparing requested information.
  - ✓ Names of key contact people.
  - ✓ Facilities and parking availability.
  - ✓ Hours for work.
  - ✓ Use of equipment.
  - ✓ The expected duration of the examination.
  - ✓ Any planned interruptions (these should be kept to a minimum).
  - ✓ Names of assisting examiners.
- The EIC should schedule regular meetings with the CEO to discuss the progress of the examination and to address any issues of concern. Conduct the examination efficiently to minimize undue disruption for the association. Convey any unresolved concerns management expresses about exam progress to a supervisor.
- The EIC should schedule an examination exit meeting with the association's senior management to discuss examination findings, the examiner's overall conclusions, and recommendations. Do not disclose proposed ratings during examination exit meetings. This is particularly important for examination reports that require review by the large bank unit. For all other cases, it is preferable to use the rating definition terminology in describing the

examination results, but not the actual ratings. See [Handbook Section 070](#), Ratings: Developing, Assigning, and Presenting.

- **Manage staff development and evaluation of assistants:** Assistants may need guidance, depending on their experience and ability. The EIC should encourage questions and ensure that someone is available to provide guidance. Depending on the size of the job, the EIC should be familiar with the work performed by the assistant(s) so that they can make fair and constructive evaluations of their work.
  - Whenever possible, assign assistants to program areas that they can complete, including report pages and comments, before leaving the assignment. This allows for efficiency and accountability and provides necessary on-the-job training.
  - Monitor assistants' performance throughout the examination to ensure that they are meeting objectives according to schedule and consistent with agency standards for quality work product. Early identification of work-related problems also allows the assistants the opportunity to correct mistakes and to immediately improve upon skills.
- **Ensure a cooperative and positive working environment:** Conduct examinations with as little disruption, conflict, and confusion as possible. A positive work environment fosters the productivity of the team members. Disagreements will occur at times, but avoid an antagonistic role. Allow for regular meetings with management to discuss findings and questions, and avoid monopolizing the time of the staff as much as possible. A professional and considerate approach usually results in cooperation from the association staff.

## **Off-Site Examination Procedures**

OTS may conduct certain examination procedures offsite as proficiently as they conduct them onsite. The completion of off-site examination work complements the OTS strategy that seeks to maximize the efficient and effective use of agency resources. At the same time, it should minimize the burden on both the thrift industry and the examination staff. Some of the advantages of performing procedures offsite may include reduction in travel expenses and minimal disruption to thrift operations.

Regional directors or their designee should develop appropriate policies and procedures for performing examination procedures offsite. Examiner discretion and the ability to exercise judgment will remain a critical aspect of the process whereby the risks identified within each examination assignment will drive the level of off-site work that the examination team can effectively perform.

## ***Savings Association Selection Criteria***

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

- The association's CAMELS and Compliance ratings.

- Prior history.
- Complexity of operations.
- Reliability of data.
- Capabilities of examination staff assigned.

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

Open lines of communication with association personnel are essential at all examinations, but you may have to take extra steps to keep those lines open during off-site portions of the examination. Advise association management of the start and completion of off-site work.

### ***On-Site Presence***

You should periodically perform on-site examinations at the principal locations of the higher risk lines of business operated by a savings association. These lines of business may be in any kind of entity including operating subsidiaries, loan production offices, service corporations, etc.

An on-site presence allows you to:

- Directly observe and inspect the place of business, processes and procedures, original documents and records, and behavior of personnel.
- Conduct inquiries and interviews of staff members and management directly responsible for the information provided.

An on-site presence allows you to observe how the entity operates, the business culture, and the competence and adequacy of personnel.

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

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

### **Continuing Examination and General Administrative Documents**

Retention of the following documents preserves examination continuity and reduces excessive requests for information during examinations.



## ***Continuing Examination Documents***

Retain the following documents with the electronic work papers:

- Copy of Charter and Bylaws
- Copy of Conditions for Insurance (in force)
- Summary of Leases
- Proxy Statement, if applicable
- Schedule of Branch Offices and LPOs

File in ECEF:

- Enforcement Documents
- Recent Correspondence
- News articles

Retain the following documents with the electronic PERK files:

- Management and Director Committees and Members (PERK01)
- Organizational Chart (PERK01)
- Officer Resumes (PERK01)
- Directors' and Officers' Home Addresses (PERK03)
- Holding Company/Affiliates Corporate Structure (PERK21)
- Internal Audit Program (PERK01)
- Stockholders' Schedule (PERK08)
- Approved Appraisers and Qualifications (PERK01)
- Copies of new or significant Policies

## General Administrative Documents

File examination-related administrative information in the Administration folder of the electronic work papers. This might include any of the following items:

- Examination Scope Worksheet ([Appendix B](#)).
- Examination Management Checklist ([Appendix C](#)).
- Examination Scheduling, Scoping, and Management Program.
- Pre-Assignment Analysis.
- Exception Sheets ([Appendix D](#)).
- Ratings: Developing, Assigning, and Presenting Program.

You should use exception sheets to record all specific regulatory and policy violations that you do not specifically discuss in the ROE. Either the managing officer or the appropriate department head must provide a disposition for each problem noted and initial the exception sheet. Provide a copy of all exception sheets to the managing officer.

## Examination Conclusion

The EIC is responsible for reviewing and compiling the examination findings, identifying matters that require Board attention or savings association action, and ensuring the Examination Conclusions and Comments page presents a concise and balanced portrayal of an association's condition and future prospects. The ratings should reflect the overall examination findings and conclusions.

Responsible OTS regional staff should update the ECEF and, if applicable, create or update the Regulatory Profile. In addition, regional staff should:

- Enter matters requiring board attention and corrective actions in the Follow-Up tab of the EDS/ROE System.
- Ensure that the association takes timely and appropriate corrective action for any problems found during the examination.
- Closely monitor (during and outside of the examination process) compliance with matters requiring board attention and other required corrective actions.
- Promptly identify and address any significant noncompliance or recurrence of identified problems.

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

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

## **OTS/FDIC JOINT EXAMINATION PROCESS**

Pursuant to the Information Sharing and Special Examination Agreement with the FDIC, OTS and FDIC regional staffs will meet regularly to review the examination schedule. The FDIC should indicate those examinations in which they desire joint participation. FDIC will perform all savings association examination activities on a joint basis unless compelling reasons dictate otherwise.

For joint examinations, the FDIC and OTS will jointly scope the examination at the EIC level or at the respective regional office level. Disagreements over scope should default to the broader alternative. When examinations of savings association affiliates are necessary, the EIC should decide how to conduct the examinations.

OTS will provide the FDIC with a copy of the ROE through an automated process when transmitting the ROE to the association.

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

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

## **Report of Examination**

Joint examinations represent a division of responsibilities among the joint staff; the OTS and FDIC each provide an EIC, who share responsibility for managing the examination and are responsible for resolving interagency differences during the examination process. EICs of both agencies will coordinate and communicate during the examination to ensure that they achieve examination objectives with a minimum of redundancy.

The FDIC's ROE will be for internal purposes only, although they provide a copy to the OTS regional office. If the FDIC Board authorizes an enforcement action, however, the FDIC would then transmit its examination report to the institution. As the OTS and FDIC regional staffs prepare the concurrent reports, they should attempt to resolve all significant differences of opinion concerning the thrift's overall condition and the enforcement or corrective action needed.

## **COMPREHENSIVE LIMITED EXAMINATIONS**

You may conduct a comprehensive limited examination for the following associations:

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

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

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

- Changes in business activity and strategy, such as a change in loan product lines, the investment portfolio, or the deposit structure.
- Action taken by management to correct items of concern noted at the most recent examination.
- Deterioration in asset quality indicators such as nonperforming assets.
- Circumstances indicating a deteriorating and deficient Compliance management program.
- Complex trust department operations or trust departments that have significant trust assets.
- Noncompliance with prior enforcement actions.
- Negative earnings, unfavorable earnings trends, or dependence on nonoperating income.
- The levels and composition of capital, as well as trends in capital formation and accumulation.
- An excessive rate of growth or a level of growth that exceeds capital levels or regulatory or supervisory directives.
- Changes in other key financial ratios and indicators.
- Other information such as the external audit report, news articles, supervisory correspondence, consumer complaints alleging discrimination, and information obtained from examinations of other savings associations.

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

## **ELIGIBILITY EXAMINATIONS**

An eligibility examination is the collection and analysis of critical information in conjunction with an application for a new thrift charter, charter conversion, or change of control. The examination supplements the customary review and analysis of the application and provides additional information for OTS decision-makers. Therefore, the examination scope should focus on novel or significant issues or risks that have a material impact on the success of the proposed activity or strategy. Examination procedures may include on- or off-site activities. Examiners will document results in a memorandum-style ROE.

OTS will perform an eligibility examination in cases where the application involves an existing company or line of business that is to be converted to, to be combined with, or will otherwise materially alter or affect the operations of a savings association. Converting entities that have been recently examined by a federal or state banking or trust regulator, and received satisfactory ratings (CAMELS 1 or 2, Trust 1 or 2, Compliance 1 or 2, and CRA Satisfactory or Outstanding) may not require an eligibility examination, unless the application raises a material issue not addressed by the existing ROE. These are the typical circumstances that warrant an eligibility exam, but the Regional office may identify other occasions that necessitate an eligibility exam.

The Regional office should determine the need for an eligibility examination as early in the application process as possible and promptly inform the applicant if it will be conducting an examination. Typically, the Regional office will make the determination and notify the applicant in the pre-filing meeting. The Regional office must schedule and perform the examination promptly and prior to an application being deemed complete so that the examination does not delay the application review process.

## **Planning and Scoping an Eligibility Examination**

Planning and scoping eligibility examinations entails:

- Determining the work to perform.
- Arranging for qualified examiner resources.
- Coordinating with other applicable agencies.

When the Regional office establishes an exam date, promptly inform the applicant of the timing and objectives of the exam. When applicable, the OTS may conduct an eligibility examination jointly with an insurance-of-accounts examination performed by the FDIC, pursuant to a joint OTS/FDIC Examination Agreement.

The Regional office's scope-setting process must incorporate input from Regional applications staff, in addition to supervisory and examination staff. The applications staff should coordinate with other parties involved in the applications review process, including DC supervisory and legal staff, to ensure that supervision and examiners are aware of all pertinent issues and information needs. Generally, the applications staff input should be in the form of a brief, written summary of issues. As part of the scoping process, the EIC should also obtain and review, as applicable:

- The application itself, including the applicant's current business plan.
- Subsequent responses by the applicant to requests for additional information or any subsequent related filings (along with the related requests).
- Any information or comments provided by application processing staff.
- The applicant's two most recent examination reports (and work papers, if necessary) from other regulatory agencies (i.e., OCC, FDIC, FRB, NCUA, NASD, or state).

During the examination, supervision and examiners must communicate with regional applications staff to ensure that the exam scope addresses all material issues as they evolve.

## **Examination Procedures**

You should tailor each eligibility examination to the particular risks posed by the applicant's business plan. The examination scope should dictate the examination procedures, that is, perform procedures necessary to assess significant or novel issues that are relevant to the application decision. When appropriate, you may reduce or modify procedures based upon the findings and conclusions of prior regulatory examination reports. An eligibility examination should address the following general disciplines, as applicable.

### ***Safety and Soundness***

You should generally select appropriate Level I examination procedures from the Examination Handbook to address the risks posed by the applicant and the circumstances. You should use judgment in reviewing specific risks unique to specialty businesses such as credit card operations or insurance companies.

### ***Compliance/CRA***

The Regional office should consider a compliance component in the eligibility examination, performed by a qualified compliance examiner. As with safety and soundness, limit compliance review procedures to the minimum necessary to identify critical compliance management risks. You may also review CRA performance as necessary to gather information to supplement CRA plans and representations provided in the application.

## ***Information Technology***

Depending on the applicant's size and complexity, the Regional office may determine that a review of the applicant's information technology (IT) is necessary. Specific issues that may require review include the following:

- Transactional web site processing and electronic banking.
- Complex local and wide area networks.
- Use of emerging or untested technology.
- Systems conversions or other major upcoming systems projects.
- Poor past performance in IT areas.

An experienced IT examiner should perform the review of this area.

## ***Trust Operations***

When the applicant proposes significant trust activities, a qualified trust examiner should participate in the eligibility examination to assess critical trust management and control functions. The trust examiner should generally perform selected Level I examination procedures from the Trust and Asset Management Handbook as appropriate to address the risks posed by the applicant and the circumstances. Generally, trust will only require review when trust operations are expected to form a substantial portion of the applicant's business. When trust operations are the only substantial activity of the applicant, it may not be necessary to include other examination segments.

## **ROE**

Prepare a memorandum style ROE summarizing the examination scope and procedures, any novel or critical issues, management's response, and the significant findings for each area reviewed including CAMELS, compliance, CRA, IT, and trust, as applicable. The memorandum should clearly state the overall conclusions of the examination and issues that application processing staff and other OTS decision-makers should consider in their evaluation of the application.

## REFERENCES

### Code of Federal Regulations (12 CFR)

§ 563.171                      Frequency of Examinations

### Office of Thrift Supervision CEO Memos and Bulletins

CEO Memo 369                Risk Assessment Summary in the Thrift Report of Examination

TB 68b                         Appeals and Ombudsman Matters

### Closely Related Handbook Sections

[Section 010](#)                 Handbook and Program Use

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

[Section 080](#)                 Enforcement Actions

### Interagency Agreements

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

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



# Examination Scheduling, Scoping, and Management Program

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## EXAMINATION OBJECTIVES

To ensure that OTS conducts a full-scope, on-site examination according to scheduling requirements:

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

To ensure that the examination makes efficient use of resources:

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

To ensure that the examination is well-managed:

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

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

# Examination Scheduling, Scoping, and Management Program

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- Appropriate documentation of work.
- To provide useful information for future planning, scoping, monitoring, and management.

## SCHEDULING

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

## SCOPING PROCEDURES

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

1. Prior to the examination, review the Electronic Continuing Examination Folder (ECEP) and, if applicable, the Regulatory Profile for the savings association.  

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2. Ensure the PERK is tailored to the savings association and type of examination. Send the PERK to the association at least four weeks prior to the examination start date.  

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

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

# Examination Scheduling, Scoping, and Management Program

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

- 
5. Review the Matters Requiring Board Attention and Corrective Actions from the previous three or four ROEs to ensure that the board and management have taken appropriate corrective action where necessary and persistent problems have not recurred.

- 
6. Conduct management and compliance interviews. See this Handbook Section for interview discussion topics. Conduct interviews with management by phone, if possible.

- 
7. Formulate an initial risk assessment based on the following:
- The association's current financial condition.
  - Management and the BOD's prior track record in managing risk and taking corrective action.
  - Material changes in risk profile or operating strategy and management's response to those changes.
  - Quality of internal controls, technology controls, risk management, and compliance management systems.
  - Responsiveness of management and the board in implementing corrective action to risk management and compliance management deficiencies since the previous examination, audits or reviews.
  - Association's efforts to stay abreast of and train the board, management, and staff on safety and soundness and regulatory compliance developments.
- 

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

# Examination Scheduling, Scoping, and Management Program

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

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

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

- 
10. Prepare assignments for assistants (before commencing the examination, if possible) based on the scope and areas of expertise. Assign examiners S&S and consumer compliance review in areas where there is overlap, such as lending and deposit areas. You should prepare an Examination Scope Worksheet (see [Appendix B](#)) and budget exam hours accordingly.

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

- Review the association's current Thrift Financial Reports (TFR) and Management Information Systems (MIS) reports and determine if there have been significant changes in the level of capital, lending or investment activity, earnings, or nonperforming assets.
- Review the minutes of the board of directors' meetings. Focus attention on significant changes in the association's business activities (lending, investment, joint ventures, etc.). Assess the level of oversight performed by the directorate.

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

# Examination Scheduling, Scoping, and Management Program

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- Discuss with management any changes in key management, the directorate, or business activities that have occurred since the preceding examination. Also inquire as to any proposed changes or pending litigation that may affect earnings and capital.
- Determine through a review of correspondence, discussions with management, and other appropriate verification methods, if management corrected any problems related to the following areas:
  - Prior examination report comments and supervisory letters.
  - External auditor's exceptions.
  - Internal auditor's exceptions.
  - Any enforcement actions and directives.
- Determine if there are written policies governing key areas such as lending and investments. Evaluate the adequacy of new or revised written policies, procedures, and strategic plans. These guidelines should adequately address safety and soundness (including internal controls), profitability, and compliance with laws and regulations.

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

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

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## EXAMINATION MANAGEMENT PROCEDURES

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

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

# Examination Scheduling, Scoping, and Management Program

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

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

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

---

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

---

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

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19. Throughout the examination:

- Review on a regular basis the workflow, findings, and actual versus budgeted time.
- Take appropriate steps to include on-the-job training. Consider your assistants' task records, if applicable.

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

# Examination Scheduling, Scoping, and Management Program

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WKP. REF.

- Discuss all items of concern with the assistants to ensure that the OTS presents accurate information at the closing conference with the CEO.
  - Keep the supervisor and the CEO abreast of any developing significant issues.
  - Ensure that your assistants are preparing examination work in accordance with policies, including: work papers, interim reports, exception sheets, draft comments, report pages, time sheets, and administrative reports. Refer to [Examination Handbook Section 070](#), Ratings: Developing, Assigning, and Presenting, for a discussion of report content.
- 

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

---

21. Ensure that the examination meets the Examination Objectives of this Handbook Section.

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## EXAMINATION CLOSING PROCEDURES

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

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

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

# Examination Scheduling, Scoping, and Management Program

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24. Make appropriate entries into the EDS/ROE system. You should verify all totals in the examination report and other reports. Refer to Examination [Handbook Section 070](#), Ratings: Developing, Assigning, and Presenting; and the ROE Instructions.

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25. Ensure the completion and upload of the General Administrative documents to the Administration folder of the electronic work papers.

---

26. The EIC should conduct a final review of the work paper content and conclusions before finalization of the conclusions and comments.

---

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

---

28. Initiate the PERK PAC for the next examination. Summarize any other information useful to the planning, scoping, and control of future examination activities and include the information in ECEF. Compare actual and budgeted exam hours.

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29. If applicable, create or update the Regulatory Profile with any significant data obtained from the examination. In large bank cases, update the supervisory plan.

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



# Examination Scheduling, Scoping, and Management Program

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30. Transmit the completed report and return any hard copy documents and files to the regional office in accordance with established procedures. Finalize electronic work papers.
- 

## EXAMINER'S SUMMARY, RECOMMENDATIONS, AND COMMENTS

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

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# Appendix A: Examination Scheduling, Scoping, and Management

## Section 060

### BASIC SCOPING MATRIX

Institution: Docket: Field Manager: EIC:	Product Lines										
	Savings Accounts	Transaction Accounts	Mortgage Loans (Including Construction)	Consumer Non-Mortgage Loans	Commercial Non-Mortgage Loans	Finance Leasing	Monetary Instrument Sales	Payment Systems Risk	Insurance Sales	Securities Sales	Branch Security & Notices
<b>Compliance Areas</b>											
Equal Credit Opportunity – EH 1205			X	X	X	X					X
Fair Housing – EH 1210			X								X
Home Mortgage Disclosure – EH 1215			X								X
Fair Credit Reporting – EH 1300	X	X	X	X	X				X		
Truth-in-Lending – EH 1305			X	X							
OTS Mortgage Regulations – EH 1315			X								
Real Estate Settlement Procedures – EH 1320			X								
Homeowners Protection – EH 1323			X								
Consumer Leasing – EH 1325						X					
Electronic Fund Transfer – EH 1330	X	X						X			
Expedited Funds Availability – EH 1335		X									X
Check 21 – EH 1336		X									
Flood – EH 1340			X								
Right to Financial Privacy – EH 1345	X	X	X	X	X	X	X	X	X	X	X
Fair Debt Collection – EH 1350			X	X							
Unfair or Deceptive Acts – FTC EH 1354	X	X	X	X	X				X		
Unfair or Deceptive Acts – Credit Practices Rule – EH 1355			X								
Military Service Member Protections – EH 1356	X	X		X							
Servicemembers Civil Relief Act – EH 1357		X	X	X							
Homeownership Counseling – EH 1360			X								
Truth-in-Savings – EH 1365	X	X									
Electronic Banking – EH 1370	X	X	X	X	X	X	X	X	X	X	
Privacy of Consumer Financial Information – EH 1375	X	X	X	X	X		X	X			
Insurance Consumer Protection – EH 1380				X	X	X			X		
Bank Secrecy Act and OFAC– FFIEC BSA/AML	X	X	X	X	X		X	X	X	X	
Bank Protection Act – EH 1405											X
Interest on Deposits – EH 1420	X	X									
Advertising – EH 1425	X	X	X	X	X		X	X	X	X	X

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# Appendix B: Examination Scheduling, Scoping, and Management

## Section 060

### EXAMINATION SCOPE WORKSHEET

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

Scope Summary and areas of risk:

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Examination Priorities:

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

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

#### Administration

Exam Scheduling, Scoping, Management (060)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Enforcement Actions (080)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

#### Capital

Risk-Focused Procedures (100RP)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (100TP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Capital Stock and Ownership (110)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Capital Adequacy (120)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
TARP CPP (049)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

#### Asset Quality

Risk-Focused Procedures (200RP)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (200TP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Overview: Lending Ops/Portfolio Risk (201)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Appraisal (208)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

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

**SECTION 060**

Examination Procedures (*Required)	Incl. in scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Sampling (209)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Income Property Lending (210)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Loans to One Borrower (211)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
One- to Four-Family RE Lending (212)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Construction Lending (213)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Other Commercial Lending (214)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Letters of Credit (215)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Floor Plan and Indirect Lending (216)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Consumer Lending (217)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Credit Card Lending (218)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Leasing Activities (219)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Asset-Backed Securitizations (221)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Equity Investments (230)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Troubled Debt Restructurings (240)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Other Assets/Liabilities (250)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Owned and Other Repossessed Assets (251)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fixed Assets (252)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Classification of Assets (260)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Adequacy of Valuation Allowances (261)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Qualified Thrift Lender Test (270)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Margin Securities Regulation U (280)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Management**

Risk-Focused Procedures (300RP)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (300TP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Oversight by the Board of Directors (310)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Management Assessment (330)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Internal Control (340)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
IT Risks and Controls (341)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
External Audit (350)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Internal Audit (355)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fraud/Insider Abuse (360)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Transactions with Affiliates (380)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Earnings**

Risk-Focused Procedures (400RP)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (400TP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Financial Records and Reports (410)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

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

**SECTION 060**

Examination Procedures (*Required)	Incl. In scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Operations Analysis (430)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Liquidity**

Risk-Focused Procedures (500RP)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (500TP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Funds Management (510)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Cash Flow and Liquidity Management (530)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Investment Securities (540)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Deposits/Borrowed Funds (560)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Reserve Requirements Reg D (561)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Government Securities Act (563)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Payment Systems Risk (580)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Sensitivity to Market Risk**

Risk-Focused Procedures (600RP)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Tailored Procedures (600TP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Interest Rate Risk Management (650)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Derivative Instruments and Hedging (660)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Other Activities**

Networking Arrangements (710)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Insurance (720)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Subordinate Organizations (730)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Development (740)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Mortgage Banking (750)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
New Activities and Services (760)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Unlawful Internet Gambling (770)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Compliance Management**

Tailored Procedures (1000TP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Compliance Oversight Examination Program (1100)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Fair Lending/Nondiscrimination<sup>1</sup>**

Fair Lending – Potential for Discriminatory Conduct (1201)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
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**APPENDIX B: EXAMINATION SCHEDULING, SCOPING,  
AND MANAGEMENT**

**SECTION 060**

Examination Procedures (*Required)	Incl. in scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Nondiscrimination (1200)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fair Lending – other (1201)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Equal Credit Opportunity Act (1205)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Fair Housing Act (1210)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Home Mortgage Disclosure Act (1215)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Equal Employment Opportunity (1410)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Americans with Disabilities Act	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Privacy<sup>1</sup>**

Telephone Consumer Protection Act (1300)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Controlling the Assault of Non-Solicited Pornography Marketing Act (1300)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Right to Financial Privacy Act (1345)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Electronic Banking (1370)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Gramm-Leach-Bliley Act Privacy Provisions (1375)*	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Bank Secrecy Act (BSA), USA PATRIOT Act, Office of Foreign Assets Control (OFAC) Economic Sanctions<sup>1</sup>**

Bank Secrecy Act and OFAC – FFIEC BSA Exam Manual	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
USA Patriot Act	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

**Lending Laws and Regulations<sup>1</sup>**

Fair Credit Reporting Act (1300)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Truth in Lending Act (1305)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Truth in Lending Act Restitution (1310)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OTS Mortgage Regulations (1315)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Real Estate Settlement Procedures Act (1320)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Homeowners Protection Act (1323)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Consumer Leasing Act (1325)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Flood Disaster Protection Act (1340)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Military Service Member Protections (1356)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Service Members Civil Relief Act (1357)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Homeownership Counseling Procedures (1360)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>



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

**SECTION 060**

Examination Procedures (*Required)	Incl. In scope?			Comments	Review Next Exam?	
	Yes	No	Consider		Yes	No
Electronic Banking – lending aspects (1370)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Federal Housing Administration Awareness Requirements	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Miscellaneous OTS Lending Regulations (late charges, prepayment penalties, due-on-sale or transfer clauses)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
<b>Deposit Operations Laws and Regulations<sup>1</sup></b>						
Electronic Fund Transfer Act (1330)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Expedited Funds Availability Act (1335)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Check 21 (1336)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Truth in Savings Act (1365)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Electronic Banking (1370)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Interest on Deposits (1420)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Deposit Insurance of Accounts	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
<b>Preventing Abusive Practices</b>						
Fair Debt Collection Practices Act (1350)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Unfair and Deceptive Acts/Practices – FTC Act (1354)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Unfair and Deceptive Acts/Practices – Credit Practices Rule (1355)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Consumer Protection in Sales of Insurance (1380)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OTS Advertising Rule (1425)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
<b>Other Operational Issues</b>						
Bank Protection Act (1405)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Branch Closings (1430)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Branch Review Procedures	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

# Appendix B: Examination Scheduling, Scoping and Management

## Section 060

### Estimated Time to Complete Exam

This Exam:

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

\_\_\_\_\_

\_\_\_\_\_

Next Exam:

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

\_\_\_\_\_

\_\_\_\_\_

### Other Comments

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

### Scope for This Exam

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

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

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

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

### Scope Recommendations for Next Exam

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

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

After the exam has concluded, please:

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

---

<sup>1</sup> The required compliance review areas during each examination cycle include BSA/ OFAC Economic Sanctions/ USA PATRIOT Act, Fair Lending/ Nondiscrimination, Compliance Management, Truth in Lending Act, and Flood Disaster Protection Act. In addition, the required compliance review areas include any new nondiscrimination, consumer protection, or public interest requirement, for the initial exam cycle after implementation.

**EXAMINATION MANAGEMENT CHECKLIST**

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

<b>Prior to the Examination</b>	
<b>No later than 60 days prior to exam</b>	<b>Initial When Completed</b>
Contact ARD/FM/Lead Compliance Examiner/Office Examiner/Financial Analyst/CRA Specialist to discuss the following (contact association management for an update, if warranted):	
• Developments at the association since the prior examination	
• Staffing and assignments	
• Potential need for specialists, including:	
– Credit specialist	
– Capital Market examiners	
– Appraiser	
– Accountant	
– Trust examiner	
– Information technology specialist	
• Items to be reviewed /prepared prior to final customization of the PERK:	
• Travel issues	
• Telecommuting options	
• Involvement of other agencies, if applicable	
• Application Condition Monitoring Report, if applicable	
Date of Meeting/Discussion:	

## Appendix C: Examination Scheduling, Scoping, and Management

## Section 060

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

<b>No later than 30 days prior to exam</b>	<b>Initial When Completed</b>
Finalize and send PERK – Date sent:	
Input PERK Mail Date online	
Ensure CRA PERK is included in the PERK, if applicable	
Contact CRA Specialist for preparation of fair lending summaries	
E-mail assisting examiners regarding assignments, travel issues, telecommuting options, and other logistical information	

<b>No later than one week before exam</b>	<b>Initial When Completed</b>
Finalize Scope Worksheet	
Review ILDR and LARs and create loan samples	
Contact CEO regarding exam logistics (start time, dress code, etc.) and to schedule initial meeting	
E-mail assisting examiners with any additional information obtained since initial e-mail	
Complete and submit an exam supply checklist	
Send prior exam work papers, supplies, etc. to exam site, if applicable	
Review telecommute requests and forward to ARD/FM for approval	

## Appendix C: Examination Scheduling, Scoping, and Management

## Section 060

<b>During the Examination</b>	
<b>First week of exam</b>	<b>Initial When Completed</b>
Input exam start date online and download the appropriate ROE shell	
Input PERK complete date online	
Provide phone number(s) to appropriate personnel	
Conduct initial meeting with CEO/senior management	
Establish ongoing meetings with management of savings association	
Establish ongoing updates with ARD/FM/Compliance EIC/CRA Specialist	
Discuss scope and assignments with assistants, including time for completion	
Ensure timely receipt and dissemination of PERK materials	
Distribute exam shells to appropriate examiners by including them in "working group" when shell is downloaded	

<b>Ongoing</b>	<b>Initial When Completed</b>
Coordinate schedules/timeframes	
Establish exit meeting and other meeting dates	
Coordinate interactions with association staff (control flow of memos and findings sheets)	
Provide exception sheets to association management for its review and response, if necessary	
Adjust scope and exam procedures to address issues/findings/concerns and reallocate resources if warranted; discuss with ARD/FM	
Ensure all required Compliance programs are completed, including programs required for at least one examination cycle after a new or amended regulation goes into effect. Compliance minimums:	
<ul style="list-style-type: none"> <li>• Compliance Oversight Examination Program (COEP)</li> </ul>	
<ul style="list-style-type: none"> <li>• Fair Lending</li> </ul>	
<ul style="list-style-type: none"> <li>• BSA/ OFAC/ USA PATRIOT Act</li> </ul>	
<ul style="list-style-type: none"> <li>• Flood</li> </ul>	
<ul style="list-style-type: none"> <li>• Truth in Lending</li> </ul>	
Communicate with other agencies as warranted	
Monitor the following:	
<ul style="list-style-type: none"> <li>• Telecommuting issues</li> </ul>	
<ul style="list-style-type: none"> <li>• Travel issues</li> </ul>	
<ul style="list-style-type: none"> <li>• WebTA/Leave issues</li> </ul>	
Prepare updates for FM/ AD, and regional scheduler on the status of the exam, if necessary. (For example, changes to staffing, requests for additional examiners, early release of examiners, or requests for extension of exam.)	
Review work papers to ensure that conclusions and ratings are supported	

## Appendix C: Examination Scheduling, Scoping, and Management

## Section 060

Prepare preliminary findings and conclusions	
Draft ROE comments and edit comments prepared by assisting examiners. Verify completion of: <ul style="list-style-type: none"> <li>• Matters Requiring Board of Attention page</li> <li>• Risk Assessment Summary page</li> <li>• Concentrations page</li> </ul>	
Discuss findings, conclusions, and potential ratings with ARD/FM and obtain concurrence prior to exam exit meeting. Discuss any compliance issues with regional compliance examiner.	
Enforcement Review Committee needed?	
Prepare exam exit meeting agenda and conduct meeting	
Assemble OTS materials (work papers, reference materials, supplies) for shipment	
Return association materials	
Complete ROE and upload Field Final	
Input exam completion date in EDS	
Input EDS information: <ul style="list-style-type: none"> <li>• Ratings</li> <li>• Supplemental</li> <li>• Reportable Data</li> <li>• Compliance</li> <li>• Follow-Up tab: <ul style="list-style-type: none"> <li>– Matters Requiring Board Attention</li> <li>– Corrective actions</li> <li>– Check appropriate BSA box</li> </ul> </li> </ul>	
Prepare memo and update Scope Worksheet for inclusion in Administration File that sets forth information for the next exam, i.e., areas that should be reviewed next field visit or exam, new activities or management that were not in place during the full review period.	
Request assistant examiners' completed Examiner Self Assessment forms	
Initiate PERK PAC for next exam	

<b>Post-Examination</b>	
Issue ROE: <ul style="list-style-type: none"> <li>• Within 30 days – “1” or “2” composite ratings</li> <li>• Within 45 days – “3,” “4,” or “5” composite ratings</li> </ul>	
ROE Response Due Date (if required):	
ROE Response Reviewed (if applicable)	
Enforcement Review Committee Scheduled date:	
Conduct the Board meeting	
Complete and discuss examiner assignment records with examiners and case FM/ ARD	
Discuss ongoing role of EIC with ARD/FM, including possible role in ongoing	

## Appendix C: Examination Scheduling, Scoping, and Management

## Section 060

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monitoring of the association	
Finalize PERK PAC for next exam	
Update Regulatory Profile data and develop scoping recommendations for next exam	
Discuss findings with financial analyst/ review examiner	
Trust Exams – complete Trust Regulatory Profile, if applicable	
Ensure Holding Company ROE and rating are finalized, if applicable	
Close out any outstanding issues with other agencies, if applicable	
Update Application Condition Monitoring Report, if applicable	
Complete and transmit work paper documentation	
<ul style="list-style-type: none"><li>• Upload/review remaining electronic work papers</li></ul>	
<ul style="list-style-type: none"><li>• Ensure indexes of hard copy work papers identify all electronic work papers</li></ul>	
<ul style="list-style-type: none"><li>• Send hard copy work papers to ARD/FM/record center</li></ul>	
<ul style="list-style-type: none"><li>• Lock electronic work papers</li></ul>	
File this form in the Administration work papers at 060C	

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# Appendix D: Examination Scheduling, Scoping, and Management

## Section 060

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### EXCEPTION SHEET

(Number [Click&type])

---

Date:	[Click&type]
Management Response Required by:	[Click&type]

Institution:	[Click&type]	Docket No:	[Click&type]
City, State:	[Click&type]	Exam Date:	[Click&type]

Work Paper Reference:	[Click&type]	Subject:	[Click&type]
Regulation or Regulatory Guidance Reference:	[Click&type]		

Background (basis, context):

Exception No. 1:	[Click&type]		
Corrective Action Required:	[Click&type]		
Exception No. 2:	[Click&type]		
Corrective Action Required:	[Click&type]		
Examiner:	[Click&type]	Date:	[Click&type]

### MANAGEMENT RESPONSE

---

[Click&Type] {Response should address each exception and include planned corrective actions, including timetables.}

Signature: /s/

Date:

---

### EXAMINER REVIEW

---

[Click&Type] {Review should assess whether management's planned corrective actions, including timetables, are adequate/appropriate}

Signature: /s/

Date:

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## Ratings: Developing, Assigning, and Presenting

This Handbook Section provides guidance in the following areas:

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

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### LINKS

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

### COMMENTS AND CONCLUSIONS

There are unique factors to consider when developing conclusions, comments, and ratings for each CAMELS component, Compliance, and Trust area. (See the Trust and Asset Management Handbook for guidance in the Trust area.) Each comment should be accurate, complete and concise.

### Developing Report Comments

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

- Disclose the rating.
- Clearly state the conclusion and a summary of findings.
- Clearly identify patterns, practices, trends, and their causes.
- Present comments in a meaningful order, discussing major strengths and weaknesses, with proper emphasis and tone accorded to individual topics. The severity of the problem will dictate its order of presentation. Consider how the problem affects the association's other activities and any mitigating circumstances.
- Identify substantive safety and soundness and compliance issues.

- Include the deficient underlying practices when you note patterns of regulatory noncompliance.
- Include a summary of material deficiencies that support 3, 4, and 5 component and compliance ratings.
- Support conclusions with appropriate analysis and prepare a concise, effective summary that does not lose the reader in detail.
- Assess the effect of examination findings on future operations.
- Include a discussion of corrective action where necessary.
- Identify actions needed to correct weaknesses, outstanding deficiencies, or violations as appropriate.
- The extent to which the association has adequately addressed self-identified deficiencies and violations, substantive violations discovered during the examination, with a discussion of the underlying cause of each substantive violation.
- Support the comments with work papers and other retained documents. Include information that provides a clear understanding of the overall condition, adequacy of management practices, causes of major problems, and recommendations for remedial action.

The Compliance comment should discuss:

- The details of the compliance management program and the effectiveness of management in implementing the compliance program.
- The BSA and Customer Identification Program. Discuss the structure and effectiveness of the association's BSA Program, specifically referencing regulatory requirements (internal controls, independent testing, designated person and training), Customer Identification Program, and any comments pertinent to examination findings. Examination comments on BSA must address all of the applicable requirements set forth in the most current FFIEC BSA/AML Examination Manual as specified in Preparing the BSA/AML Comments for the Report of Examination on pages 50-51. For associations with effective BSA Programs, comments should be concise but convey that the program contains all required elements and is effective. For associations with isolated to pervasive BSA Program issues or concerns, clearly identify where weaknesses exist, corrective action is needed, and the association's progress toward or capacity to implement those actions.
- The adequacy of inclusion and coverage of each of the working SMAART components.

- The extent to which the association has adequately addressed self-identified deficiencies and violations, substantive violations discovered during the examination, with a discussion of the underlying cause of each substantive violation.

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

## Primary Factors to Consider

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

- Material items that relate to safety and soundness, and significant adverse findings for technology risks, compliance, or trust and the causes of those problems.
- An assessment of the compliance management program's performance.
- An assessment of the effectiveness of overall risk management.
- Regulatory violations and the reasons for any material patterns. List violations on the Violations of Laws and Regulations page. You should not include them on the Examination Conclusions and Comments page unless they are significant.
- How your findings within each of the CAMELS, Compliance, and Trust areas interrelate, affect the overall financial condition and safety and soundness of the association's operations, and reflect on the effectiveness of management.
- Material adverse findings outstanding from the prior examination and management's efforts to date to correct the problems.

## Formulating an Overall Conclusion

As you complete individual report comments and compile work papers, you should begin to formulate an impression of the association's overall condition. The Examination Conclusions and Comments page must provide a concise narrative statement of the major findings of examination, supporting the conclusions you present.

The development of a substantive overall conclusion requires that you:

- Review major findings from the examination (including trends).
- Consider the association's operating environment (both internal and external factors).

- Consider the need for supervisory monitoring or enforcement action.
- Convert ultimate determinations into ratings.
- Communicate results effectively.
- Facilitate the corrective action process.
- State conclusions and the overall evaluation in the ROE.

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

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

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

- Existing systems, policies, and procedures.
- The business plan.
- Projections for operating performance.
- Use of information technology.
- Management effectiveness and ability to effect corrective actions.
- Current financial market and economic conditions.

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

## ASSIGNING RATINGS

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

- **CAMELS components and composite ratings** – OTS uses the CAMELS rating system to evaluate a savings association's overall condition and performance by assessing six rating components. The six components are Capital Adequacy, Asset Quality, Management, Earnings,

Liquidity, and Sensitivity to Market Risk. OTS then assigns each association a composite rating based on your assessment of its overall condition and level of supervisory concern.

- **Compliance rating** – OTS uses a Compliance Rating System that addresses general compliance with fair lending, consumer protection, and other public interest laws and regulations. This rating system is substantially equivalent to the FFIEC-approved interagency compliance rating system.
- Trust component and composite ratings – when applicable, OTS uses the Uniform Interagency Trust Ratings Definitions to evaluate the overall condition and performance of the trust operations. (See [Trust and Asset Management Handbook Section 060](#), Assignment of Ratings.)

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

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

OTS personnel use the ratings for a variety of purposes:

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

The ratings help determine appropriate strategies including the following:

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

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

## **CAMELS Rating System**

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

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

### **Composite Rating**

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

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

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

Although the composite rating assigned to the association should normally have a close relationship to the individual CAMELS component ratings, you should not derive the composite rating merely by

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

computing an arithmetic average of the component ratings. Such a simplistic, mechanical approach will not reflect the true condition of the savings association; nor will it indicate the appropriate supervisory actions.

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



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

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

When you examine an association in troubled condition, you should consult the regulatory profile, supervisory correspondence, the previous examination, and any other pertinent information to determine the operating restrictions to which an association is subject. You must then analyze the association's operations and ensure that it complies with all restrictions. For further information regarding operating restrictions, refer to [Examination Handbook Section 080](#), Enforcement Actions.

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

- [Examination Handbook Section 080](#), Enforcement Actions.
- RB 3b (Policy Statement on Growth for Savings Associations).
- OTS assessment regulation at 12 CFR § 502.10.
- OTS audit regulation at 12 CFR § 562.4.
- OTS transactions with affiliates regulation at 12 CFR § 563.41.
- OTS capital regulation at 12 CFR § 565.4.
- OTS directors' regulation at 12 CFR §§ 563.550 through 563.590.
- FDIC risk-based deposit insurance assessment regulation at 12 CFR Part 327.
- FDIC brokered deposit restrictions regulation at 12 CFR § 337.6.

## ***Component Ratings***

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

### **Capital Adequacy**

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

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

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

### ***PCA Levels***

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

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

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

## **Asset Quality**

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

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

## **Management**

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

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

- Credit
- Interest rate
- Market
- Operating or transaction
- Reputation
- Strategic

- Compliance
- Legal
- Liquidity
- Price

The following practices demonstrate sound management:

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

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

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

You must address your assessment of management and the board as it relates to overall risk mitigation activities including compliance management, technology risk controls and, if applicable, trust and asset management. A Compliance or Trust rating of 3 or lower, or most recent IT examination rating of 3 or lower, should be reflected in the Management component of the CAMELS rating as follows:

- When the Compliance, IT, or Trust rating is 3, the Management rating may not be better than 2.
- When the Compliance, IT, or Trust ratings is 4 or 5, the Management rating may not be better than 3.

Generally, the level of substantive violations, programmatic deficiencies and OTS supervisory attention associated with compliance ratings of 4 or 5 are inconsistent with management performance under the CAMELS system of anything higher than a 3 for Management, and may be sufficient alone, or in combination with other management shortcomings, to compel even lower ratings of Management.

## **Earnings**

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

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

You should also consider the association's operating risks to determine if its earnings position is stable and sufficient. Use professional judgment and analyze the stability and sufficiency of noninterest earnings, including gains on sales of loans and securities. In addition, consider the adequacy of an association's interest rate risk management; if it is inadequate the association's earnings may be adversely affected by a change in market interest rates.

## **Liquidity**

Savings associations must maintain sufficient liquidity to ensure safe and sound operations (12 CFR 563.161.) An association's liquidity management process should be sufficient to meet its daily funding needs and cover both expected and unexpected deviations from normal daily operations. Primary tools for measuring and managing liquidity risk include cash flow projections, diversified funding sources, stress testing, a cushion of liquid assets, and a formal, well-developed contingency funding plan. OTS expects all savings associations to manage liquidity risk using processes and systems commensurate with the institution's complexity, risk profile, and scope of operations. See [CEO Memo 342](#), Interagency Policy Statement on Funding and Liquidity Risk Management.

## **Sensitivity to Market Risk**

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

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

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

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

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

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

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

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

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

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

- Quality of oversight by the board and senior management.

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

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

### ***Thrift Performance Evaluation and CAMELS Rating Assignments***

The Uniform Thrift Performance Report (UTPR) provides percentile rankings for many measures of association performance as compared to peer performance. Use the Risk Monitoring System (RMS) Query Builder to find the CAMELS composite ratings of other associations with similar key ratios. These tools are useful in comparing an association's performance with that of its peers to assign ratings that are consistent with associations having similar ratios. However, since the composite CAMELS rating is an indicator of the overall health and viability of an association, it is important that you rate associations on their absolute performance as well as against regional or state peer performance. Associations in some states or regions may perform better than peer averages or medians, but perform poorly in absolute terms or when compared with peer averages or medians of other regions. Peer performance in such cases would not necessarily reflect associations that were being operated in a safe and sound manner. Rather, those averages could reflect substandard performance. The CAMELS ratings should accurately reflect the condition of an association, regardless of local or regional peer performance.

**Because an association meets its minimum regulatory capital or other regulatory requirement does not guarantee that its condition is viable.**

You cannot measure an association's performance solely in numbers. Because an association meets its minimum regulatory capital or other regulatory requirement does not guarantee that its condition is viable. Therefore, you must use professional judgment and

consider both qualitative and quantitative criteria when analyzing an association's performance, taking into account:

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

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

## **Compliance Rating System**

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

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

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

## ***Assigning the Compliance Rating***

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

In general, these factors include:

- Implementation of a formal written compliance management program reliably covering OTS's SMAART components suitable to the size and operational complexity of the association.



- The commitment of the board and management, as evidenced by its ability and willingness to maintain compliance.
- Internal self-assessments and compliance reviews.
- Competency of management, as evidenced by the adequacy of operating systems, including internal procedures and controls designed to ensure compliance.
- Appropriate compliance training programs.
- The nature and extent of violations (including repeat violations) and deficiencies in actual compliance performance as a measure of the effectiveness of management's efforts.

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

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

The Compliance Rating System is a scale of 1 through 5, in increasing order of supervisory concern. A rating of 1 indicates excellence, while a rating of 5 represents the lowest, most critically deficient level of performance and the highest level of supervisory concern. The Compliance Rating System is a single-value rating system. The single rating value assigned reflects overall compliance performance and you must substantiate the rating by the contents of the ROE and the examination work papers. Characteristics of the five Compliance Ratings available to the examiner will conform to the rating descriptions in Appendix B. However, as these descriptions are a composite, not all characteristics will be present at every institution. You must apply this guidance to capture an accurate overall evaluation of the association's compliance management performance for the examination period, keeping in mind the policy to encourage self-identifying and self-correcting controls.

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

## Consistency in Rating Assignments

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

## Maintaining and Updating the Ratings

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

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

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

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

### ***Documentation and Support***

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

### ***Disclosure of Ratings***

OTS discloses CAMELS composite and component, and Compliance ratings in the ROE. OTS does not disclose ratings in meetings with association management and boards of directors. (See the next section on Meetings with Management and the Board of Directors.)

Obtain sufficient concurrence from regional management, so that the ratings are final, or subject to revision only in rare instances. In accordance with OTS's ROE instructions add the component and Compliance rating to the applicable ROE page. The Examination Conclusions and Comments page should provide a concise narrative statement of the major findings of the examination. In addition, the Examination Conclusions and Comments page should clearly state how the examination findings

within each of the CAMELS, Compliance, and Trust areas interrelate and affect the overall financial condition and safety and soundness of the association's operations.

## ***Supervisory Letter***

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

## **MEETINGS WITH MANAGEMENT AND THE BOARD OF DIRECTORS**

You should not disclose ratings during examination exit meetings. This is particularly important for examination reports that require review by the large bank unit. For all other cases, it is preferable to use the rating definition terminology in describing the examination results, but not the actual ratings.

## **Management Discussions**

During the discussion with management, you should discuss the criteria you considered in assigning CAMELS component and composite ratings and the compliance rating. You should not disclose the ratings themselves, but do discuss all factors considered in assigning each component rating and those considered in assigning the composite rating. You should indicate that a careful evaluation of each CAMELS component and Compliance determines the composite rating. You should clarify that OTS does not base the composite rating on an arithmetic average of the components, but on a qualitative analysis of the criteria comprising each component, the interrelationship between components, and, more importantly, the overall level of supervisory concern.

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

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

## Meetings with the Board of Directors

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

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

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

## Types of Meetings

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

### **Regular Meetings**

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

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

Generally, you should always meet with the board. While a face-to-face meeting may not be necessary for an association rated 1 or 2, you must make every effort to communicate with the board following each comprehensive examination. A conference call can be an effective option and may enhance the Board’s understanding of the regulatory process, as well as bolster lines of communication between the board and regulators.

Always meet face to face if you note adverse trends, increased risk profile, or other matters that need the board's attention. You must meet face to face with the board of directors if the association has:

- A CAMELS composite or Compliance rating of 3, 4 or 5.
- A Holding Company rating of Unsatisfactory.

If an association's assets exceed \$1 billion, you should meet face to face with the board regardless of adverse trends.

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

## ***Participation***

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

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

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

## ***Special Meetings***

Reasons to schedule a special meeting include the following:

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

- To comply with directorate's request to meet.

## **Meeting Preparation, Presentation, and Documentation**

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

- **Preparation**

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

- **Presentation**

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

- **Documentation**

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

## **REFERENCES**

### **Code of Federal Regulations (12 CFR)**

#### ***OTS Regulations***

§ 502.10	Assessments
§ 562.4	Audit of Savings Associations and Holding Companies
§ 563.161	Management and Financial Policies
§ 563.41	Transactions With Affiliates
§ 563.550	Notice of Change of Directors or Senior Executive Officer
§ 565.4	Capital Measures and Capital Category Definitions

#### ***FDIC Regulations***

Part 327	Assessments
§ 337.6	Brokered Deposits

## **Office of Thrift Supervision CEO Memos and Bulletins**

- CEO 212 Interagency Advisory on the Confidentiality of the CAMELS Rating and Other Nonpublic Supervisory Information
- CEO 342 Interagency Policy Statement on Funding and Liquidity Risk Management
- RB 3b Policy Statement on Growth for Insured Institutions
- RB 18 General Enforcement Policy Series
- TB 13a Management of Interest Rate Risk, Investment Securities, and Derivative Activities
- TB 48-27 Assessments and Fees Under 12 CFR Part 502
- TB 48-29 Assessments and Fees Under 12 CFR Part 502
- TB 68b Appeals and Ombudsman Matters

## **Other References**

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

OTS Transmittal 166: Regulatory Citations to UFIRS



# Ratings: Developing, Assigning, and Presenting Program

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## EXAMINATION OBJECTIVES

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

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

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

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

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

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

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

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

## EXAMINATION PROCEDURES

WKP. REF.

1. Ensure that examiners reviewed the Matters Requiring Board Attention and Corrective Actions from the three or four previous ROEs to ensure that the board and management have taken appropriate corrective action where necessary and persistent problems have not recurred.
- 
2. Review analyses, comments, exceptions, and conclusions in the work papers for each CAMELS area, Compliance, and if applicable, Trust, and perform the following:

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

# Ratings: Developing, Assigning, and Presenting Program

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WKP. REF.

- Resolve any contradictory conclusions. Support all conclusions with facts obtained during the examination.
  - Determine the significance of the findings related to safety and soundness and overall regulatory compliance.
  - Discuss findings with appropriate institution personnel and verify conclusions as appropriate.
  - Ensure all violations are listed on the Violations of Laws and Regulations page in the ROE.
- 
3. Review the draft CAMELS, Compliance, and Trust comments. Review assisting examiners' comments on management's self-assessment efforts and record of self-correcting compliance deficiencies. Talk with assisting examiners about their overall observations and findings applicable to the comments and determine whether conclusions are reasonable. Consider the interrelationships between findings noted for each CAMELS component, Compliance, and if applicable, Trust. If necessary, make adjustments to ensure that comments are comprehensive and to eliminate any duplication. If the EIC is aware of other criteria that are not known to assisting personnel, the EIC should determine if these criteria are relevant and whether or not to include the comments.
- 
4. Ensure comments fairly represent examination results according to ROE instructions. Ensure conclusions are well supported in work papers and comments include any significant items noted in work papers. The tone and content of each comment should be concise and appropriate, as outlined in the Handbook.
- 
5. Review the proposed corrective actions related to any violation or exception to ensure it is appropriate.
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<b>Exam Date:</b>	
<b>Prepared By:</b>	
<b>Reviewed By:</b>	
<b>Docket #:</b>	

# Ratings: Developing, Assigning, and Presenting Program

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WKP. REF.

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

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

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

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

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

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

# Ratings: Developing, Assigning, and Presenting Program

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WKP. REF.

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

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11. Review the Examination Conclusions and Comments page to ensure the tone and content supports the assigned composite, Compliance, and if applicable, Trust ratings. Finalize the ratings and comments after a thorough review. Ensure the completion of the EDS/ROE ratings section, including the Technology Risk Controls (TRC) flag.

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12. Discuss findings with management, typically the CEO. We recommend that you use an agenda. Discuss at least the following topics:
  - The purpose of the meeting.
  - All items that you might include in the examination report.
  - Overall conclusions regarding the institution.
  - Management's corrective action responses.

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

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

# Ratings: Developing, Assigning, and Presenting Program

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WKP. REF.

14. Include only actions that require a response from the board of directors on the Matters Requiring Board Attention page. Obtain a firm commitment for corrective action in the appropriate narrative. Place corrective actions at the end of the narrative on the appropriate ROE page. Communicate specific timeframes for implementation of significant required actions.
- 

15. Provide any information to the regional office that will be useful for revising the Regulatory Profile.
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16. Prepare the ROE cover page letter, if necessary, in accordance with regional office policy.
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17. Prepare to meet with the board of directors regarding findings.
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18. Ensure that your review meets the Objectives of this Handbook Section.
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## Off-Site Ratings

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

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

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

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

# Ratings: Developing, Assigning, and Presenting Program

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WKP. REF.

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

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

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

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

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

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

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

# Ratings: Developing, Assigning, and Presenting Program

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WKP. REF.

26. Identify any changes in the association's condition and operating practices. Determine if a change in a CAMELS component or composite rating, or Compliance rating, more appropriately reflects the condition of the association.
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27. Determine the need for and recommend, if necessary, a regular examination or a limited on-site examination of areas that you cannot adequately analyze off-site.
- 

28. Recommend any change in the CAMELS component or composite ratings, or Compliance rating, to the supervisory manager or other appropriate manager in the regional office. Support any recommendation for change with a narrative memorandum and documented analysis explaining and supporting the reasons for the change.
- 

29. If the regional office approves a change in the composite or a component CAMELS rating, or the Compliance rating, prepare a supervisory letter or memorandum to the association's board of directors to inform them of the change in the rating. The memo should explain the reasons for the change and any resulting consequences. The memorandum should also contain a definition of the new rating assigned and standard language prohibiting disclosure of the rating.
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30. Enter the new rating(s) in the EDS ratings section and make certain they are correct.
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31. Update the Regulatory Profile with any other appropriate information.
- 

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

# Ratings: Developing, Assigning, and Presenting Program

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WKP. REF.

## EXAMINER'S SUMMARY, RECOMMENDATIONS, AND COMMENTS

Exam Date:	
Prepared By:	
Reviewed By:	
Docket #:	



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

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

**Introduction**

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

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

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

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

**Overview**

Under the UFIRS, each financial institution is assigned a composite rating based on an evaluation and rating of six essential components of an institution's financial condition and operations. These component factors address the adequacy of capital, the quality of assets, the capability of management,

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

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

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

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

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

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

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

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

## **COMPOSITE RATINGS**

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

### **Composite 1**

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

### **Composite 2**

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

### **Composite 3**

Financial institutions in this group exhibit some degree of supervisory concern in one or more of the component areas. These financial institutions exhibit a combination of weaknesses that may range from moderate to severe; however, the magnitude of the deficiencies generally will not cause a component to be rated more severely than 4. Management may lack the ability or willingness to effectively address weaknesses within appropriate time frames. Financial institutions in this group generally are less capable of withstanding business fluctuations and are more vulnerable to outside influences than those institutions rated a composite 1 or 2. Additionally, these financial institutions may be in significant noncompliance with laws and regulations. Risk management practices may be less than satisfactory relative to the institution's size, complexity, and risk profile. These financial institutions require more

than normal supervision, which may include formal or informal enforcement actions. Failure appears unlikely, however, given the overall strength and financial capacity of these institutions.

#### **Composite 4**

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

#### **Composite 5**

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

### **COMPONENT RATINGS**

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

#### **Capital Adequacy**

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

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

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

### **Ratings**

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

### **Asset Quality**

The asset quality rating reflects the quantity of existing and potential credit risk associated with the loan and investment portfolios, other real estate owned, and other assets, as well as off-balance sheet transactions. The ability of management to identify, measure, monitor, and control credit risk is also reflected here. The evaluation of asset quality should consider the adequacy of the allowance for loan and lease losses and weigh the exposure to counterparty, issuer, or borrower default under actual or implied contractual agreements. All other risks that may affect the value or marketability of an

institution's assets, including, but not limited to, operating, market, reputation, strategic, or compliance risks, should also be considered.

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

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

***Ratings***

- 1 A rating of 1 indicates strong asset quality and credit administration practices. Identified weaknesses are minor in nature and risk exposure is modest in relation to capital protection and management's abilities. Asset quality in such institutions is of minimal supervisory concern.
- 2 A rating of 2 indicates satisfactory asset quality and credit administration practices. The level and severity of classifications and other weaknesses warrant a limited level of supervisory attention. Risk exposure is commensurate with capital protection and management's abilities.
- 3 A rating of 3 is assigned when asset quality or credit administration practices are less than satisfactory. Trends may be stable or indicate deterioration in asset quality or an increase in risk

exposure. The level and severity of classified assets, other weaknesses, and risks require an elevated level of supervisory concern. There is generally a need to improve credit administration and risk management practices.

- 4 A rating of 4 is assigned to financial institutions with deficient asset quality or credit administration practices. The levels of risk and problem assets are significant, inadequately controlled, and subject the financial institution to potential losses that, if left unchecked, may threaten its viability.
- 5 A rating of 5 represents critically deficient asset quality or credit administration practices that present an imminent threat to the institution's viability.

## **Management**

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

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

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

- The level and quality of oversight and support of all institution activities by the board of directors and management.
- The ability of the board of directors and management, in their respective roles, to plan for, and respond to, risks that may arise from changing business conditions or the initiation of new activities or products.
- The adequacy of, and conformance with, appropriate internal policies and controls addressing the operations and risks of significant activities.

- The accuracy, timeliness, and effectiveness of management information and risk monitoring systems appropriate for the institution's size, complexity, and risk profile.
- The adequacy of audits and internal controls to: promote effective operations and reliable financial and regulatory reporting; safeguard assets; and ensure compliance with laws, regulations, and internal policies.
- Compliance with laws and regulations.
- Responsiveness to recommendations from auditors and supervisory authorities.
- Management depth and succession.
- The extent that the board of directors and management is affected by, or susceptible to, dominant influence or concentration of authority.
- Reasonableness of compensation policies and avoidance of self-dealing.
- Demonstrated willingness to serve the legitimate banking needs of the community.
- The overall performance of the institution and its risk profile.

***Ratings***

- 1 A rating of 1 indicates strong performance by management and the board of directors and strong risk management practices relative to the institution's size, complexity, and risk profile. All significant risks are consistently and effectively identified, measured, monitored, and controlled. Management and the board have demonstrated the ability to promptly and successfully address existing and potential problems and risks.
- 2 A rating of 2 indicates satisfactory management and board performance and risk management practices relative to the institution's size, complexity, and risk profile. Minor weaknesses may exist, but are not material to the safety and soundness of the institution and are being addressed. In general, significant risks and problems are effectively identified, measured, monitored, and controlled.
- 3 A rating of 3 indicates management and board performance that need improvement or risk management practices that are less than satisfactory given the nature of the institution's activities. The capabilities of management or the board of directors may be insufficient for the type, size, or condition of the institution. Problems and significant risks may be inadequately identified, measured, monitored, or controlled.
- 4 A rating of 4 indicates deficient management and board performance or risk management practices that are inadequate considering the nature of an institution's activities. The level of problems and risk exposure is excessive. Problems and significant risks are inadequately



identified, measured, monitored, or controlled and require immediate action by the board and management to preserve the soundness of the institution. Replacing or strengthening management or the board may be necessary.

- 5 A rating of 5 indicates critically deficient management and board performance or risk management practices. Management and the board of directors have not demonstrated the ability to correct problems and implement appropriate risk management practices. Problems and significant risks are inadequately identified, measured, monitored, or controlled and now threaten the continued viability of the institution. Replacing or strengthening management or the board of directors is necessary.

### **Earnings**

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

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

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

***Ratings***

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

**Liquidity**

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

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

- The adequacy of liquidity sources compared to present and future needs and the ability of the institution to meet liquidity needs without adversely affecting its operations or condition.

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

### ***Ratings***

- 1 A rating of 1 indicates strong liquidity levels and well-developed funds management practices. The institution has reliable access to sufficient sources of funds on favorable terms to meet present and anticipated liquidity needs.
- 2 A rating of 2 indicates satisfactory liquidity levels and funds management practices. The institution has access to sufficient sources of funds on acceptable terms to meet present and anticipated liquidity needs. Modest weaknesses may be evident in funds management practices.
- 3 A rating of 3 indicates liquidity levels or funds management practices in need of improvement. Institutions rated 3 may lack ready access to funds on reasonable terms or may evidence significant weaknesses in funds management practices.
- 4 A rating of 4 indicates deficient liquidity levels or inadequate funds management practices. Institutions rated 4 may not have or be able to obtain a sufficient volume of funds on reasonable terms to meet liquidity needs.
- 5 A rating of 5 indicates liquidity levels or funds management practices so critically deficient that the continued viability of the institution is threatened. Institutions rated 5 require immediate external financial assistance to meet maturing obligations or other liquidity needs.

### **Sensitivity to Market Risk**

The sensitivity to market risk component reflects the degree to which changes in interest rates, foreign exchange rates, commodity prices, or equity prices can adversely affect a financial institution's earnings or economic capital. When evaluating this component, consideration should be given to: management's ability to identify, measure, monitor, and control market risk; the institution's size; the nature and

complexity of its activities; and the adequacy of its capital and earnings in relation to its level of market risk exposure. For many institutions, the primary source of market risk arises from nontrading positions and their sensitivity to changes in interest rates. In some larger institutions, foreign operations can be a significant source of market risk. For some institutions, trading activities are a major source of market risk.

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

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

***Ratings***

- 1 A rating of 1 indicates that market risk sensitivity is well controlled and that there is minimal potential that the earnings performance or capital position will be adversely affected. Risk management practices are strong for the size, sophistication, and market risk accepted by the institution. The level of earnings and capital provide substantial support for the degree of market risk taken by the institution.
- 2 A rating of 2 indicates that market risk sensitivity is adequately controlled and that there is only moderate potential that the earnings performance or capital position will be adversely affected. Risk management practices are satisfactory for the size, sophistication, and market risk accepted by the institution. The level of earnings and capital provide adequate support for the degree of market risk taken by the institution.
- 3 A rating of 3 indicates that control of market risk sensitivity needs improvement or that there is significant potential that the earnings performance or capital position will be adversely affected. Risk management practices need to be improved given the size, sophistication, and level of market risk accepted by the institution. The level of earnings and capital may not adequately support the degree of market risk taken by the institution.
- 4 A rating of 4 indicates that control of market risk sensitivity is unacceptable or that there is high potential that the earnings performance or capital position will be adversely affected. Risk management practices are deficient for the size, sophistication, and level of market risk accepted by the institution. The level of earnings and capital provide inadequate support for the degree of market risk taken by the institution.

- 5 A rating of 5 indicates that control of market risk sensitivity is unacceptable or that the level of market risk taken by the institution is an imminent threat to its viability. Risk management practices are wholly inadequate for the size, sophistication, and level of market risk accepted by the institution.

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## **COMPLIANCE RATING SCALE**

OTS defines the five-point Compliance Ratings as follows:

### **Rating 1**

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

### **Rating 2**

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

### **Rating 3**

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

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

**Rating 4**

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

**Rating 5**

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