

# COMMUNITY BANKING CONNECTIONS<sup>®</sup>

A SUPERVISION AND REGULATION PUBLICATION

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## VIEW FROM THE DISTRICT

*A Third District Perspective — Philadelphia*

### Preparing Now to Weather Conditions Ahead

*by Bill Spaniel, Senior Vice President & Lending Officer, Federal Reserve Bank of Philadelphia*



Bill Spaniel

Prior to becoming the senior officer in charge of supervision at the Federal Reserve Bank of Philadelphia, I spent 25 years at the Board of Governors, where I gained a deep appreciation for developing supervisory

policy. I'm looking forward to enhancing that experience by obtaining a firsthand view of supervisory operations from the frontlines. My hope is that combining these two perspectives will provide me with unique insights that I can use when interacting with Third District institutions.

When I moved from Washington, D.C., to Philadelphia in November 2015, I made one particular observation early on. Philadelphia is well prepared to handle a snowstorm! I found out firsthand that 20 inches of snow, which brought the nation's capital to a halt, can be managed effectively in Philadelphia and the surrounding region. Many cities are simply better prepared for these and other events based on history, planning, or practical experience.

Preparing for severe weather or other adverse events is an important concept for the banking industry. Although the industry has recovered from the depths of the financial crisis, with many financial ratios comparable to precrisis levels, bankers still need to be mindful of the credit cycle. Bank regulators are not at the point of sending off warnings that "a blizzard is coming," but it is still a good time for both bankers and regulators to remain attentive and prepare for the next storm clouds.

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# Helpful Hints When Filing an Application with the Federal Reserve

by Kathryn E. Haney, Director of Applications, Federal Reserve Bank of Atlanta

Banking organizations file applications and notices (collectively, “applications” or “filings”) to form holding companies, engage in nonbank activities, establish new branches, and acquire and/or merge with other institutions. This article provides some helpful hints, particularly for organizations that may not have filed an application with the Federal Reserve in recent years. Several resources are available to bankers to assist them in filing an application. These resources, as described in more detail in this article, include an electronic filing option, online information, and recent guidance issued by the Federal Reserve. Banking organizations are also encouraged to contact Reserve Bank applications staff before submitting an application to discuss the potential impact that pending examinations, outstanding supervisory issues, or material changes in an organization could have on the outcome of the application. This “best practice” can allow for meaningful dialogue between the applicant and Federal Reserve staff about potential issues that could adversely impact the timing or action on an application proposal.

## Electronic Filing Option

The Federal Reserve offers E-Apps,<sup>1</sup> an electronic filing option for applications. E-Apps, which was launched in 2008, is a web-based application that allows banking organizations

supervised by the Federal Reserve to submit applications, directly or through their authorized representatives (lawyers or consultants). No fees are associated with using E-Apps.

E-Apps is intended for filings related to bank and savings and loan holding company formations, mergers, and acquisitions; nonbanking activities; state member bank mergers and branch expansion; Federal Reserve membership; and international banking applications. E-Apps allows for submission of the original filing plus supplemental information, such as responses to the Federal Reserve’s requests for additional information.

To access E-Apps, a banking organization must first obtain a digital certificate or designate someone who already has a certificate to file on its behalf. The digital certificate is one feature of E-Apps that helps to ensure a secure environment for electronic filings. A digital certificate authenticates individuals authorized to use E-Apps and helps to secure the personal and confidential information transmitted as part of the applications filing process. Digital certificates also help to prevent unauthorized users from accessing E-Apps.

<sup>1</sup> For more information about E-Apps, see [www.federalreserve.gov/bankinfo/afi/afi.htm](http://www.federalreserve.gov/bankinfo/afi/afi.htm).

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To obtain a digital certificate, the user must complete and submit a couple of short online forms before the initial application filing through E-Apps. A digital certificate generally is issued within 48 hours, and after a certificate is obtained, it can be used for all filings. Financial institutions have the option to authorize an unlimited number of designated certificate users, such as attorneys, consultants, or in-house staff, who can file applications on their behalf through E-Apps. After being designated as a user, an authorized filer's certificate will reside on the authorized party's computer. No matter



how many institutions a party is authorized to act on behalf of, the party will receive only one certificate. Instructions and forms for obtaining a certificate can be found on the Federal Reserve's website.<sup>2</sup> After obtaining the digital certificate, the banking organization's management (or authorized representative) can access E-Apps through the Federal Reserve's website. The website includes a Quick Reference Guide and Frequently Asked Questions to guide users through the steps for submitting a filing through E-Apps. In addition, the website provides contact information for Federal Reserve Bank staff who can answer questions about E-Apps.

The process for submitting applications over the Internet has been carefully designed to ensure the confidentiality of the data and authenticity of the filer. In addition to providing a secure environment, E-Apps also provides convenience and cost savings relative to the submission of paper applications.

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<sup>2</sup> To sign up for E-Apps, see [www.federalreserve.gov/bankinforeg/afi/eapps\\_sign\\_up.htm](http://www.federalreserve.gov/bankinforeg/afi/eapps_sign_up.htm).

<sup>3</sup> More information about the electronic filing process is available at [www.federalreserve.gov/bankinforeg/afi/afi.htm](http://www.federalreserve.gov/bankinforeg/afi/afi.htm).

<sup>4</sup> For more information about the different types of applications available, see [www.federalreserve.gov/bankinforeg/afi/res\\_forms.htm](http://www.federalreserve.gov/bankinforeg/afi/res_forms.htm).

Banking organizations are encouraged to explore the use of E-Apps and reach out to their respective Federal Reserve Bank if they have questions.<sup>3</sup>

### Online Federal Reserve System Resources

The Federal Reserve also provides a number of online resources to assist banking organizations with application filings. The filing forms and related instructions for the different types of applications are located on the Federal Reserve's website.<sup>4</sup> Some filings, such as for the establishment of a

branch, do not have a form but are filed by submitting a letter to the Federal Reserve and publishing a notice in local newspapers regarding the proposed branch. The website provides "model language" that can be used for the newspaper publication.<sup>5</sup> In addition, the website offers contact information for Federal Reserve Bank applications staff in case a banking organization has a question about filing an application.<sup>6</sup>

### Recent Guidance Issued by the Federal Reserve System

The Federal Reserve has issued guidance<sup>7</sup> in recent years on the filing of applications. Banking organizations are encouraged to review this guidance, which is briefly summarized in this section. If the organization has questions regarding the guidance, Reserve Bank staff members are available to address these questions.

### New Process for Requesting Guidance from the Federal Reserve Regarding Application Proposals

In 2012, the Federal Reserve System issued Supervision and Regulation (SR) letter 12-12/Community Affairs (CA) letter 12-11, which outlines the process for an applicant to request feedback on a potential acquisition or other proposal before submission of a formal application.<sup>8</sup> Although this "prefiling" process is optional, it may be particularly helpful for

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<sup>5</sup> Filing resources are available at [www.federalreserve.gov/bankinforeg/afi/afiresources.htm](http://www.federalreserve.gov/bankinforeg/afi/afiresources.htm).

<sup>6</sup> For Federal Reserve applications contacts or other banking market information, see [www.federalreserve.gov/bankinforeg/afi/reserve\\_bank\\_info.htm](http://www.federalreserve.gov/bankinforeg/afi/reserve_bank_info.htm).

<sup>7</sup> Information about supervisory policy and guidance topics is available at [www.federalreserve.gov/bankinforeg/topics/applications.htm](http://www.federalreserve.gov/bankinforeg/topics/applications.htm).

<sup>8</sup> See SR letter 12-12/CA letter 12-11, "Implementation of a New Process for Requesting Guidance from the Federal Reserve Regarding Bank and Non-Bank Acquisitions and Other Proposals," available at [www.federalreserve.gov/bankinforeg/srletters/sr1212.htm](http://www.federalreserve.gov/bankinforeg/srletters/sr1212.htm).

# Examiners' View: A Fiduciary's Responsibilities for Unique and Special Assets

by Matthew E. Rowland, Senior Examiner, Federal Reserve Bank of Kansas City, and Erin F. Connelly, Senior Examiner, Federal Reserve Bank of Philadelphia

More than 800 community banks exercise fiduciary powers in the United States; this does not include nondepository trust companies also exercising these powers. As fiduciaries, these organizations have a duty to manage assets in the best interests of their clients, including account beneficiaries (current and remaindermen).

Often a client brings into the fiduciary relationship unique and special assets, such as real estate (e.g., residential, farm, and commercial), closely held businesses (e.g., nonpublicly traded stocks and family businesses), mineral interests (e.g., oil, gas, and coal), commodities (e.g., timber and cattle), insurance products (e.g., policies and annuities), collectibles (e.g., artwork, stamps, and jewelry), promissory notes, and tangible assets (e.g., household goods and vehicles). These assets are held in any number of managed and nonmanaged accounts, including irrevocable and revocable trusts, individual retirement accounts, directed accounts, and irrevocable life insurance trusts.

Unique and special assets present particular challenges to the fiduciaries acting as the administrators and asset managers for these accounts. For example, unique and special assets are difficult to value because they are not traded on a financial market and, therefore, do not have readily determinable market values compared with more traditional assets, such as stocks and bonds. This article identifies the challenges and risks of retaining unique and special assets in fiduciary accounts and suggests practices to mitigate these risks.

## Challenges with Administering Unique and Special Assets

The first and foremost challenge fiduciaries may face is that the retention of unique and special assets may not align with the organization's basic fiduciary duties, such as return maximization or loyalty to the current beneficiaries and remaindermen. For example, in many instances, grantors will direct a fiduciary to retain a unique and special asset in an account to ensure the asset, such as farm property, closely

held businesses, or collectibles, remains within a family. However, these assets may not provide an appropriate investment return for the account. Similarly, grantors may request that the fiduciary maintain insurance policies in a trust account to provide financial support for family members in the future. Because the intent of the insurance policy is to provide for a possible future event, this type of asset may not provide an appropriate return to an account. In addition, the fiduciary's ability to transfer these assets outside of the trust account is limited because the governing documents require retention even if a fiduciary is of the opinion that an asset should not be retained. Therefore, fiduciaries should make every effort to obtain a retention letter from interested parties that provides specific direction to the fiduciary for the continued retention of the unique and special asset. While not a complete line of defense, the existence of retention letters, which should be renewed periodically, ensures that clients and beneficiaries are aware of and understand the risks associated with retaining a unique and special asset in an account.

Another potential challenge with retaining unique and special assets in accounts is the risk that a fiduciary will not be able to adhere to the prudent investor rule, which, in part, requires fiduciaries to diversify an account's investments. When a unique and special asset represents a significant portion of the account's holdings, the account will not be diversified. As a result, the administration of such an account could be criticized if a fiduciary does not appropriately document the permissibility of the holding and conduct appropriate periodic account reviews.

## Risks Posed by Individual Unique and Special Assets

Unique and special assets may pose risks to an account that must be managed by the fiduciary. For example, real estate, mineral interests, and timberland pose environmental risks. Therefore, these types of assets may require studies to ensure environmental factors do not contribute to a decline in the value of the asset. The fiduciary must also manage the reverse

and ensure that an asset does not cause environmental harm that may expose the account to liability, resulting in remediating damages. In certain instances, such as in the management of working mineral interests, the fiduciary can obtain environmental liability insurance for the account to protect against the risk of an asset causing harm to the environment.

Certain unique and special assets may require special safe-keeping procedures for fiduciaries to guard against deterioration in the asset's value or theft. For example, personal items must be held under dual control to prevent one party from misappropriating the asset. Certain assets, such as artworks or collectibles, may require temperature-controlled storage

“ The first and foremost challenge fiduciaries may face is that the retention of unique or special assets may not align with the organization's basic fiduciary duties. ”

facilities to preserve their condition. In addition, for tangible assets that are physically held outside of the organization's premises, the fiduciary must conduct periodic visits to confirm the asset's condition and to reassess its value.

Other unique and special assets held in fiduciary accounts, such as closely held businesses, have limited marketability. Given that these interests tend to be held among a few individuals, the ability to liquidate such an interest is limited, especially for a minority interest or if contentious situations arise. In addition, with a closely held business, the fiduciary is required to complete financial evaluations periodically to assess the appropriateness of retaining the asset given the account's overall investment objective. Also, depending on the percentage of the business that is held in the account, the fiduciary may have to attend the company's board meetings or appoint an officer of the trust department or trust company as a voting member to the board of the closely held company to protect the interest of the trust. The fiduciary's policies on the management of unique and special assets held in accounts should address the level of its participation in the management of closely held companies.

## Additional Risks to Consider

Unique and special assets can also increase the fiduciary's operational, legal, and reputational risks. Operational risk is increased because the organization will have to retain staff who have the specialized expertise necessary to administer and manage unique and special assets, which may require the completion of asset evaluations, financial analyses, or industry certifications. The fiduciary or a third party should perform regular asset valuations to confirm the value of an account's assets and assist with the regulatory reporting of asset values. Further, fiduciaries should implement appropriate safeguards to preserve and protect an account's assets.

The organization's legal risk increases since it must comply with all fiduciary duties and laws as well as with an account's governing documents that outline the procedures for administering unique and special assets. Any deviation from legal obligations places a fiduciary at risk for potential liability if challenged by an account holder, beneficiary, or remainderman. As a result, an organization's legal fees can increase quickly when an organization has to defend itself from actual or potential claims of mismanagement.

Mismanagement of an account, including an account with unique and special assets, can negatively impact an organization's reputation. Therefore, the ability of staff to appropriately manage and administer these assets is essential to the organization's reputation, and failure to do so may result in the loss of current and potential clients and referrals. The organization's reputation is also at risk if a third party retained by the organization to oversee the assets fails to exercise its duties in accordance with the appropriate standards of care.

## Examiners' Expectations of a Fiduciary's Administration of Unique and Special Assets

During fiduciary examinations, examiners will review a fiduciary's oversight of unique and special assets.<sup>1</sup> The examiners will rely on the board of directors, which is ultimately responsible

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<sup>1</sup> See the Office of the Comptroller of the Currency Bulletin 2012-22, "Unique and Hard-to-Value Assets," available at <http://ow.ly/ZiXBJ>. Although this bulletin directly applies to national banks and federal savings associations, Federal Reserve fiduciary examiners reference this bulletin during their reviews, as it provides an extensive overview of unique and special assets and supervisory expectations.

# Less Risky Business: An Overview of a New Cybersecurity Assessment Tool

by Brian Bettle, Senior Examiner, Supervision and Regulation, Federal Reserve Bank of Atlanta

Over the years, financial institutions have increased their level of maturity with respect to business continuity and disaster recovery so that they may better manage environmental events, such as tornadoes, earthquakes, and hurricanes, that could affect their organizations. Managing through environmental events has become part of the normal course of business for many financial institutions, especially those in regions prone to these events. As a result, these financial institutions have very robust business continuity and disaster recovery plans. The plans are tested annually and are often activated when severe weather events are anticipated. Financial institutions operating in this type of environment have learned to adapt quickly and resume operations with minimal impact on customers after the weather-related event is over.

Since cybersecurity is becoming one of the greatest risks that can affect financial institutions today, these organizations need to react similarly to this growing threat by enhancing their cybersecurity maturity levels. Since the 2012 distributed denial-of-service attacks,<sup>1</sup> financial institutions have placed greater emphasis on improving security and combating potential incidents. Financial institutions have increased their information technology (IT) security budgets and invested in systems and personnel to address these risks. Despite these efforts, financial institutions are unsure whether their actions are sufficient and whether their preparations and ongoing security programs adequately address the risks.

Members of the Federal Financial Institutions Examination Council (FFIEC)<sup>2</sup> have also experienced challenges in assessing whether financial institutions' actions are appropriate and sufficient. Therefore, the organization developed a cybersecurity assessment tool (CAT) that is designed to help financial

institutions determine their inherent level of cybersecurity risk and then assess the appropriateness of their cybersecurity control environments given their identified risks. This tool is based on the National Institute of Standards and Technology (NIST) Cybersecurity Framework and existing regulatory guidance. The CAT is not a silver bullet to address all cybersecurity concerns. However, the tool should help an institution identify control gaps in its operating environment based on its inherent risk profiles. The supervisory expectation is that an institution will assess its cybersecurity risk; the CAT provides one option to perform this assessment.

## Implementation

On July 2, 2015, the Board of Governors issued Supervision and Regulation (SR) letter 15-9, "FFIEC Cybersecurity Assessment Tool for Chief Executive Officers and Boards of Directors."<sup>3</sup> The letter includes information on the CAT. The Federal Reserve plans to use these self-assessments in the review of cybersecurity preparedness during the IT and safety-and-soundness examinations and inspections. As part of the examination process, examiners will assess a firm's self-assessment of cybersecurity risk. The use of the CAT remains voluntary; however, firms are expected to perform a cybersecurity assessment using either the CAT or an industry-accepted practice, such as the NIST Cybersecurity Framework or ISO 27001.

## Establishing an Inherent Risk Profile

The first portion of the CAT process focuses on an institution's current inherent risk environment. The tool helps determine the level of cybersecurity risk based on a firm's activities, services, and products. The CAT measures five inherent risk categories.

- 1. Technologies and Connection Type.** The assessment begins with measuring the inherent risk of technologies

<sup>1</sup> In the fall of 2012, an unprecedented amount of traffic was directed at the websites of several major banks, causing interruptions, slowdowns, or the suspension of services.

<sup>2</sup> FFIEC membership includes 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, the Consumer Financial Protection Bureau, and the State Liaison Committee.

<sup>3</sup> See SR letter 15-9, "FFIEC Cybersecurity Assessment Tool for Chief Executive Officers and Boards of Directors," available at [www.federalreserve.gov/bankinforeg/srletters/sr1509.htm](http://www.federalreserve.gov/bankinforeg/srletters/sr1509.htm).

and connections. Certain connections may pose additional cyber-related risks. The risk profile may be adjusted depending on the number of Internet service providers and third-party connections used and whether they are in-house or outsourced. The volume of unsecured connections and the use of end-of-life systems, cloud services, and personal devices can also increase the risk at a firm.

2. **Delivery Channels.** Numerous delivery channels for products and services may pose a higher level of inherent risk. The increase in the risk level depends on the nature of the specific product or service offered and is elevated as the variety and number of delivery channels increase.
3. **Online Mobile Products and Technology Services.** The use of online and mobile delivery channels can also influence the inherent risk levels. The greater the number of online and mobile delivery channels and the use of smart automated teller machines (ATMs) — those with touch screens that provide onscreen directions through the entire transaction — the greater the risks. Expanding the number of delivery channels also presents cyber-related risks due to the additional paths that an attacker can use to exploit a target. A financial institution's mobile or online services may also heighten risk, particularly if a funds transfer component is available.
4. **Organizational Characteristics.** This category can also raise the inherent cybersecurity risk at a firm. In some instances, data breaches occurred after a merger because of a lack of control over the newly consolidated environment. In the postmerger environment, compiling a comprehensive inventory of hardware can be challenging. An overlooked server can go without security updates for a significant amount of time, which opens the door to a data breach. Also, in a postmerger environment, changes in staffing or the use of contractors can lead to excessive user-access privileges being granted and then overlooked. Lastly, organizational changes can also affect morale, which may increase the potential of an insider security threat.
5. **External Threats.** The last inherent risk factor comes from external threats. A large multinational financial institution will have a higher risk profile than a small community bank in a rural setting. Both firms will always face the potential for a cyberattack. However, a small community bank may be unknown outside of its market area and face fewer threats. Although community banks may not be well known internationally, they remain at risk because they are often perceived to have fewer cybersecurity controls in place.

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## FEDLINKS

*Connecting Policy with Practice*

*FedLinks: Connecting Policy with Practice* is a single-topic bulletin prepared specifically for community banks and holding companies with total assets of \$10 billion or less. Each bulletin provides an overview of a key supervisory topic; explains how supervisory staff members typically address that topic; highlights related policies and guidance, if applicable; and discusses examination expectations as appropriate at community banks. *FedLinks* is not intended to establish new supervisory expectations beyond what is already set forth in existing policies or guidance but rather to connect policy with practice.

These bulletins can be found online at [www.cbefrs.org/fedlinks](http://www.cbefrs.org/fedlinks).

By subscribing to *FedLinks* bulletins at [www.cbefrs.org/subscribe](http://www.cbefrs.org/subscribe), you will receive an e-mail notification when new bulletins become available.

# The Federal Reserve's Discount Window: What It Is and How It Works

by Pam Hendry, Director, Credit and Risk Management, Federal Reserve Bank of Atlanta

Lending at the Federal Reserve's Discount Window<sup>1</sup> serves two primary functions: (1) as a backup source of liquidity that individual depository institutions can use when faced with temporary, unforeseen changes in their asset and liability structure and (2) as a complement to open market operations in achieving the target federal funds rate by making Federal Reserve balances available to depository institutions when the normal functioning of financial markets is disrupted.

Being prepared to borrow from the Discount Window can be an important component of a depository institution's planning for both strategic and contingency purposes. Depository institutions that do not envision using the Discount Window in the ordinary course of events are encouraged to execute the necessary documents for contingency purposes because a need for Discount Window credit could arise suddenly and unexpectedly.

This article provides basic information on the Discount Window,<sup>2</sup> including the types of borrowing programs available; interest rates; eligibility criteria; and borrowing arrangements, such as documentation, acceptable collateral, and collateral margins.

## Types of Borrowing Programs Available

### Primary Credit

Primary credit is available to generally sound depository institutions on a very short-term basis, typically overnight. Depository institutions are not required to seek alternative sources of funds before requesting occasional advances of primary credit. The Federal Reserve expects that depository institutions will use the Discount Window as a backup rather than as a regular source of funding, given the above-market pricing of primary credit.

<sup>1</sup> Much of the statutory framework that governs Discount Window lending is contained in section 10B of the Federal Reserve Act, as amended, available at [www.federalreserve.gov/aboutthefed/section10b.htm](http://www.federalreserve.gov/aboutthefed/section10b.htm). The programs and policies that implement the statutory framework are set forth in the Federal Reserve's Regulation A, available at [www.federalreserve.gov/bankinforeg/reglisting.htm](http://www.federalreserve.gov/bankinforeg/reglisting.htm).

<sup>2</sup> Detailed information on the Discount Window is available at [www.frbdiscountwindow.org](http://www.frbdiscountwindow.org).

Primary credit may be used for any purpose, including financing the sale of federal funds. The primary credit program complements open market operations in the implementation of monetary policy by making funds readily available at the primary credit rate when there is a temporary shortage of liquidity in the banking system, thus capping the actual federal funds rate at or close to the primary credit rate.

Reserve Banks ordinarily do not require depository institutions to provide reasons for requesting very short-term primary credit advances. Rather, borrowers are asked to provide only the minimum information necessary for the Reserve Bank to process a loan, which is usually the amount and term of the loan. If the pattern of borrowing or the nature of a particular borrowing request strongly indicates that a depository institution is not in generally sound financial condition, the lending Reserve Bank may seek additional information.

Primary credit may be extended for periods of up to a few weeks to small depository institutions in generally sound financial condition that are experiencing short-term funding difficulties or cannot obtain temporary funds in the market at reasonable terms. Large- and medium-sized depository institutions generally have access to market funds to meet their temporary funding needs. Longer term extensions of credit are subject to increased administration as determined by the lending Reserve Bank.

### Secondary Credit

Secondary credit may be available to depository institutions that are not eligible for primary credit. The secondary credit program entails a higher level of Reserve Bank administration and oversight than the primary credit program. This type of credit is also extended on a very short-term basis, typically overnight. However, in contrast to primary credit, there are restrictions on the uses of secondary credit. Secondary credit is available to meet backup liquidity needs when its use is consistent with helping a depository institution return to market funding sources or the orderly resolution of a troubled institution. Secondary credit may not be used to fund an expansion of the institution's assets.

## Seasonal Credit

The Federal Reserve’s seasonal credit program is designed to assist small depository institutions in managing liquidity needs that arise above their regular swings in loans and deposits caused by seasonal types of businesses such as construction, college, farming, resort, tourism, and municipal financing. A

U.S. branches and agencies of foreign banks that hold reserves are eligible to borrow under the same general terms and conditions that apply to domestic depository institutions. Foreign banks with more than one branch or agency operating in the United States may have access to the Discount Window in more than one Reserve Bank District. Any Discount Window

loan to those branches or agencies will be made by the Reserve Banks where the borrowing branches or agencies maintain accounts. Reserve Banks coordinate and monitor lending to such branches and agencies on a nationwide basis.

Bankers’ banks, corporate credit unions, and other financial institutions are not required to maintain reserves under the Board’s Regulation D and therefore do not have regular access to the Discount Window. However, the Board of Governors has determined that such institutions may obtain access to the Discount Window if they voluntarily maintain reserves.

**Table: Summary of Interest Rate Setting by Type of Borrower**

Lending Program	Eligible Borrowers	Setting of Interest Rate <sup>a</sup>
Primary credit	Depository institutions (DIs) in generally sound financial condition	Recommended by the boards of directors of the Reserve Banks and approved by the Board of Governors; currently 50 basis points above the top of the range for the FOMC’s target federal funds rate <sup>b</sup>
Secondary credit	DIs that do not qualify for primary credit	Spread above the primary credit rate, currently 50 basis points
Seasonal credit	Smaller DIs with a regular seasonal need for funds	Average of the effective federal funds rate and the three-month CD rate, typically resulting in a rate close to the federal funds rate target

<sup>a</sup>Current and historical primary, secondary, and seasonal rates are available at [www.frbdiscountwindow.org/en/Pages/Discount-Rates/Current-Discount-Rates.aspx](http://www.frbdiscountwindow.org/en/Pages/Discount-Rates/Current-Discount-Rates.aspx).

<sup>b</sup>Rates for all programs are proposed by the board of directors of the lending Reserve Bank and approved by the Board of Governors of the Federal Reserve System.

depository institution may qualify for up to nine months of seasonal credit during the calendar year to assist in meeting the needs of the local communities where it operates.

## Interest Rates on Primary, Secondary, and Seasonal Credit

Reserve Banks’ boards of directors establish the primary credit rate at least every two weeks, subject to review and determination by the Board of Governors. The interest rates applied to primary and secondary credit change periodically to complement changes in the Federal Open Market Committee’s (FOMC) target for the federal funds rate and to achieve broad monetary policy goals (see the table above). The interest rate applied to seasonal credit is a floating rate based on market rates.

## Eligibility to Borrow

By law, depository institutions that maintain reservable transaction accounts or nonpersonal time deposits (as defined in the Board’s Regulation D) may establish borrowing privileges at the Discount Window. Eligibility to borrow is not dependent on or related to the use of Federal Reserve priced services.

(Refer to Regulation D for more details.<sup>3</sup>)

## Eligibility for the Credit Programs

### Primary Credit

A depository institution must be in generally sound financial condition, as determined by its Reserve Bank, to qualify for primary credit. A Reserve Bank reviews a depository institution’s condition on an ongoing basis using supervisory ratings and capitalization data. Supplementary information, when available, may also be used. Criteria used in determining whether an institution is in generally sound financial condition include but are not limited to:

- An institution assigned a composite CAMELS rating of 1, 2, or 3 (or SOSA 1 or 2 and ROCA 1, 2, or 3) that is at least adequately capitalized is eligible for primary credit unless supplementary information indicates that the

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<sup>3</sup> See [www.federalreserve.gov/bankinfo/reg/reglisting.htm](http://www.federalreserve.gov/bankinfo/reg/reglisting.htm) for more information about Regulation D.

# Preparing Now to Weather Conditions Ahead *continued from page 1*

While regulators and bankers have learned important lessons from the previous crisis — especially the importance of having robust risk management — we must continue to monitor evolving financial trends and portfolio concentrations. This will help us better identify emerging risks and negative trends in the credit cycle. We should also be mindful to take necessary actions now, ahead of these risks, before they become credit losses.

## Current Performance Trends

Industry banking performance continues to recover after the Great Recession. National unemployment trends have returned to precrisis levels, and house prices have increased in most regions of the country. Problem banking institutions (those with composite CAMELS ratings of 4 or 5) have fallen 79 percent since 2010. The Third District (which covers parts of the Mid-Atlantic region) generally fared better than the nation during the crisis; however, postcrisis loan performance has been lagging the national pace. Loan performance metrics within the Third District did not deteriorate as much as they did across the nation, so the recovery in the Third District was not as well recognized when compared with national improvements.

Financial performance data for Third District institutions with less than \$10 billion in assets show clear improvement, with median capital levels that have increased 4.7 percent year over year and 7 percent year over year for the nation since 2010.<sup>1</sup> Third District bank earnings, as measured by the median return on average assets, have increased by 26.7 percent compared with 41.5 percent for the nation over the same period. Further, since 2009, Third District banks have shown consistent improvement in asset-quality metrics.

## Sources of Uncertainty

While these market trends are encouraging, there are indications of rising pressure on bank balance sheets, increased operational risk, and volatile capital market trends. Earnings have stabilized since the crisis but remain compressed by historically low net interest margins.

Additionally, there are sources of uncertainty that raise concerns for both community bankers and regulators.

Community bankers have voiced concerns over the continued viability of the community bank model. Low interest rates, competition from nonbank sources, and rising compliance costs have affected earnings and led banks to consider mergers and acquisitions in order to find economies of scale. While loan performance metrics, such as charge-off rates, delinquency levels, and nonperforming asset ratios, have almost returned to precrisis levels, asset concentration levels appear to be increasing and underwriting standards appear to be easing.

The substantial rise in commercial real estate (CRE) credit concentrations is a particular area that bank regulators are monitoring. A national commercial property price index from Moody's Investors Service and Real Capital Analytics rose 12.7 percent in 2015, which is 17.3 percent above the precrisis peak.<sup>2</sup> Banks have increased their CRE credit concentrations nationwide. As of year-end 2015, 415 community banks, or 8 percent, that meet the regulatory CRE or construction and land development (CLD) concentration levels as discussed in Supervision and Regulation (SR) letter 07-1 were in operation.<sup>3</sup> Multifamily credit exposures have also increased, with a growth rate that has outpaced many other asset categories, including CLD loans, commercial and industrial loans, and nonfarm nonresidential lending.

Bankers also need to be aware that the volatility in commodity prices can adversely impact business sectors dependent on a particular commodity. For example, the Federal Reserve Bank of Philadelphia's state coincident index,<sup>4</sup> which mea-

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<sup>2</sup> Serena Ng, "Warning Light Flashes for the Commercial Property Boom," *Wall Street Journal*, February 16, 2016.

<sup>3</sup> See SR letter 07-1, "Interagency Guidance on Concentrations in Commercial Real Estate," available at [www.federalreserve.gov/boarddocs/srletters/2007/SR0701.htm](http://www.federalreserve.gov/boarddocs/srletters/2007/SR0701.htm).

<sup>4</sup> See [www.philadelphiafed.org/research-and-data/regional-economy/indexes/coincident](http://www.philadelphiafed.org/research-and-data/regional-economy/indexes/coincident) for more information about the Philadelphia Fed's coincident indexes.

<sup>1</sup> Data were obtained from the National Information Center database.

asures factors such as employment, hours worked in manufacturing, and the change in state gross domestic product growth, shows that historically low oil prices are weighing heavily on the economies of Alaska, Louisiana, North Dakota, Oklahoma, and Wyoming because of their extensive energy reserves and/or oil and gas refining facilities. Similarly, in 2016, low oil prices impacted the earnings of banks with exposure to the energy sector, as noncurrent loans in the oil and gas industry rose sharply.

### Applying Lessons Learned from the Last Storm

Against this backdrop, it is a good idea for bankers and bank regulators to take a step back and review the hard-learned lessons from the last storm. For instance, financial institutions, particularly community banks, should pay attention to lending and risk management fundamentals. Community banks that fared well during the crisis focused on the traditional community bank model that emphasized relationship lending tempered by strong credit standards, a robust understanding of products and markets, and an active board of directors that provided oversight.

In the Great Recession, we learned the difficult lesson of not paying full attention to the fundamentals of banking and risk management. Both bankers and bank regulators recognize that strong underwriting practices and well-established risk management processes were central to a bank's success in weathering the Great Recession. Further, a bank needs a capital buffer appropriate for its risk profile. These actions need to be instituted during relatively benign economic periods so that a bank has a solid foundation to better insulate itself from potential economic downturns and adverse credit cycles. At the same time, a bank needs to thoughtfully assess the amount of risk in its portfolios and ensure that it has the proper tools, management information system reporting, and qualified personnel to face the challenges of the next storm.

Now during the balmy days of summer is the time for bankers and regulators to prepare for winter. Regulators should listen carefully to bankers and other industry experts to glean information that may not yet be present in early warning risk models and examination findings. By taking a thorough and principled approach to bank supervision that includes both quantitative and qualitative analysis of bank practices, risk governance, management, and mitigation, regulators will be able to identify and recommend actions to address these risks at supervised institutions.

Recent interagency guidance shows that bank regulators are watching trends and providing sound direction. In 2015, the Federal Reserve System issued SR letter 15-17 to address the substantial growth in CRE credit concentrations and the easing of underwriting standards.<sup>5</sup> The guidance was designed to remind financial institutions to maintain underwriting discipline and conduct prudent risk management practices for CRE lending activity.

Similarly, in 2013, the agencies issued SR letter 13-3, which provided interagency guidance on safe-and-sound leveraged lending activities.<sup>6</sup> The guidance emphasizes the importance of transaction controls in the distribution pipeline and underwriting standards that are commensurate with an institution's risk appetite. Risk management and risk reporting go hand in hand with this, as higher risk credits require diligent monitoring and provisioning. The best defense from a risk standpoint is to originate loans with a sound business plan, a sustainable capital structure, and a borrower capacity for repayment.

### Final Thoughts

Preparation is the key to being ready for the next negative turn in the credit cycle. The steps we take now will determine how well we weather the conditions ahead. Although we are unable to predict the next storm, we can agree that some level of vigilance and preparation is necessary. In addition, it's important to pay attention to the fundamentals, such as capital planning, strong underwriting standards, and appropriate provisioning, especially as the banking industry looks to continue rebuilding capital and earnings. Collectively, we can begin to prepare to meet the challenges of the next storm. ■

*The author would like to thank Lincy Chacko, Christopher Henderson, and Christopher Hahne of the Federal Reserve Bank of Philadelphia for their contributions to this article.*

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<sup>5</sup> See SR letter 15-17, "Interagency Statement on Prudent Risk Management for Commercial Real Estate Lending," available at [www.federalreserve.gov/bankinfo/srletters/sr1517.htm](http://www.federalreserve.gov/bankinfo/srletters/sr1517.htm).

<sup>6</sup> See SR letter 13-3, "Interagency Guidance on Leveraged Lending," available at [www.federalreserve.gov/bankinfo/srletters/sr1303.htm](http://www.federalreserve.gov/bankinfo/srletters/sr1303.htm).

# Helpful Hints When Filing an Application with the Federal Reserve

*continued from page 3*

community banking organizations that typically do not file applications on a frequent basis or are contemplating a novel proposal. Applicants have the opportunity to receive feedback from Federal Reserve staff on potential issues related to an application proposal. Prefilings can include inquiries about a specific aspect of a proposal, a potential issue, or presentations outlining the specifics of the proposal. Prefilings may also include draft documents such as shareholder agreements, purchase agreements, or offering documents. An applicant may ask questions regarding the type of filing required, if any; the individuals or entities that would need to join the filing; and whether an entity would be considered to be a “company” or have “control” under the Bank Holding Company Act or the Home Owners’ Loan Act.

For a prefiling, the Federal Reserve staff review is targeted to the specific request for feedback and is not intended to resolve all issues or concerns related to a possible future application or notice or be predictive of the final outcome. Furthermore, the Federal Reserve staff’s prefiling evaluation is not part of the formal review period for applications outlined in relevant statutes and regulations.

Banking organizations should submit prefilings to the appropriate Reserve Bank or through E-Apps. The Federal Reserve anticipates reviewing prefiling and submitted information regarding a particular proposal for no more than 60 days. At the conclusion of the review period, a prefiler wishing to pursue a proposal or a prefiler who has been informed that a proposal requires a filing is encouraged to submit a final application. The final filing should stand on its own and address any issues raised during the prefiling review. The applicant should provide all pertinent documents in the final filing. An applicant’s final submission generally is expected to be more quickly reviewed and acted upon when previously identified issues or concerns are fully addressed.

## Interagency Statement on Restrictions on Conversions of Troubled Banks

In 2012, the Federal Reserve issued SR letter 12-16/CA letter 12-12, which provides guidance for implementation of section 612 of the Dodd–Frank Act, concerning certain charter conversions.<sup>9</sup> Section 612 places restrictions on certain charter

conversions and generally prohibits charter conversions while an institution is subject to a formal enforcement order issued by or a memorandum of understanding entered into with its current federal banking agency or state bank supervisor with respect to a “significant supervisory matter” (collectively referred to as a “significant enforcement action”).

The statute contains an exception to the prohibition that permits approval of a charter conversion if certain conditions are met, including that the federal banking agency or state banking supervisor that issued the significant enforcement action does not object to the conversion. In addition, section 612 requires that, at the time an insured depository institution files a conversion application with the prospective chartering authority, the institution must also send a copy of the conversion application to both its current federal banking agency and its prospective federal banking agency.

## Branching by Institutions in Less-Than-Satisfactory Condition

In 2013, the Federal Reserve issued SR letter 13-7/CA letter 13-4, which clarifies the Federal Reserve’s policy concerning the application process for a state member bank in less-than-satisfactory condition to establish a de novo branch.<sup>10</sup> The letter describes the circumstances under which a state member bank may be permitted to establish a branch on a de novo basis if it or its parent holding company is in less-than-satisfactory condition. Although the letter explains the criteria for the establishment of a de novo branch, a banking organization’s proposal must be consistent with general safety-and-soundness standards and adhere to the Federal Reserve’s application process.

A state member bank in less-than-satisfactory condition (see the SR letter for definition) or that has a less-than-satisfactory record of consumer compliance or performance under the

<sup>9</sup> See SR letter 12-16/CA letter 12-12, “Interagency Statement on Restrictions on Conversions of Troubled Banks,” available at [www.federalreserve.gov/bankinforeg/srletters/sr1216.htm](http://www.federalreserve.gov/bankinforeg/srletters/sr1216.htm).

<sup>10</sup> See SR letter 13-7/CA letter 13-4, “State Member Bank Branching Considerations,” available at [www.federalreserve.gov/bankinforeg/srletters/sr1307.htm](http://www.federalreserve.gov/bankinforeg/srletters/sr1307.htm).

Community Reinvestment Act (CRA) generally should not pursue expansionary proposals and should focus on remediating identified supervisory issues. Expansionary transactions such as mergers and acquisitions require a significant amount of management's time and can distract an organization from restoring the holding company or bank to a safe and sound condition or establishing an effective consumer compliance program. However, the establishment of a limited number of de novo branches generally should not require a significant amount of time or distract management from addressing the organization's supervisory issues. Accordingly, the Federal Reserve will consider such proposals. However, the bank should be able to demonstrate that it can effectively plan and execute branch expansions; absent a history of successful de novo branching, the branching proposal should include an execution plan.

The letter provides de novo branching criteria considered by the Federal Reserve, which include:

- A well-defined rationale for branching that will not materially increase risk
- Satisfactory progress in remediating outstanding supervisory issues
- Stable or improving risk management and financial factors at the organization
- Strong or satisfactory capital
- Acceptable component supervisory ratings
- Branching limited to within, or contiguous to, the bank's existing market area

The letter also specifies quarterly and annual branching limits. Potential applicants should contact Reserve Bank applications staff before submitting an application.

### **Enhancing Transparency in the Federal Reserve's Applications Process**

In 2014, the Federal Reserve issued SR letter 14-2/CA letter 14-1, which provides a better understanding of the Federal Reserve's approach to applications that may not satisfy statutory requirements for approval of a proposal or otherwise raise supervisory or regulatory concerns.<sup>11</sup> Applicants are generally expected to resolve their outstanding substantive supervisory issues before submitting an application filing to the Federal

Reserve. Filers with proposals that present unique and novel issues are encouraged to use the prefiling process, as described earlier, to seek feedback on potential issues before submitting a formal filing.

The 2014 guidance notes common issues identified by the Federal Reserve that have resulted in filings being considered problematic such as:

- Applicants with less-than-satisfactory ratings or enforcement actions
- Financial factors such as inadequate capital, lack of holding company source of strength, or expansionary proposals funded by short-term debt
- Managerial factors such as proposed directors or managers with insufficient banking experience or negative background information or proposed principals with a lack of financial resources and integrity to meet their financial obligations
- Other factors, such as the organization's record regarding the Bank Secrecy Act, an inappropriate business plan, and consumer compliance and its CRA rating

Often, these issues are resolved by providing additional information or making changes to the proposal, resulting in the Federal Reserve System's ultimately approving or not objecting to the application. However, there are instances when substantive issues are not resolved during the application review process and staff recommends that the Board of Governors deny the proposal. In such cases, the Federal Reserve's general practice has been to inform the filer before taking a final action to provide the filer with the option to withdraw the filing. Typically, the filing is withdrawn, and the withdrawal is noted on the Federal Reserve's public H.2 Release.<sup>12</sup>

To further enhance transparency and provide better insight into the issues that could prevent the Federal Reserve from acting favorably on a proposal, the Federal Reserve publishes a semiannual report that provides pertinent information on applications filed with the Federal Reserve. The report includes statistics on the length of time to process various applications and the overall volume of approvals, denials, and withdrawals and provides the primary reasons for withdrawals.<sup>13</sup>

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<sup>11</sup> See SR letter 14-2/CA letter 14-1, "Enhancing Transparency in the Federal Reserve's Applications Process," available at [www.federalreserve.gov/bankinfo/srletters/sr1402.htm](http://www.federalreserve.gov/bankinfo/srletters/sr1402.htm).

<sup>12</sup> See [www.federalreserve.gov/releases/h2](http://www.federalreserve.gov/releases/h2).

<sup>13</sup> See [www.federalreserve.gov/bankinfo/semiannual-reports-banking-applications-activity.htm](http://www.federalreserve.gov/bankinfo/semiannual-reports-banking-applications-activity.htm).

## Name Check Process for Domestic and International Applications

In 2015, the Federal Reserve issued SR letter 15-8 that announced changes to the Federal Reserve's general name check process. These changes streamlined and simplified the process and thereby reduced the burden associated with the application process overall, particularly for community banking organizations.<sup>14</sup> The Federal Reserve reviews applications that may include changes to the ownership or composition of the board of directors or executive management of a banking organization. For many of these applications, the Federal Reserve's review includes an assessment of whether certain proposed

“Community bankers can contact their Reserve Bank's applications and supervision staff for more information about examinations related to a proposed membership or merger filing.”

shareholders and policymakers have the competence, experience, integrity, character, and financial resources to effectively lead a supervised financial institution in a safe and sound manner. Under certain circumstances, the Federal Reserve also requests background information about an individual or company involved in a proposal from other regulatory and investigative agencies.

## Examinations of Insured Depository Institutions Before Membership or Merger into a State Member Bank

In 2015, the Federal Reserve issued SR letter 15-11/CA letter 15-9, which explains the Federal Reserve's criteria for waiving or conducting premembership safety-and-soundness and consumer compliance examinations of insured depository institutions that are either (1) seeking to become state member banks or (2) merging with another institution when a state member bank would be the surviving entity.<sup>15</sup> Community bankers can contact their Reserve Bank's applications and supervision staff for more information about examinations related to a proposed membership or merger filing.

<sup>14</sup> See SR letter 15-8, "Name Check Process for Domestic and International Applications," available at [www.federalreserve.gov/bankinforeg/srletters/sr1508.htm](http://www.federalreserve.gov/bankinforeg/srletters/sr1508.htm).

<sup>15</sup> See SR letter 15-11/CA letter 15-9, "Examinations of Insured Depository Institutions Prior to Membership or Merger into a State Member Bank," available at [www.federalreserve.gov/bankinforeg/srletters/SR1511.htm](http://www.federalreserve.gov/bankinforeg/srletters/SR1511.htm).

## Supervisory Concerns Related to Shareholder Protection Arrangements

In 2015, the Federal Reserve issued SR letter 15-15, which explains supervisory concerns related to arrangements structured by bank and savings and loan holding companies (collectively, "holding companies") to protect the financial investments made by shareholders (collectively, "shareholder protection arrangements").<sup>16</sup> Such arrangements raise concerns because they can have negative implications on a holding company's capital or financial position or limit the holding company's ability to raise capital in the future. A holding company should be aware that the Federal Reserve

may object to a shareholder protection arrangement based on the facts and circumstances of the particular arrangement. Therefore, a holding company that is engaged in capital-raising efforts or is considering the implementation or modification of a shareholder protection arrangement should review this guidance to help ensure that supervisory concerns are addressed. When a proposal involves the raising of capital, community banking

organizations are encouraged to review this guidance and reach out to their Reserve Bank supervision and applications staff contacts with questions.

## Concluding Thoughts

Many resources are available to banking organizations to assist them when filing applications with the Federal Reserve. Banking organizations can use the E-Apps system to file applications electronically in a secure environment, which provides time and cost savings to an organization. Banking institutions can also use online resources to assist with completing application forms and publishing notices in newspaper publications for filings. Federal Reserve guidance related to filing applications is also available on the Federal Reserve's website and provides pertinent information for banking organizations to consider when contemplating the filing of an application. Finally, banking organizations are encouraged to contact Reserve Bank applications staff<sup>17</sup> to discuss any questions and issues related to filing an application or specific issues related to an application proposal. ■

<sup>16</sup> See SR letter 15-15, "Supervisory Concerns Related to Shareholder Protection Arrangements," available at [www.federalreserve.gov/bankinforeg/srletters/sr1515.htm](http://www.federalreserve.gov/bankinforeg/srletters/sr1515.htm).

<sup>17</sup> See [www.federalreserve.gov/bankinforeg/afi/bank\\_contacts.htm](http://www.federalreserve.gov/bankinforeg/afi/bank_contacts.htm).

# Examiners' View: A Fiduciary's Responsibilities for Unique and Special Assets *continued from page 5*

for the oversight of the organization's fiduciary activities, to address the challenges of administering and managing unique and special assets by implementing policies that require appropriate internal controls and risk management practices. Risk management practices should generally align with the value, number, and types of unique and special assets that the fiduciary manages and administers for its clients. For example, risk management efforts may include reporting to the appropriate committee and/or board of directors, completing internal audit reviews of accounts holding unique and special assets, and reviewing these assets during initial and periodic account review processes.

## **Policies and Procedures**

Policies and procedures should define the extent to which a fiduciary will accept unique and special assets in an account. Further, administrative practices and documentation standards should be defined within the policies and/or procedures. At a minimum, appropriate policies and procedures should:

- assign a board or senior management committee with the oversight responsibility for unique and special assets, whether as part of the review processes or otherwise;
- identify the types of assets that the fiduciary will or will not accept;
- establish account acceptance standards when unique and special assets are involved;
- require that these assets align with the fiduciary's investment policy standards;
- require insurance policies for certain assets;
- outline the frequency and methods for obtaining asset valuations; and
- identify how these assets are included in the fiduciary's administrative and investment reviews.

## **Pre-acceptance Reviews**

The fiduciary should ensure that the pre-acceptance account review process includes an evaluation of the unique and special assets in order to understand the nature, risks, and condition of these assets. For example, the pre-acceptance review process for real estate assets may include

environmental inspections to identify potential risks. During the pre-acceptance review, the fiduciary is expected to review the account's governing instrument to understand any explicit responsibilities and expectations for retaining a unique or special asset as well as to determine whether the fiduciary has the appropriate expertise to administer and manage the asset. The pre-acceptance review should clearly document the reasons for retention of any unique or special asset in the account.

A pre-acceptance review also identifies any potential risks associated with administering the specific asset. During the pre-acceptance review, a fiduciary has the opportunity to accept or decline the asset and/or account as well as to adjust the fees appropriately to reflect the risks associated with managing the account. For example, the risks associated with holding mineral interests in a fiduciary account differ depending on whether the asset is a royalty interest or a working mineral interest. In the former, the fiduciary is simply collecting payments, while in the latter the fiduciary has additional duties, including obtaining environmental insurance, performing physical inspections, and monitoring the operating agreement.

During examinations, examiners will evaluate whether the retention of a unique or special asset complies with the fiduciary's established policies and procedures as well as the account's governing instrument. Further, examiners will verify that the account file contains all documentation to support a fiduciary's decisions and actions in administering and managing the asset.

## **Expertise for Ongoing Management and Administration**

A fiduciary should retain experienced and knowledgeable staff to administer and manage accounts with unique and special assets. These individuals should have the knowledge and experience to manage a particular asset as well as the industry expertise for that asset. For example, account officers may be required to negotiate lease terms for mineral or gas assets, complete financial analyses for closely held businesses, or conduct periodic inspections of real estate properties. In certain instances, the individual may have to maintain an

industry certification to demonstrate this expertise. Industry certification programs also provide employees with educational and training opportunities to stay abreast of industry developments and asset management practices.

When a fiduciary recognizes additional experience is needed, the fiduciary may engage a qualified third-party service provider that possesses the expertise to assist with certain responsibilities and roles. As with any outsourcing or third-party arrangement, an organization needs to comply with supervisory guidance for the monitoring and periodic review of the relationship.<sup>2</sup>

### Account Review Processes

Unique and special assets should be evaluated during the initial and periodic reviews of fiduciary accounts, including investment and administrative reviews. Any fiduciary account, whether with traditional or unique assets, must have an established investment objective. In some cases, the retention of unique or special assets may go against the account's established investment objective. In these situations, the fiduciary needs to consider how to retain the asset(s) and still meet the investment objective. Therefore, during the annual investment review, a fiduciary needs to document the reasons for the continued retention of the unique and special asset.

Administrative reviews should consider the fiduciary's handling of the asset in the account and evaluate any concerns relating to the asset. The account review process should be customized to the type of asset involved and may include:

- **On-site visitations of real estate, mineral interests, or other tangible items.** Visitations allow a fiduciary to confirm an asset's existence and to evaluate any deferred maintenance or damage.
- **Valuations.** The nature and scope of valuations vary depending on the asset type. Valuations determine the market values for assets held, which in turn affect the account's asset value and the fiduciary's account manage-

ment fees. Valuations should be obtained periodically to ensure values remain current and useful.

- **Evaluations of insurance companies when an account holds an insurance product.** These reviews evaluate the insurance company's continued viability and financial condition and also confirm that the policy is still in place, coverage is adequate, and the account's policy premium is paid on time.

During an examination, examiners will assess the initial and annual account review processes, including whether unique or special assets are considered. Examiners will evaluate how unique or special assets within an account are considered during periodic administrative reviews and annual investment reviews. These account reviews should highlight, among other areas, the existence of the assets, actions taken with respect to the assets, any changes in the condition and value of the assets, client discussions about the account's holdings, and confirmation of continued asset retention.

### Internal Controls and Safekeeping

The organization's board of directors should adopt policies that require management to implement internal controls to ensure the safekeeping of unique and special assets. Assets held by the fiduciary should be properly safeguarded to prevent loss and damage by segregating administrative duties and requiring dual control over assets.

During examinations, examiners will evaluate vault procedures and assets maintained therein as well as review the results from the organization's own vault audits. Also, examiners will review operational functions to determine the existence of segregation of duties.

### Conclusion

The administration and management of unique and special assets are common activities in most institutions with trust and fiduciary powers. However, fiduciaries should understand that administering and managing these assets entail greater risks. Accordingly, these institutions should invest in the necessary staff resources and implement the appropriate risk management practices to mitigate the risks. During examinations, examiners will review all account assets, including unique and special assets, to ensure they are being appropriately administered and managed. ■

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<sup>2</sup> See, for example, Supervision and Regulation letter 13-19/Community Affairs letter 13-21, "Guidance on Managing Outsourcing Risk," available at [www.federalreserve.gov/bankinforeg/srletters/sr1319.htm](http://www.federalreserve.gov/bankinforeg/srletters/sr1319.htm).

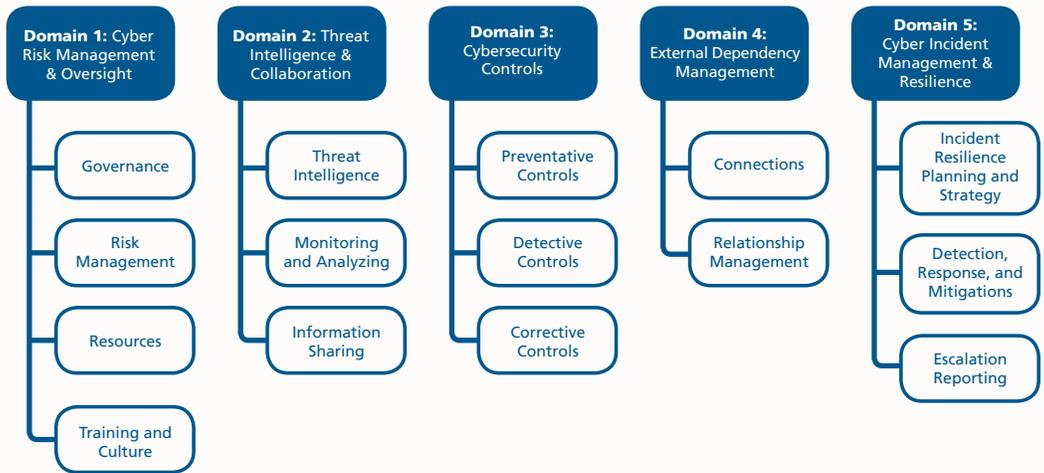
# Less Risky Business: An Overview of a New Cybersecurity Assessment Tool *continued from page 7*

## Considering Cybersecurity Maturity

The second portion of the CAT focuses on assessing the cybersecurity maturity of a firm’s control environment. This maturity assessment is based on the following five domains:

1. **Cyber Risk Management and Oversight** — the governance infrastructure that a firm has in place to oversee cyber-related risk
2. **Threat Intelligence and Collaboration** — the capability to monitor, acquire, analyze, and track the potential cyberthreat landscape and how it might affect the firm
3. **Cybersecurity Controls** — the measures put in place to deter and prevent a cyberattack
4. **External Dependency Management** — how well a firm manages its vendors, including an assessment of the robustness of its vendor management program

**Figure 1: The Five Domains and Their Assessment Factors**



Source: Federal Financial Institutions Examination Council, FFIEC Cybersecurity Assessment Tool: Overview for Chief Executive Officers and Boards of Directors, available at [www.ffiec.gov/pdf/cybersecurity/FFIEC\\_CAT\\_CEO\\_Board\\_Overview\\_June\\_2015\\_PDF1.pdf](http://www.ffiec.gov/pdf/cybersecurity/FFIEC_CAT_CEO_Board_Overview_June_2015_PDF1.pdf).

5. **Cyber Incident Management and Resilience** — the steps management takes to identify, prioritize, respond to, and mitigate cyberthreats and vulnerabilities when they occur

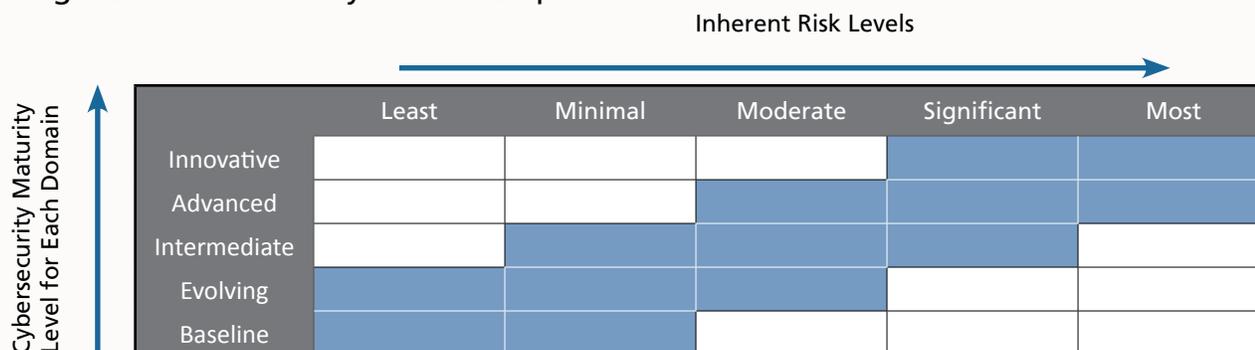
Figure 1 details the five domains and the assessment factors that inform these domains. For each assessment factor, the table below provides a set of declarative statements that describe activities that inform the level of maturity for each domain.

**Table: Maturity Levels Defined**

<b>Baseline</b>	Baseline maturity is characterized by minimum expectations required by law and regulations or recommended in supervisory guidance. This level includes compliance-driven objectives. Management has reviewed and evaluated guidance.
<b>Evolving</b>	Evolving maturity is characterized by additional formality of documented procedures and policies that are not already required. Risk-driven objectives are in place. Accountability for cybersecurity is formally assigned and broadened beyond protection of customer information to incorporate information assets and systems.
<b>Intermediate</b>	Intermediate maturity is characterized by detailed, formal processes. Controls are validated and consistent. Risk-management practices and analysis are integrated into business strategies.
<b>Advanced</b>	Advanced maturity is characterized by cybersecurity practices and analytics that are integrated across lines of business. The majority of risk-management processes are automated and include continuous process improvement. Accountability for risk decisions by frontline businesses is formally assigned.
<b>Innovative</b>	Innovative maturity is characterized by driving innovation in people, processes, and technology for the institution and the industry to manage cyber-related risks. This may entail developing new controls or new tools or creating new information-sharing groups. Real-time, predictive analytics are tied to automated responses.

Source: Federal Financial Institutions Examination Council, FFIEC User’s Guide, available at [www.ffiec.gov/pdf/cybersecurity/FFIEC\\_CAT\\_User\\_Guide\\_June\\_2015\\_PDF2\\_a.pdf](http://www.ffiec.gov/pdf/cybersecurity/FFIEC_CAT_User_Guide_June_2015_PDF2_a.pdf).

**Figure 2: Risk/Maturity Relationship**



Source: Federal Financial Institutions Examination Council, FFIEC User’s Guide, available at [www.ffiec.gov/pdf/cybersecurity/FFIEC\\_CAT\\_User\\_Guide\\_June\\_2015\\_PDF2\\_a.pdf](http://www.ffiec.gov/pdf/cybersecurity/FFIEC_CAT_User_Guide_June_2015_PDF2_a.pdf).

### Using the CAT

The CAT provides an institution’s management and board of directors with a repeatable and measurable process to determine whether the institution is applying sufficient resources and has the appropriate controls to manage cybersecurity risk. The CAT can help inform management and the board about the institution’s level of inherent cyber-related risk. The board may then consider this information and, given its risk appetite, determine the appropriate level of cybersecurity maturity needed to manage the institution’s particular risk environment. Not all financial institutions are expected to be at an innovative level of maturity. In fact, very few need to strive for this level. Figure 2 helps to define the appropriate levels of maturity based on the inherent cybersecurity risk identified.

After the board determines the desired maturity level, management can then measure the current processes against this level, identify any gaps, and take action to move the institution’s control environment toward the desired outcome.

### Concluding Thoughts

An institution may wish to compare its preparation for a cyberevent with the preparation that financial institutions regularly undertake in advance of a severe weather event. For example, the Federal Reserve examines many financial insti-

tutions and technology service providers in the southeastern United States for potential risks arising from a hurricane. As a result, these financial institutions have very robust business continuity and disaster recovery plans. Plans are tested annually and are often activated during severe weather events. Given this operating environment, these financial institutions have learned to adapt quickly and resume operations with minimal impact on customers in the aftermath of a weather event. Therefore, financial institutions across the United States should seek to maintain a cybersecurity maturity consistent with their inherent risk profile. Firms should assume that it is only a matter of time before they experience a cyberevent. In the ideal state of maturity, when a cyberevent happens, an institution will be prepared to react quickly, minimize impact, and resume operations as soon as possible. The CAT is a good first step toward moving the financial industry to this state of maturity.

In the future, the FFIEC will update the tool and the *IT Examination Handbook* based on the cybersecurity threat landscape. Additional information on the CAT and improving cybersecurity risk management is available.<sup>4</sup> ■

<sup>4</sup> See [www.ffiec.gov/cyberassessmenttool.htm](http://www.ffiec.gov/cyberassessmenttool.htm).

# The Federal Reserve's Discount Window: What It Is and How It Works *continued from page 9*

institution is not generally sound.<sup>4</sup>

- Institutions assigned a composite CAMELS rating of 4 (or SOSA 1 or 2 and ROCA 4 or 5) are not eligible for primary credit unless an ongoing examination or other supplementary information indicates that the institution is at least adequately capitalized and that its condition has improved sufficiently to be deemed generally sound by its Reserve Bank.
- Institutions assigned a composite CAMELS rating of 5 (or SOSA 3 regardless of ROCA) are not eligible for primary credit.

## Secondary Credit

Depository institutions that do not qualify for primary credit may be eligible for secondary credit when the use of such credit is consistent with a timely return to a reliance on market sources of funding or the orderly resolution of a troubled institution. A Reserve Bank must have sufficient information about a depository institution's financial condition and reasons for borrowing to ensure that an extension of secondary credit would be consistent with the purpose of the facility.

Note that there are restrictions on lending to undercapitalized depository institutions: The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA)<sup>5</sup> amended the Federal Reserve Act to restrain extensions of Federal Reserve credit to an FDIC-insured depository institution that has fallen below minimum capital standards or has received a composite CAMELS rating of 5 (or its equivalent) from its federal regulator. Such depository institutions may request secondary credit, but Federal Reserve lending to a depository institution that is undercapitalized, significantly undercapitalized, or rated a composite CAMELS 5 (or its equivalent) is generally limited to 60 days in any 120-day period. Ordinarily, a depository institution that is critically undercapitalized

may receive Discount Window credit only during the five-day period that begins on the day it becomes critically undercapitalized. Reserve Banks apply the same rules to depository institutions that are not insured by the FDIC but that are otherwise eligible to borrow at the Discount Window.

Any depository institution subject to one of the above-mentioned limits should maintain liquidity sufficient to keep its needs for Discount Window credit within appropriate bounds. If it appears that liquidity may prove inadequate, the depository institution should consult with its Reserve Bank as far in advance as possible. Such consultations may also include discussions of collateral arrangements needed to ensure the orderly continuation of Federal Reserve payment services.

## Seasonal Credit

To become eligible for seasonal credit, a depository institution must establish a seasonal qualification with its Reserve Bank. Eligible institutions are generally limited to those with deposits less than \$500 million. A depository institution that anticipates a possible need for seasonal credit is encouraged to contact its Reserve Bank to ascertain its eligibility and make arrangements in advance. Making arrangements does not obligate the institution to borrow.

Critically undercapitalized depository institutions are not eligible for seasonal credit. Undercapitalized or significantly undercapitalized depository institutions may be eligible but only after careful review of their condition and prospects; any lending to such institutions would be subject to statutory limitations established by the FDICIA as discussed earlier under Secondary Credit.

## Documentation Requirements for Borrowing

Any depository institution that expects to use the Discount Window should file the necessary lending agreements and corporate resolutions under the terms set forth in the Federal Reserve's lending agreement, Operating Circular No. 10. Operating Circular No. 10 documents include:

- **Letter of Agreement** — indicates a depository institution's acceptance of the terms and conditions in Operating Circular No. 10

<sup>4</sup> CAMELS stands for capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to market risk; SOSA stands for strength of support assessment; and ROCA stands for risk management, operational controls, compliance, and asset quality.

<sup>5</sup> See <https://www.fdic.gov/regulations/laws/rules/8000-2400.html> for more information about the act.

- **Authorizing Resolutions for Borrowers** — provides a depository institution’s authorization to borrow from and pledge assets to a Reserve Bank
- **Official OC-10 Authorization List** — a list of individuals or corporate titles of individuals who are authorized to borrow, pledge, or withdraw collateral as specified in the depository institution’s Authorizing Resolutions for Borrowers
- **Letter of Agreement to Correspondent Credit and Payment Agreement** — required only if the depository institution does not have a Federal Reserve account and a correspondent is selected to receive Discount Window advances and make payments on the depository institution’s behalf
- **Certificate** — provides the Reserve Bank with all the necessary information to make an effective Uniform Commercial Code-1 financing statement filing against the borrower. Note: This document may not be required; contact the respective Reserve Bank for more information.
- **Legal Opinions from Both Foreign and U.S. Outside Counsel** — are required from U.S. branches and agencies of foreign branches

## Collateral

All extensions of credit must be secured to the satisfaction of the lending Reserve Bank by collateral that is acceptable for that purpose. Most performing or investment-grade assets held by depository institutions are acceptable as collateral. Reserve Banks require a perfected security interest in all collateral pledged to secure Discount Window loans.

Reserve Bank staff can offer guidance on other types of collateral that may be acceptable. The following assets are most commonly pledged to secure Discount Window advances:

- Commercial, industrial, or agricultural loans
- Consumer loans
- Residential and commercial real estate loans
- Corporate bonds and money market instruments
- Obligations of U.S. government agencies and government-sponsored enterprises
- Asset-backed securities
- Collateralized mortgage obligations
- U.S. Treasury obligations
- State or political subdivision obligations

Assets accepted as collateral are assigned a lendable value (market value or an internally modeled fair market value

estimate multiplied by standard, published margins), with additional adjustments as deemed appropriate by the Reserve Bank. The financial condition of an institution may be considered when assigning values. Collateral margins are applied to the Federal Reserve’s fair market value estimate and are designed to account for risk characteristics of the pledged asset as well as the volatility of the value of the pledged asset over an estimated liquidation period.

Collateral margins for loans are as follows:

- The Federal Reserve uses reported cash flow characteristics and proxy credit spreads to calculate a fair market value estimate for each pledged loan. When individual loan cash flow characteristics are not available, the Federal Reserve uses general assumptions to estimate the fair market value of the loan pool.
- Margins for loan collateral are likewise based on reported cash flow characteristics. Margins are established based on the historical volatility of risk-free rates and proxy credit spreads, measured over typical liquidation periods.

Collateral margins for securities are as follows:

- Securities are typically valued daily using prices supplied by external vendors. Eligible securities for which a price cannot readily be obtained will be assigned an internally modeled fair market value estimate based on comparable securities, and they will receive the lowest margin for that asset type.
- Margins for securities are assigned based on asset type and duration. Margins are established based on the historical price volatility of each category, measured over typical liquidation periods.

Arrangements for pledging collateral should be reviewed with the Reserve Bank. Securities issued by the U.S. government and most securities issued by U.S. government agencies are held in an automated book-entry records system at the Federal Reserve. Other securities pledged as collateral generally are held by a depository or other agent through a custodian arrangement. Loans (customer notes) pledged as collateral typically are held by a custodian or under a borrower-in-custody arrangement. Physical securities, promissory notes, and other definitive assets may, however, be held on the Reserve Bank’s premises.

## Disclosure

In accordance with the provisions of the Dodd–Frank Wall Street Reform and Consumer Protection Act,<sup>6</sup> the Federal Reserve changed its practices with respect to disclosure of Discount Window lending information. Effective for Discount Window loans (primary, secondary, and seasonal credit) extended on or after July 21, 2010, the Federal Reserve will publicly disclose the following information, generally about two years after a Discount Window loan is extended to a depository institution:

- The name and identifying details of the depository institution
- The amount borrowed by the depository institution
- The interest rate paid by the depository institution
- Information identifying the types and amounts of collateral pledged in connection with any Discount Window loan. This disclosure requirement does not apply to collateral pledged by depository institutions that do not borrow.

This information will be released quarterly and may be disclosed with less than a two-year lag if the Chair of the Federal Reserve determines that it is in the public’s interest and that the disclosure would not harm the purpose or conduct of the Discount Window.

## Conclusion

Since the Federal Reserve System was established in 1913, Discount Window policies and programs have evolved in response to the changing needs of the economy and financial system. The primary credit program serves as a safety valve for ensuring adequate liquidity in the banking system and a backup source of short-term funds for generally sound depository institutions. Most depository institutions qualify

for primary credit. Minimal administration of and minimal restrictions on the use of funds make it a reliable short-term backup funding source.

Being prepared to borrow primary credit — similar to access to any backup liquidity facility — enhances a depository institution’s liquidity and eliminates the need to bid for marketplace funds when available funds are tight. Even if a depository institution does not envision using the Discount Window in the ordinary course of events, it is encouraged to execute the required documentation for contingency purposes because the need for Discount Window credit could arise suddenly and unexpectedly.

“ Being prepared to borrow primary credit — similar to access to any backup liquidity facility — enhances a depository institution’s liquidity and eliminates the need to bid for marketplace funds when available funds are tight. ”

Depository institutions that may be eligible for the seasonal credit program are encouraged to contact their Reserve Bank to determine eligibility. Institutions that experience fluctuations in deposits and loans frequently qualify for the seasonal lending program. This program provides funding of these seasonal needs so that the institution can carry fewer liquid assets during the rest of the year and make more funds available for local lending.

Depository institutions are encouraged to contact their Reserve Bank to discuss collateral requirements and arrangements before a need to borrow arises.<sup>7</sup> ■

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<sup>6</sup> The text of the Dodd–Frank Wall Street Reform and Consumer Protection Act is available at [www.gpo.gov/fdsys/pkg/BILLS-111hr4173enr/pdf/BILLS-111hr4173enr.pdf](http://www.gpo.gov/fdsys/pkg/BILLS-111hr4173enr/pdf/BILLS-111hr4173enr.pdf).

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<sup>7</sup> Discount Window contacts are available at [www.frbdiscountwindow.org/Pages/Select-Your-FRB.aspx](http://www.frbdiscountwindow.org/Pages/Select-Your-FRB.aspx).

**Chair Janet Yellen gave her semiannual Monetary Policy Report to Congress before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, on June 21, 2016.** The report is available at [www.federalreserve.gov/newsevents/testimony/yellen20160621a.htm](http://www.federalreserve.gov/newsevents/testimony/yellen20160621a.htm).

**Four federal financial institution regulatory agencies issued a joint statement on the new accounting standard on financial instruments — credit losses.** The agencies issued a joint statement regarding the new accounting standard, Accounting Standards Update (ASU) No. 2016-13, Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, issued by the Financial Accounting Standards Board. The joint statement provides initial supervisory views regarding the standard's implementation. The press release, which was issued on June 17, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160617b.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160617b.htm).

**The federal banking agencies issued host state loan-to-deposit ratios.** The federal banking agencies issued the host state loan-to-deposit ratios that they will use to determine compliance with section 109 of the Riegle–Neal Interstate Banking and Branching Efficiency Act of 1994. These ratios replace the prior year's ratios, which were released on June 29, 2015. In general, section 109 prohibits a bank from establishing or acquiring a branch or branches outside of its home state primarily for the purpose of deposit production. Section 109 also prohibits branches of banks controlled by out-of-state bank holding companies from operating primarily for the purpose of deposit production. The press release, which was issued on June 17, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160617c.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160617c.htm).

**The federal banking agencies released a list of distressed or underserved nonmetropolitan middle-income geographies.** The federal banking agencies announced the availability of the 2016 list of distressed or underserved nonmetropolitan middle-income geographies, where revitalization or stabilization activities are eligible to receive Community Reinvestment Act consideration as community development. The press release, which was issued on June 17, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160617a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160617a.htm).

**Chair Janet Yellen gave a speech at the World Affairs Council of Philadelphia in Philadelphia.** The June 6, 2016, speech “Current Conditions and the Outlook for the U.S. Economy” is available at [www.federalreserve.gov/newsevents/speech/yellen20160606a.htm](http://www.federalreserve.gov/newsevents/speech/yellen20160606a.htm).

**Agencies invited comment on a proposed rule to prohibit incentive-based pay that encourages inappropriate risk taking in financial institutions.** Six federal agencies invited public comment on a proposed rule to prohibit incentive-based compensation arrangements that encourage inappropriate risks at covered financial institutions. The proposed rules would apply to covered financial institutions with total assets of \$1 billion or more. The deadline for comments on the proposed rule, which was submitted for publication in the *Federal Register*, was July 22, 2016. The press release, which was issued on May 16, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160516a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160516a.htm).

**The Federal Reserve Board implemented new procedures for examiners to conduct off-site loan reviews for community and small regional banks.** State member banks and U.S. branches and agencies for foreign banking organizations with less than \$50 billion in total assets can opt to allow Federal Reserve examiners to review loan files off-site during both full-scope or target examinations as long as loan documents can be sent securely and with the required information. The Board is offering this option as part of its ongoing efforts to improve efficiency and provide burden reduction while maintaining quality supervision. The press release, which was issued on April 19, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160419a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160419a.htm).

**Federal financial institution regulatory agencies released guidance to issuing banks on applying Customer Identification Program (CIP) requirements to holders of prepaid cards.** The guidance clarifies the applicability of the CIP rule to prepaid cards issued by banks, savings associations, credit unions, and U.S. branches and agencies of foreign banks. The press release, which was issued on March 21, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160321a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160321a.htm).

**Agencies clarified expectations for the use of property evaluations.** The federal banking agencies issued an advisory

to clarify expectations for the use of property evaluations by banking institutions. The advisory responds to questions raised during outreach meetings held by the agencies last year pursuant to the Economic Growth and Regulatory Paperwork Reduction Act. The press release, which was issued on March 4, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160304a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160304a.htm).

**Federal banking agencies expanded the number of banks and savings associations qualifying for an 18-month examination cycle.** Federal banking agencies increased the number of small banks and savings associations eligible for an 18-month examination cycle rather than a 12-month cycle. Under the interim final rules, qualifying well-capitalized and well-managed banks and savings associations with less than \$1 billion in total assets may now be eligible for an 18-month examination cycle. Previously, firms with less than \$500 million in total assets could be eligible for the extended examination cycle. The examination cycle changes may also apply to qualifying well-capitalized and well-managed U.S. branches and agencies of foreign banks with less than \$1 billion in total assets. The changes are intended to reduce regulatory compliance costs for smaller institutions while still maintaining safety-and-soundness protections. The press release, which

was issued on February 19, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160219a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160219a.htm).

**The Federal Reserve Board issued an interim final rule that amends Regulation I to implement provisions of the Fixing America's Surface Transportation (FAST) Act.** The FAST Act reduced the dividend rate applicable to Reserve Bank depository institution stockholders with total assets of more than \$10 billion (large member banks) to the lesser of 6 percent or the most recent 10-year Treasury auction rate prior to the dividend payment. The dividend rate for other member banks remains at 6 percent. Reserve Banks typically pay dividends to member banks in June and December each year. The interim final rule also adjusts the treatment of accrued dividends when a Reserve Bank issues or cancels capital stock owned by a large member bank. The press release, which was issued on February 18, 2016, is available at [www.federalreserve.gov/newsevents/press/bcreg/20160218a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20160218a.htm).

**Chair Janet Yellen gave her semiannual Monetary Policy Report to Congress before the Committee on Financial Services, U.S. House of Representatives, on February 10, 2016.** The report is available at [www.federalreserve.gov/newsevents/testimony/yellen20160210a.htm](http://www.federalreserve.gov/newsevents/testimony/yellen20160210a.htm).

## Connect with Us

What banking topics concern you most? What aspects of the supervisory process or the rules and guidance that apply to community banks would you like to see clarified? What topics would you like to see covered in upcoming issues of *Community Banking Connections*?

With each issue of *Community Banking Connections*, we aim to highlight the supervisory and regulatory matters that affect you and your banking institution the most, providing examples from the field, explanations of supervisory policies and guidance, and more. We encourage you to contact us with any ideas for articles so that we can continue to provide you with topical and valuable information.

Please direct any comments and suggestions to [www.cbcrfs.org/feedback](http://www.cbcrfs.org/feedback).



## Supervision & Regulation (SR) & Consumer Affairs (CA) Letters

The following SR and CA letters that have been published since the last issue (and are listed by most current) apply to community banking organizations. Letters that contain confidential supervisory information are not included. All SR letters are available by year at [www.federalreserve.gov/bankinforeg/srletters/srletters.htm](http://www.federalreserve.gov/bankinforeg/srletters/srletters.htm) and by topic at [www.federalreserve.gov/bankinforeg/topics/topics.htm](http://www.federalreserve.gov/bankinforeg/topics/topics.htm). A complete list of CA letters can be found at [www.federalreserve.gov/bankinforeg/caletters/caletters.htm](http://www.federalreserve.gov/bankinforeg/caletters/caletters.htm).

**SR Letter 16-12**, “Interagency Guidance on the New Accounting Standard on Financial Instruments — Credit Losses”

**SR Letter 16-11**, “Supervisory Guidance for Assessing Risk Management at Supervised Institutions with Total Consolidated Assets Less Than \$50 Billion”

**SR Letter 16-10**, “*FFIEC Information Technology Examination Handbook* — Retail Payment Systems Booklet”

**SR Letter 16-9**, “Interactive Supervisory Guidance”

**SR Letter 16-8**, “Off-site Review of Loan Files”

**SR Letter 16-7**, “Interagency Guidance to Issuing Banks on Applying Customer Identification Program Requirements to Holders of Prepaid Access Cards”

**SR Letter 16-6**, “Updates to the Expanded Examination Cycle for Certain State Member Banks and U.S. Branches and Agencies of Foreign Banking Organizations”

**SR Letter 16-5**, “Interagency Advisory on the Use of Evaluations in Real Estate–Related Financial Transactions”

**SR Letter 16-4** “Relying on the Work of the Regulators of the Subsidiary Insured Depository Institution(s) of Bank Holding Companies and Savings and Loan Holding Companies with Total Consolidated Assets of Less Than \$50 Billion”

**CA Letter 16-5**, “Final Interagency Questions and Answers Regarding Community Reinvestment”

**CA Letter 16-4**, “Repeal of Regulation AA and Publication of Revised Examination Procedures for Section 5 of the Federal Trade Commission (FTC) Act”

**CA Letter 16-3**, “Revised Interagency Examination Procedures for Regulation P”

**CA Letter 16-2**, “Interagency Guidance Regarding Deposit Reconciliation Practices”

**CA Letter 16-1**, “Revised Interagency Examination Procedures for the Flood Disaster Protection Act”

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