Description of document:	Eight (8) Federal Housing Finance Agency (FHFA) Division of Enterprise Regulation (DER) Operating Procedures Bulletins (OPB), 2013-2016
Requested date:	30-July-2018
Release date:	14-September-2018
Posted date:	22-July-2019
Source of document:	FOIA Request Federal Housing Finance Agency 400 7th Street, SW 8th Floor Washington, D.C. 20219 Fax: 202-649-1073 Email: foia@fhfa.gov

From: Easter, Stacy <Stacy.Easter@fhfa.gov>
Sent: Fri, Sep 14, 2018 12:35 pm
Subject: FHFA FOIA No. 2018-FOIA-056
September 14, 2018

Re: FHFA FOIA No. 2018-FOIA-056

This letter is in response to your Freedom of Information Act (FOIA) request, dated July 29, 2018. Your request was received in the Federal Housing Finance Agency's (FHFA) FOIA office on July 30, 2018, and assigned FHFA FOIA request number 2018-FOIA-056. Your request was processed in accordance with the FOIA (5 U.S.C. § 552) and FHFA's FOIA regulation (12 CFR Part 1202).

You requested the following documents: 2014-DER-OPB-01, 2014-DER-OPB-02, 2013-DER-OPB-01, 2013-DER-OPB-03.1, 2013-DER-OPB-04, DER-OPB-01, DER-OPB-02, and 2016-OPB-DER-01."

A search of FHFA files and records located material responsive to your request. The FHFA has determined that the documents are releasable in their entirety. A copy of the accessible material is attached.

Your FOIA request is releasable to the public under subsequent FOIA requests. In responding to these requests, FHFA does not release personal information, such as home or email addresses and home or mobile telephone numbers which are protected from disclosure under FOIA Exemption 6 (5 U.S.C. § 552(b)(6)).

There are no fees associated with processing this request.

Please note that you may seek dispute resolution services from the Office of Government Information Services (OGIS) at the National Archives and Records Administration. OGIS can be reached at 8601 Adelphi Road – OGIS, College Park, Maryland 20740-6001; by email at ogis@nara.gov; by telephone at 202-741-5770 or toll free at 1-877-684-6448; or by facsimile at 202-741-5769.

If you have any questions regarding the processing of your request, please contact me directly at Stacy.Easter@fhfa.gov.

Sincerely,
Stacy J. Easter
FOIA/Privacy Officer
FOIA Public Liaison
Office of General Counsel | O G C
Federal Housing Finance Agency | F H F A
O: 202.649.3067 | Stacy.Easter@fhfa.gov

Federal Housing Finance Agency

January 27, 2014

DER OPERATING PROCEDURES BULLETIN

2014-DER-OPB-01

GUIDELINES FOR PREPARING SUPERVISORY PRODUCTS AND EXAMINATION WORKPAPERS

PURPOSE

This Division of Enterprise Regulation (DER) Operating Procedures Bulletin (OPB) expands upon the FHFA's Examination Manual and establishes DER-specific procedures and guidelines to examiners for creating and storing examination documentation to support supervisory products that relate the results, conclusions, findings and ratings of FHFA's safety and soundness examinations and other supervisory activities of Fannie Mae and Freddie Mac (the Enterprises).[1]

DER's primary supervisory product is the annual Report of Examination, but DER also produces supervisory correspondence, such as Conclusion Letters, Supervisory Letters, and Supervisory Expectation Letters to the Enterprises to communicate safety and soundness concerns throughout the annual examination cycle. Further, DER utilizes a variety of workpaper forms to document the findings and conclusions of the safety and soundness examinations. These workpapers, as defined by FHFA's Records Management Policy, 2013 File Plan for DER, include Conclusion Letters, Matters Requiring Attention, Request Letters, Supervisory Letters, Meeting Notes, Research, Analysis, and Planning Documents. These workpapers are Agency "records" for purposes of the Federal Records Act and are governed by FHFA's Records Management Policy. Examiners must be familiar with FHFA's records management policy and complete all required FHFA records management training.

This OPB applies to all supervisory activities conducted by DER and on behalf of DER that support the annual Report of Examination.

GENERAL GUIDELINES

1. Examiners are responsible for producing and storing work papers that support findings, conclusions, and supervisory ratings.
2. Examiners must file workpapers in the FHFA electronic recordkeeping system that the EIC has authorized for examination documentation.

[1] The scope of this OPB excludes examination documentation that facilitates and supports DER's Supervisory Planning process, which is addressed under 2013-DER-OPB-03.1, *Supervisory Planning Process.*

3. Prior to finalizing any findings, conclusions, or ratings and submitting to the Enterprises, Examination Managers should review supporting workpapers to ensure the record of examination is complete and stored appropriately.
4. In preparing workpapers, examiners should keep in mind that they must be prepared in a manner that provides a third-party with a clear understanding of the examination work performed, the examination findings, conclusions, and ratings reached, and any implications of the findings, conclusions, and ratings.
5. As examiners identify conclusions as well as potential safety and soundness concerns during the normal course of an examination, examiners are expected to document the following in the workpapers:
    a. Documentation to support the conclusion or potential concern;
    b. Discussion with DER management to determine if any potential concerns should be categorized as an examination finding in accordance with Advisory Bulletin, AB-2012-01; and,
    c. DER management's decision.
6. Examiners are encouraged to follow established naming conventions, as set forth in this OPB.
7. All outgoing letters to the Enterprises must have a correspondence control number in the subject line of the letter that is issued by the records management administrator. The format is as follows: FNM-DER-201X-XXX or FRE-DER-201X-XXX.[2]
8. Examiners are encouraged to use available templates created for DER's use to prepare work products and workpapers.

WORK PRODUCT AND WORKPAPER TYPES AND DESCRIPTIONS

The following list provides a description of work products and workpapers for use by examiners in conducting supervisory activities.

TYPE	DESCRIPTION
Request Letter	• Is required to notify the Enterprise of an upcoming targeted examination and requests specified information • Is not required for ongoing monitoring, but may be sent at EIC's discretion • Communicates the objective and scope of the supervisory activity • Provides an estimated fieldwork begin and end date • Provides FHFA contact information • Requests documentation to be delivered to the examiner(s) from the Enterprise by a specific due date • Requests the Enterprise to schedule follow-up meetings, including the

[2] Contact the Records Administrator to obtain the correspondence control number.

	examination kick-off meeting • If the targeted examination is being conducted by DSPS then the DSPS Deputy Director, or delegate, must approve the draft Request before EIC approval • Is addressed to the highest level of senior management responsible for the area under examination • The subject line of the Request Letter should include the same title of the supervisory activity as stated in the Supervisory Plan • CC's to: o Additional senior management from the business unit, if known o Chief Compliance Officer and/or regulatory liaison o Head of Internal Audit o Chief Enterprise Risk Officer
Procedures Document	• Is required for all targeted examinations and ongoing monitoring assignments • Ties the objective(s) of the supervisory activity to the Supervisory Plan and documents the steps taken to achieve the objective(s) • Examiners are encouraged to review applicable Examination Modules for the subject area(s) and the associated work programs when developing the Procedures Document. While the EIC has latitude in determining the scope and depth of an examination, the supervisory activities should be documented by using the 5-step Procedures Document (i.e., the Work Program) that accompanies each Examination Module. Those 5-steps include: 1. description of the scope of the supervisory activity 2. description of risks 3. steps to assess risk management 4. steps to complete any testing, as appropriate 5. summary of conclusions for all examination work, including any examination findings and areas requiring follow-up activities or monitoring • Examiners are required to complete a Procedures Document, adjust it as necessary, and file it in the required electronic recordkeeping system before fieldwork begins; or in the case of a targeted examination, at the time the Request Letter is sent • Any significant revisions made to the draft Procedures Document after the start of fieldwork (i.e., those that have a substantial impact on the hours needed to complete the work and/or materially change the scope and objective of the supervisory activity) should be based on risk, and the rationale must be approved by the Examination Manager • Provides the audit trail and the decision path for the work performed to support the conclusions and examination findings described in the Analysis Memorandum
Meeting Notes	• Summarizes the discussion points made during meetings between examiners and the Enterprises, or other key stakeholders involved in a supervisory activity • Is not meant to be a verbatim transcript of a discussion; should focus on the main points

	• The context should include enough detail for a reviewer to understand the specifics of the key points discussed and what the examiners learned • Should include the meeting date, attendee names and titles, purpose of the meeting, and a summary of the major topics discussed • If a handout is presented at the meeting, the Meeting Note should hyperlink or refer to an electronic copy of the handout • The summary portion of the Meeting Note should only contain factual information and should not contain examiner opinions or other information that was not discussed during the meeting • If the examiner wishes to includes his/her own opinions or takeaways in the Meeting Note, those points must be separated from the summary portion of the Meeting Note and clearly identified so that the opinions are not confused with the actual content discussed at the meeting • Generally, at least two examiners should attend each meeting and review the Meeting Note for accuracy and completeness of content • Examiners should exercise sound judgment when deciding whether meetings should be documented in a Meeting Note. If the content of the discussion supports the performance of a procedure step(s) of a supervisory activity, or is relied upon to support a decision or conclusion reached during the supervisory activity, then a Meeting Note is required • Examiners should complete the Meeting Note as soon as possible after the meeting while the discussion is still fresh
Report Notes	• Documents how reports (e.g., Enterprise-produced documents, authoritative literature) were used for analysis during the supervisory activity; if the reports are self-explanatory, there is no requirement to prepare a Report Note • Provides the evidence of the examiner's review of reports that are relied upon to conclude upon the objective of the supervisory activity • Summarizes the comments, questions, or conclusions reached during the review of the report • Provides a clear description of the source and scope of the report reviewed • The Report Note should include a hyperlink or a reference to the document
Enterprise Documents	• Includes documents submitted by the Enterprise during the course of the supervisory activity in response to DER's requests regardless of whether they are responsive to the request • If the documents are relevant and responsive to DER's requests, and support supervisory results, conclusions, findings or ratings, they must be filed in the electronic recordkeeping system as official agency records • If documents submitted by the Enterprise are not essential to the supervisory activity, then they do not need to be filed in the electronic recordkeeping systems as official agency records • Examiners should maintain an inventory of all documents received by the Enterprise during the course of the supervisory activity
Summary Memorandum	Results of all supervisory activity should be documented by either a Summary Memorandum or an Analysis Memorandum

	• May serve as an input to Risk Assessments and Business Profiles
	• May be used to support the content of a Supervisory Letter
	• May be used to report the results of (for example):
	  o Ongoing monitoring on a periodic basis
	  o Analysis, transaction testing, or a specific step from the Procedures Document
	  o Analysis of the Enterprise's remediation plan or closure package
	  o Analysis of IA's validation of the Enterprise's remediation activity to close an MRA
	  o A change in assigned staffing to a supervisory activity
	  o A specific procedure step or series of steps that will ultimately feed into and support the overall Analysis Memorandum
	  o A review of applicable criteria used to conclude on the objective
	  o The examiner's sampling methodology

Analysis Memorandum	• Is required for all Targeted Examinations and serves as the primary support for the Conclusion Letter • Is required for all Ongoing Monitoring assignments that result in the issuance of a Supervisory Letter containing examination findings • May be used to fully support Ongoing Monitoring even if there are no examination findings, if required by the Examination Manager • Provides the complete record of the work performed, findings, and conclusions • May serve as an input to the Risk Assessments and Business Profiles • Must appropriately link to the Procedures Document to show how the execution of the procedures resulted in the conclusions • Should include hyperlinks or references to supporting workpapers, such as: Request Letters, Enterprise Documents, Meeting Notes, Report Notes, Summary Memoranda • If the supervisory activity resulted in an examination finding, the Analysis Memorandum should contain a discussion that identifies the condition (what is wrong), the root cause (why it happened), the relevant criteria (what rule, policy, directive was not followed), and the effect (the impact of the condition) • Examination Managers must ensure examination findings are fully supported by workpapers and hyperlinked or referenced in the Analysis Memorandum before submitting to the EIC for approval • Must never be shared with the Enterprise

Supervisory Letter	• Unlike the Conclusion Letter, which is used only to conclude upon the results of a Targeted Examination, a Supervisory Letter is used to communicate to the Enterprises all other information; for example:
	  o Interim examination results
	  o Examination findings resulting from Ongoing Monitoring
	  o The EIC's expectations for Enterprise performance in a particular functional, program or business area (Supervisory Expectation Letter)
	  o The EIC's non-objection or rejection of the Enterprise's remediation plan for MRAs

	o The EIC's decision to close and no longer track an MRA o The EIC's decision to terminate supervisory activity or to rescind a previously issued MRA • Must be supported by an Analysis Memorandum if there are examination findings resulting from Ongoing Monitoring • If the supervisory activity was led by DSPS then the Supervisory Letter must be approved by the DSPS Deputy Director, or delegate, before it goes to the EIC and to the DER Deputy Director for their review
Conclusion Letter	• Is required for all targeted examinations • Is used to communicate examination findings (i.e., Matters Requiring Attention (MRAs), Violations, and Recommendations) and conclusions to the Enterprises • Draft Conclusion Letters must never be shared with the Enterprise • The addressee on the Conclusion Letter should be the same as the addressee on the Request Letter whenever possible to ensure the Enterprise is aware that the announced supervisory activity has been completed • Should use the same title of the supervisory activity as in the Request Letter • Should state substantially the same objective and scope that was formally communicated in the Request Letter for a targeted examination (or subsequent communication if significant changes to the objective and/or scope were approved by the EIC) • Each MRA should be numbered, titled, and referenced to the business area and Enterprise official responsible for follow-up • Must require a management response to be delivered to DER generally within 60 days from the date of the Conclusion Letter if MRAs are reported. The EIC can adjust the timeframe depending on the severity of the MRA. The content of the management response must include the following elements: o The Enterprise's plan for remediation o The name of the Enterprise official responsible for the remediation o The expected completion date of remediation • Must include the name and contact information of the points of contact (DER/DSPS) for the targeted examination • Recommendations should be numbered and titled. Management's response may be requested for a recommendation at the EIC's discretion • If the supervisory activity was led by DSPS then the Conclusion Letter must be approved by the DSPS Deputy Director, or delegate, before it goes to the EIC and the DER Deputy Director for their review • CC's to : o Key EVPs/SVPs from the business unit o Chief Compliance Officer o Head of Internal Audit o Chief Enterprise Risk Officer
Quality Control Memorandum	• Documents the results of an independent quality control review, as referenced in Supervisory Directive 2013-01 • Shows evidence that final examination findings, conclusions, and ratings

	underwent a quality control review Prepared by the Quality Control Reviewer; addressed to the EIC • Filed in the electronic recordkeeping system as part of the examination record
Report of Examination	• DER's primary work product that communicates to the board of directors, for each Enterprise, the cumulative results of supervisory activities conducted during the annual examination cycle • Identifies supervisory concerns and contains examination ratings that reflect FHFA's view of the regulated entity's financial safety and soundness and risk management practices • Provides the composite rating that is derived from the seven components of CAMELSO (i.e., capital, asset quality, management, earnings, liquidity, sensitivity to market risk, and operational risk) • Provides a component rating for each CAMELSO component • Requires a written response from the board of directors that acknowledges their review of the Report of Examination and affirms that correction actions is being taken, or will be taken, to resolve FHFA's supervisory concerns. • Signed by the EIC

WORKPAPER NAMING CONVENTIONS

1. In order to promote consistency in the way examiners document supervisory findings, conclusions and ratings, examiners are encouraged to use naming conventions for workpapers.
2. Using the workpaper types as indicated in the table above, examiners are encouraged to name their workpapers using these established prefixes:

Naming Convention Prefix	Type	Naming Convention Prefix	Type
ROE	Report of Examination	**ED**	Enterprise Document
RL	Request Letter	**SM**	Summary Memorandum
PD	Procedures Document	**AM**	Analysis Memorandum
MN	Meeting Note	**SL**	Supervisory Letter
RN	Report Note	**SEL**	Supervisory Expectation Letter
CL	Conclusion Letter	**QCM**	Quality Control Memorandum

3. Workpaper naming conventions should be concise, descriptive, and logical and should start with the defined prefix. Examples of naming conventions are as follows

Type	Example Workpaper Title
Report of Examination	ROE – 2014
Request Letter	RL – [Title of Targeted Examination or short name)
Procedures Document	PD- [Title of Supervisory Activity]
Meeting Note	MN – CIO [MM-DD-XXXX]
Report Note	RN – Board Materials Feb 2014
Enterprise Document	ED-Credit Risk Committee Materials-February 2014
Summary Memorandum	SM – [Name of Ongoing Monitoring Activity [MM-DD-YYYY]
Analysis Memorandum	AM – [Title of Supervisory Activity or short name]
Conclusion Letter	CL – Final [Title of Targeted Examination]
Supervisory Letter	SL – Final [Title of Supervisory Activity]
Supervisory Expectation Letter	SEL- [Topic][MM-DD-XX]

RECOMMENDED WORKPAPER FOLDER STRUCTURE

1. Supervisory activities that support the Supervisory Plan should be documented in the electronic recordkeeping system, including those activities led by DSPS (i.e., Office of Chief Accountant, Office of Risk Analysis)
2. To promote consistent recordkeeping throughout DER and to facilitate the quality control review process, examiners are encouraged to establish and maintain a standardized folder structure that will contain the core documents necessary to support the results of the supervisory activity.
3. DER Model Risk Team and DSPS examiners should store their workpapers in separate folders if they are taking the lead on an examination. However, if they are supporting a portion of the supervisory activity being led by DER examination teams, the DER Examination Manager should identify the appropriate location for storing their work.

Jon D. Greenlee, Deputy Director
Division of Enterprise Regulation

Federal Housing Finance Agency

October 31, 2014

DER OPERATING PROCEDURES BULLETIN

2014-DER-OPB-02

USE OF THE WORK OF THE ENTEPRISE'S INTERNAL AUDITOR

This Operating Procedures Bulletin (OPB) supersedes Item #1 of 2013-DER-OPB-01, Matters Requiring Attention (MRA) Process, dated April 23, 2013.

This Division of Enterprise Regulation (DER) OPB establishes expectations for examiners relating to use of the work of the Enterprise's internal audit function.

Although examiners may consider the work performed by the Enterprise's internal audit function when conducting supervisory activities, examiners must not rely on internal audit findings and conclusions when developing examination findings. Internal audit findings should not be issued as examination findings unless the examiner has performed sufficient work to support his/her own conclusions regarding the issue.

Nina A. Nichols
Deputy Director
Division of Enterprise Regulation

Federal Housing Finance Agency

April 23, 2013

DER OPERATING PROCEDURE BULLETIN

2013-DER-OPB-01

Matters Requiring Attention (MRA) Process

PURPOSE

This Division of Enterprise Regulation (DER) Operating Procedure establishes expectations for the process of issuing and monitoring the GSEs' implementation and remediation of Matters Requiring Attention (MRAs). The Examiner-In-Charge (EIC) is responsible for approving all communications of MRAs to the GSEs, and ensuring that the Deputy Director, DER, reviews all communications as part of the EIC approval process.

EXAMINATION FINDING ISSUANCE

DER issues findings in accordance with FHFA Advisory Bulletin AB 2012-01, "*Categories for Examination Findings.*" See link AB 2012-01 for the categories and definitions of findings. Findings are categorized as a Matter Requiring Attention (MRA), Violation, or Recommendation. All findings are communicated by the EIC to the GSEs in a Conclusion Letter.

1. MRA is cited by the examiner. MRAs are identified by examiners through examinations or ongoing monitoring. Generally, examiners should not carry over internal audit findings and make them MRAs except in instances where the issues are of a nature that FHFA determines it needs to monitor closely the issues and progress against their remediation.

2. Upon receipt and within a specified timeframe (60 days from the date of MRA issuance), the Enterprises need to develop and submit to FHFA an action plan that outlines specific and detailed steps that will be taken to address the MRA and ensure that a sustainable solution will be put in place.

3. FHFA reviews the action plan and determines whether the plan is sufficiently detailed and appropriate to resolve the MRAs. If the plan is deemed acceptable, FHFA will issue a "non-objection" letter. If the plan is not considered acceptable, then FHFA will issue a letter (after discussions with appropriate management) highlighting the deficiencies and requesting a new action plan.

4. Upon receipt of the "non-objection" letter, the FHFA expects the Enterprises to implement the action plan and keep FHFA onsite examiners apprised of progress against the timeline for remediating the MRAs.

5. Upon completion of the action plan and management's determination that the respective Enterprise has remediated the MRAs, internal audit or an another independent third party will review and "validate" that the action plan was implemented as intended and that the remediation is complete. The Enterprise will provide these reports to FHFA as part of its ongoing monitoring of the Enterprises. The completed validation work does not mean that FHFA has "closed" the MRA; instead, the Enterprise will receive subsequent communications from FHFA that the MRAs have been remediated.

6. FHFA will assess the remediation of the MRA through on-going monitoring or related targeted examination work. If additional reviews are needed, examiners will conduct the necessary reviews to validate the remediation. If the onsite supervisory team determines that the MRAs have been addressed, then FHFA will communicate this to the Enterprise in the next examination cycle and remove the MRA from the FHFA MRA tracking report.

Jon D. Greenlee
Deputy Director,
Division of Enterprise Supervision

April 23, 2013

DER OPERATING PROCEDURE BULLETIN

2013-DER-OPB-01

Matters Requiring Attention (MRA) Process

PURPOSE

This Division of Enterprise Regulation (DER) Operating Procedure establishes expectations for the process of issuing and monitoring the GSEs' implementation and remediation of Matters Requiring Attention (MRAs). The Examiner-In-Charge (EIC) is responsible for approving all communications of MRAs to the GSEs, and ensuring that the Deputy Director, DER, reviews all communications as part of the EIC approval process.

EXAMINATION FINDING ISSUANCE

DER issues findings in accordance with FHFA Advisory Bulletin AB 2012-01, "*Categories for Examination Findings.*" See link AB 2012-01 for the categories and definitions of findings. Findings are categorized as a Matter Requiring Attention (MRA), Violation, or Recommendation. All findings are communicated by the EIC to the GSEs in a Conclusion Letter.

1. MRA is cited by the examiner. MRAs are identified by examiners through examinations or ongoing monitoring. Generally, examiners should not carry over internal audit findings and make them MRAs except in instances where the issues are of a nature that FHFA determines it needs to monitor closely the issues and progress against their remediation.

2. Upon receipt and within a specified timeframe (60 days from the date of MRA issuance), the Enterprises need to develop and submit to FHFA an action plan that outlines specific and detailed steps that will be taken to address the MRA and ensure that a sustainable solution will be put in place.

3. FHFA reviews the action plan and determines whether the plan is sufficiently detailed and appropriate to resolve the MRAs. If the plan is deemed acceptable, FHFA will issue a "non-objection" letter. If the plan is not considered acceptable, then FHFA will issue a letter (after discussions with appropriate management) highlighting the deficiencies and requesting a new action plan.

4. Upon receipt of the "non-objection" letter, the FHFA expects the Enterprises to implement the action plan and keep FHFA onsite examiners apprised of progress against the timeline for remediating the MRAs.

5. Upon completion of the action plan and management's determination that the respective Enterprise has remediated the MRAs, internal audit or an another independent third party will review and "validate" that the action plan was implemented as intended and that the remediation is complete. The Enterprise will provide these reports to FHFA as part of its ongoing monitoring of the Enterprises. The completed validation work does not mean that FHFA has "closed" the MRA; instead, the Enterprise will receive subsequent communications from FHFA that the MRAs have been remediated.

6. FHFA will assess the remediation of the MRA through on-going monitoring or related targeted examination work. If additional reviews are needed, examiners will conduct the necessary reviews to validate the remediation. If the onsite supervisory team determines that the MRAs have been addressed, then FHFA will communicate this to the Enterprise in the next examination cycle and remove the MRA from the FHFA MRA tracking report.

Jon D. Greenlee
Deputy Director,
Division of Enterprise Supervision

October 29, 2013

DER OPERATING PROCEDURES BULLETIN

2013-DER-OPB-03.1

SUPERVISORY PLANNING PROCESS

PURPOSE

The Division of Enterprise Regulation (DER) conducts annual examinations to determine the condition, and assess the financial safety and soundness and overall risk management practices of Fannie Mae and Freddie Mac. DER uses a risk-focused rating system under which the Enterprises are assigned a composite rating based on an evaluation of various aspects of its operations.

This DER Operating Procedures Bulletin (OPB) expands upon the FHFA Examination Manual and establishes the DER-specific protocols and documentation requirements for planning the annual examination of Fannie Mae and Freddie Mac (collectively, the Enterprises.) Specifically, DER requires the following records to support the supervisory planning process and be filed in DER's system of record:

- Business Profile
- Risk Assessment
- Supervisory Strategy
- Supervisory Plan

The DER Deputy Director is responsible for developing a supervisory framework whereby the planning process is fully documented and incorporated into official agency records. The Examiner-in-Charge (EIC) is responsible for executing the supervisory framework as planned or amended.

The effective date for implementation of the requirements for the Supervisory Strategy and Supervisory Plan is immediately upon the date of issuance of this OPB. The effective date for DER's full implementation of the requirements of this OPB is January 1, 2014.

BUSINESS PROFILE

The Business Profile is a living document that serves to develop a comprehensive description of the business and risks of the Enterprise. Business Profiles can focus on a specific business line, program area or key corporate function (such as compliance, internal audit, operations and technology, ERM) and describe the core information necessary to understand the risks associated with the area. The Business Profile is developed and updated from information obtained from supervisory activity, but primarily from ongoing monitoring. The content of the Business Profile is at the discretion of each EIC, but at a minimum, should cover the following information:

- Executive summary
- Business Overview
- Organizational Structure
- Key risks and challenges
- How risks are managed
  - Business line management
  - Enterprise Risk Management and Compliance Functions
  - Internal Audit
- Compliance requirements from key laws and regulations (including Conservator Directives and the Senior Preferred Stock Purchase Agreement)
- Previously identified findings and status of remediation
- Potential or actual litigation

RISK ASSESSMENT

The Risk Assessment is a document that helps the EICs focus supervisory activities on areas of greatest risk to the Enterprises. The Risk Assessment highlights both the strengths and vulnerabilities of an Enterprise, informs the supervisory planning process, and serves as the basis for the development of the Supervisory Strategy. EICs are required to prepare a semiannual Risk Assessment that reflects an updated view of risk based upon supervisory activities conducted in the first half of the year and potentially other changes in risk caused by the external environment. EICs have the discretion to require additional periodic Risk Assessments, such as quarterly updates, throughout the year.

In preparing the Risk Assessment, EICs should consider the overall risk environment, the reliability of its internal risk management and controls, the adequacy of its information technology systems, and the risks associated with each of its significant business activities (single-family, multifamily, and capital markets.) EICs should also consider input provided by other stakeholder offices within FHFA to ensure that the Risk Assessment provides a comprehensive view of risk. At a minimum, the content of the Risk Assessment should include an executive summary, and a discussion of the following:

- Types of inherent risks (credit, market, liquidity, operations, model, legal/ compliance)
- Level of inherent risks (high, moderate, low)
- Quality of risk management controls (identification, measurement, monitoring and management)
- Residual risk
- Direction of risk (increasing, stable, decreasing)
- A summary of examination conclusions and/or emerging issues (such as changing market conditions)

SUPERVISORY STRATEGY

During the fourth quarter, the EIC prepares the Supervisory Strategy for the upcoming examination cycle for the DER Deputy Director's approval. The Supervisory Strategy is a document that reinforces FHFA's strategic goals, establishes and focuses the objectives and priorities of DER's efforts on the highest areas of risk and safety and soundness concerns, and provides the flexibility necessary to support new agency initiatives. The EICs should ensure that the Supervisory Strategy links to the FHFA Strategic Plan, and the associated performance goals and measures.

The Supervisory Strategy should include, at a minimum, the following information:

- A high level overview of the business of the Enterprise
- A summary of financial performance of the Enterprise
- A summary of the overall condition of the Enterprise, including:
    a. The supervisory component and composite ratings assigned to the Enterprise for the last two years, plus an indication of where the supervisory rating is trending for the current year
    b. Risk profile for each business unit and key corporate function, including: operational, credit, financial performance, market, model, governance and compliance based on previous supervisory activity as well as emerging risks
- Planned supervisory approach (extent of ongoing monitoring or targeted examination activity)
- Planned objectives that address the significant risks and the principal supervisory priorities for the year.

The EICs should periodically review the Supervisory Strategy and update it to reflect any changes in supervisory objectives, the Enterprise's financial condition, and/or trends in risk exposures. Any risk-based changes to the Supervisory Strategy must be approved by the DER Deputy Director. Since the Supervisory Strategy forms the basis for the Supervisory Plan, any changes to the Supervisory Strategy must also be reflected in the Supervisory Plan.

ANNUAL SUPERVISORY PLAN

The annual Supervisory Plan (Plan) is a document that is created and maintained by the EICs and approved by the DER Deputy Director. The Plan presents the expected scope and objectives for carrying out the Supervisory Strategy and sets forth the type[1] of planned supervisory activity. The Plan should also reflect resources needed for reviewing the Enterprise's remediation of Matters Requiring Attention (MRAs).

[1] Type of supervisory activity is either ongoing monitoring or targeted examinations. Special "ad hoc" projects may be initiated throughout the year as a product of ongoing monitoring; however, these activities are not planned and therefore not added to the Plan.

The Plan must clearly link to the overall Supervisory Strategy. Because planning is a continuous process, the EICs should ensure that the Plan is adjusted to add emerging risks that arise and require attention during the current examination cycle. In the event that changes to the risk environment warrant changes to the Plan, including adding or deleting supervisory activities, or changing the objective, scope, and methodology of supervisory activity during the examination cycle, these adjustments must be based on risk, and the justifications for the adjustments must be approved by the EIC (after consultation with the DER Deputy Director, if warranted) and fully documented in the workpapers.

Each EIC should include, at a minimum, the following elements in the Supervisory Plan:

- Title of supervisory activity
- Type of supervisory activity (i.e., ongoing monitoring (including MRA Remediation) or targeted exam)
- Brief description of the objectives (i.e., why we are doing the work and what are the intended results)
- Map to the Supervisory Strategy objective

SUPERVISORY ACTIVITIES

There are two types of supervisory activities: ongoing monitoring (including MRA Remediation) and targeted examinations. The minimum expectations for conducting ongoing monitoring and targeted examinations and the minimum workpaper requirements for each are addressed in more detail in 2013-DER-OPB-04, *DER Supervisory Activities*.

Jon D. Greenlee, Deputy Director
Division of Enterprise Regulation

Federal Housing Finance Agency

September 19, 2013

DER OPERATING PROCEDURES BULLETIN

2013-DER-OPB-04

DER SUPERVISORY ACTIVITIES

PURPOSE

This Division of Enterprise Regulation (DER) Operating Procedures Bulletin (OPB) establishes minimum expectations for performing supervisory activities and minimum workpaper requirements for each supervisory activity type. Ongoing monitoring and targeted examinations are the primary types of supervisory activity carried out by DER to complete the annual examinations of Fannie Mae and Freddie Mac. Workpapers to support examination conclusions are official agency records and as such, these expectations are applicable to both examination core teams.

DER's workpaper standards and descriptions are described under a separate OPB (2013-DER-OPB-05). When preparing workpapers, examiners are expected to follow established templates that are developed for each of the core teams. The Examiners-in-Charge (EICs) and Managers have the discretion to establish additional requirements to those stated below.

All ongoing monitoring and targeted examination activities commenced after January 1, 2014 should comply with the requirements outlined in this Operating Procedures Bulletin.

ONGOING MONITORING

Ongoing monitoring is an important component to effective supervision. The objective of ongoing monitoring is to allow DER to maintain a current understanding of business activities and risks. Ongoing monitoring allows examiners to identify and monitor issues that affect the risk profile and communicate with management in a timely manner regarding any areas of concern.

Ongoing monitoring activities are designed to monitor and analyze information and to identify Enterprise practices and changes in an Enterprise's risk profile that may warrant further supervisory attention. Ongoing monitoring allows the EIC to promptly respond to risks and to direct resources to those areas of increasing or emerging risk. Ongoing monitoring may reveal the first indications of control breakdowns and the emergence of material risk exposures. Alternatively, it may identify demonstrated improvement in risk management practices.

Weaknesses in Enterprise practices and substantial changes in an Enterprise's risk profile and exposures may result in, among other things, adjustments to the supervisory strategy, the supervisory plan, and examination risk ratings. Weaknesses in practices may also result in the issuance of examination findings.[1]

Ongoing monitoring includes a range of activities examiners perform in accordance with the supervisory plan that assist the EIC in developing the business and risk profile of the Enterprise. Ongoing monitoring activities take a variety of forms, and may include:

- Analysis of management, board and audit reporting;
- Meetings with Enterprise management and personnel;
- Evaluating and conducting limited testing of the Enterprise's compliance with supervisory requirements, and risk management practices and systems;
- Analysis of emerging issues and related supervisory concerns; and,
- Analysis of trends in industry practices, economic and other condition.

The nature of ongoing monitoring will depend upon, among other considerations, the Enterprise's past, current and anticipated risk profile; market developments and trends; Enterprise organizational changes; previous examination findings; and supervisory guidance and requirements issued by FHFA as supervisor and as Conservator.

Workpaper Requirements for Ongoing Monitoring

Ongoing Monitoring activities are defined and assigned by the EIC to an examination manager and carried out by a designated lead examiner according to the supervisory plan. Prior to the start of the ongoing monitoring activity, the EIC, manager and lead examiner meet to ensure there is a clear understanding of expectations for the activity and document the agreed upon expectations in the workpapers. These expectations can include the following:

- Scope and objectives;
- Start date; and,
- Expected deliverables, including due dates, which must include a Procedures Document and at least one of the following:
    - Periodic status memoranda;
    - Analysis memorandum[2];

[1] Refer to FHFA Advisory Bulletin, AB-2012-01, *Categories for Examination Findings*. FHFA defines examination findings as "deficiencies related to risk management, risk exposure, or violations of laws, regulations or orders that affect the performance or condition of a regulated entity. The Advisory Bulletin establishes three categories of examination findings: Matters Requiring Attention, Violations, and Recommendations.

[2] The Manager may require an analysis memorandum as a deliverable for ongoing monitoring activity even if no examination finding is identified. However, the manager must require an analysis memorandum once an examination finding is identified.

- Input to the business profile; and/or,
- Input to a periodic risk assessment memorandum.

If during the course of the ongoing monitoring activity the EIC approves changes to the scope and objectives based on risk-related reasons, the justification for the change as well as the evidence of manager and EIC approval must also be documented in the workpapers. Further, the manager needs to ensure that changes to the objective of the ongoing monitoring activity are appropriately reflected in the supervisory plan, if warranted.

For tracking purposes, the start date for ongoing monitoring activity is the date agreed upon by the EIC, manager and lead examiner prior to the start of the activity.

*Procedures Documents are **Required***

Procedures documents set forth the steps performed to achieve the objective and provide the official agency record of evidence to support the execution of the ongoing monitoring activity. Procedures documents are required for all ongoing monitoring activities. The lead examiner is responsible for developing procedures to meet each objective for the ongoing monitoring activity and for obtaining and documenting the manager's approval of the procedures document.

The procedures document must be updated, when warranted, to reflect additions and/or deletions of steps taken to meet the objectives. Examiners should document the justification for the change and the manager's approval in the workpapers. Further, the manager needs to ensure that changes made to the procedures document are appropriately reflected in a revised supervisory plan, when warranted.

When preparing the procedures document, the examiner should review and consider the tools available to DER, such as examination modules, supplemental guidance, and advisory bulletins that pertain to the subject of the ongoing monitoring activity.

*Request Letters, Meeting Notes and Report Notes are **Not Always Required***

Request letters may be sent to the Enterprise at the EIC's discretion, but they are not required for ongoing monitoring activities. If the EIC chooses to issue a request letter, follow the requirements found below under "Targeted Examinations."

Meeting notes and report notes[3] are required to become part of the official examination record if the examiner is relying on the information to support an examination conclusion, to substantiate

[3]Meeting notes are the examiner's documentation of a meeting they attended with enterprise personnel as part of a supervisory activity. Meeting notes summarize the discussion points made during the meeting. Report notes are an examiner's comments, questions, or conclusions reached during the review of an externally-generated document.

the execution of a procedure, or to document an examiner's status update to management. Examiners are encouraged to meet with Enterprise management as often as necessary to verify factual information and discuss topics of interest and relevance. A good practice is to have a minimum of two examiners attend each meeting in order to confirm the accuracy of the information obtained and to serve as an observer in case disagreements arise over the information conveyed in the meeting.

Analysis Memorandum/Supervisory Letters are ***Required*** *when Examination Findings are identified*

If the EIC issues an MRA, violation, or recommendation resulting from ongoing monitoring, the supporting analysis and conclusions reached leading to the finding must be documented in an analysis memorandum and communicated to the Enterprise in a supervisory letter. The analysis memorandum is considered the main work product from the supervisory activity to support the supervisory letter. The analysis memorandum:

- Is generally prepared by the lead examiner;
- Is approved by the examination manager and EIC (documented through an automated workflow);
- Must include an appropriate audit trail to the procedures document to show how the execution of the procedures resulted in the conclusions summarized in the analysis memorandum;
- Must include links to supporting workpapers such as Enterprise documents, meeting notes, report notes, and provide sufficient analysis to support the conclusion; and,
- Must never be shared with the Enterprise.

Further, all MRAs, violations and recommendations identified during the course of ongoing monitoring activity are to be communicated to the Enterprise in a supervisory letter. DER uses the term "supervisory letter" to communicate results of ongoing monitoring rather than "conclusion letter" because ongoing monitoring may continue after the issuance of an examination finding; whereas conclusion letters communicate examination findings to the Enterprise at the conclusion of a targeted examination.

TARGETED EXAMINATIONS

Targeted examinations are designed to assess a particular area, product, risk or activity of the Enterprise and by definition are narrow in scope. The advantage of choosing a targeted examination over ongoing monitoring is that the examiner is expected to conduct detailed analysis and testing in order to develop specific conclusions.

Reports notes document how the externally-generated document (e.g., enterprise documents, authoritative literature, white papers) were used during the supervisory activity to draw conclusions, and provide the basis and support for any criticism of reports used during the activity.

Each targeted examination must have a clearly defined objective, scope, and procedures document and have a distinct beginning and end. Specifically, all targeted examinations begin with a request letter and end with a conclusion letter. Targeted examinations generally include a kickoff meeting, scheduled meetings with management, document review, analyses, and transaction testing. Examiners should conduct periodic status meetings with Enterprise management to update them on any issues that may arise, and must have an exit meeting prior to the issuance of a conclusion letter. Examiners must be diligent in assuring that Enterprise management is fully aware of any emerging concerns and potential findings and conclusions prior to the exit meeting.

Workpaper Requirements for Targeted Examinations

After being defined by the EIC, targeted examinations are assigned to an examination manager, who designates a lead examiner to carry out the examination according to the supervisory plan. As with ongoing monitoring, if during the course of the targeted examination the EIC approves changes to the scope and objectives based on risk-related reasons, the justification for the change as well as the evidence of manager and EIC approval must also be documented in the workpapers. Further, the manager needs to ensure that changes to the objective of the targeted examination are appropriately reflected in the supervisory plan, if warranted.

For tracking purposes, the start date of the targeted examination is the date of the request letter.

*Procedures Documents are **Required***

Procedures documents set forth the steps performed to achieve the objective and provide the official agency record of evidence to support the execution of the targeted examination. Procedures documents are required for all targeted examinations. The lead examiner is responsible for developing procedures to meet each objective for the examination and for obtaining and documenting the manager's approval of the procedures document.

The procedures document must be updated, when warranted, to reflect additions and/or deletions of steps taken to meet the objectives. Examiners should document the justification for the change and the manager's approval in the workpapers. Further, the manager needs to ensure that changes made to the procedures document are appropriately reflected in a revised supervisory plan, when warranted.

When preparing the procedures document, the examiner should review and consider the tools available to DER, such as examination modules, supplemental guidance, and advisory bulletins that pertain to the subject of the ongoing monitoring activity.

*Request Letters and Meeting Notes are **Required***

Request letters announce the objective and scope of the targeted examination to the Enterprise, request the Enterprise to schedule a kickoff and subsequent meetings with management, and request timely delivery of a list of documentation to be produced by the Enterprise. Request letters are required to be sent to the Enterprise generally two weeks to one month prior to the start of the fieldwork. Document production due dates are included in the request letter and should generally be between two weeks to one month from the date of the request letter, but the EIC has the discretion to adjust the due dates as circumstances warrant. Before the request letter is sent, examiners are required to take reasonable steps to ensure that FHFA is not already in receipt of the requested documentation, such as checking the Enterprises' electronic report repositories.

To ensure that the requested documentation list will provide the information needed conduct the targeted examination, the procedures document and request letter should be approved concurrently.

*Meeting Notes are **Required***

Examiners are expected to conduct periodic status meetings with management throughout the targeted examination to ensure that management is kept apprised of any preliminary findings or emerging concerns. At the end of fieldwork, the examination team must meet with Enterprise management to verify the facts on which the examiner's conclusions are based.

Additionally, examiners are required to hold an exit meeting with management ***after*** the draft analysis memo has been approved by the EIC and before the quality control review[4] and issuance of the conclusion letter. The purpose of the exit meeting is to review with Enterprise management the preliminary conclusions and to discuss any examination findings (i.e., recommendations, MRAs, violations) that will be reported in the conclusion letter. Examiners should inform Enterprise management at the exit meeting that examination conclusions are not final, as they are subject to a final review by DER management.

Examiners are required to prepare meeting notes for all status and exit meetings and retain them as official agency records.

[4] On March 25, 2013, FHFA issued SD 2013-01, titled, "*Quality Control Program for Examinations Conducted by the Division of Bank Regulation and the Division of Enterprise Regulation*, which requires DER to conduct a quality control review of examination findings, conclusions, ratings, supporting workpapers, and related documents prior to issuance to the regulated entities.

Analysis Memorandum and Conclusion Letter are ***Required***

The analysis memorandum is the main work product from the supervisory activity that supports the conclusion letter. The analysis memorandum:

- Is generally prepared by the lead examiner;
- Is approved by the examination manager and EIC (documented through an automated workflow);
- Must include an appropriate audit trail to the procedures document to show how the execution of the procedures resulted in the conclusions summarized in the analysis memorandum;
- Must include links to supporting workpapers such as Enterprise documents, meeting notes, report notes, that provide sufficient analysis to support the conclusion; and,
- Must never be shared with the Enterprise.

Conclusions from targeted examinations are always communicated to the Enterprise in a conclusion letter. The conclusion must directly correlate to the stated objective(s), as stated in the request letter. If the results of examination include the identification of an examination finding (MRA, violation or recommendation), then the examiners are required to customize the content of the conclusion letter as follows:

If the Conclusion Letter identifies:	Management Response is Required	Remediation Plan is Required
No MRA, violation or recommendation	No	No
MRA	Yes	Yes
Violation	Yes	Yes
Recommendation	Optional	No

In the event a management response is required, examiners must state in the conclusion letter the due date (usually sixty days) and direct that an acceptable management response must contain the following elements:

- A remediation plan that clearly defines the steps to be taken to remediate the condition;
- The name of the Enterprise official assigned to oversee the required remediation activity; and,
- The expected date of the completion of the remediation.

For purposes of tracking, DER only tracks the remediation of MRAs and violations, not recommendations.

WORKPAPER APPROVAL REQUIREMENTS

The following table summarizes the workpaper types, whether they are required or optional, and the required approvals for workpapers for each supervisory activity.

Supervisory Activity	Workpaper Type	Required Documents (FHFA Records)	Optional	Required Approvals (via Workflow)
Ongoing Monitoring	Procedures Document	X		Lead Examiner Manager EIC (Optional)
	Request Letter		X	Lead Examiner Manager
	Meeting/Report Notes		X	Lead Examiner
	Analysis Memo	X (w/Examination Findings)	X (no Examination Findings)	Lead Examiner Manager EIC
	Periodic Risk Assessment		X	Lead Examiner Manager EIC DD-DER (Optional)
	Business Profile		X	Lead Examiner Manager EIC
	Supervisory Letter	X (w/Examination Findings)	X (no Examination Findings)	Lead Examiner Manager EIC DD-DER DD-DSPS (Optional)
Targeted Examination	Procedures Document	X		Lead Examiner Manager EIC (Optional)
	Request Letter	X		Lead Examiner Manager EIC
	Meeting/Report Notes	X		Lead Examiner Manager
	Analysis Memorandum	X		Lead Examiner Manager EIC
	Conclusion Letter	X		Lead Examiner Manager EIC DD-DER (DD-DSPS (Optional)

/s/

Jon D. Greenlee, Deputy Director
Division of Enterprise Regulation

Federal Housing Finance Agency

May 25, 2016

DIVISION OF ENTERPRISE REGULATION (DER) OPERATING PROCEDURES BULLETIN

DER-OPB-01

ENTERPRISE SUPERVISION: MID-YEAR RISK ASSESSMENTS

PURPOSE

DER's risk assessments are critical components of effective risk-based supervision of the Enterprises. Enterprise supervision staff's assessment of risks in key areas is a foundation for the annual examination plan for each Enterprise and a basis for evaluating the Enterprises' risk management in those areas and their overall safety and soundness.

This Operating Procedures Bulletin (OPB) sets forth procedures for the preparation, approval, and documentation of mid-year risk assessments. The procedures include formats to improve consistency of definitions and use of key terms and risk measures. While the assessment of risk by supervision staff is an ongoing process, specific documentation and approval requirements apply to the mid-year risk assessment, as described in this OPB.

This OPB supersedes Supervision Directive SD-2013-02 (*Division of Enterprise Regulation: Periodic Risk Assessments)* (December 3, 2013).

GUIDANCE

The Examiner-in-Charge (EIC) at each Enterprise annually assigns a composite rating and component ratings to the Enterprise in accordance with FHFA's Examination Rating System (AB 2012-03, December 19, 2012). The ratings are assigned as of December 31 each year and are included in the annual report of examination (ROE), which includes the examination work and findings for the calendar year. The ratings and ROE must be approved by the Deputy Director, DER, and they are transmitted to the Enterprise's board of directors in the first quarter of the following calendar year.

Each EIC is responsible for risk assessment for their respective Enterprise, and the overall risk assessment supports the composite rating and component ratings of each Enterprise. The EIC completes the mid-year risk assessment, with documentation to be finalized and approved in accordance with DER's standard workflow approval practices by September 30. Documentation of the mid-year risk assessment must include credit, market, and operational risk components in the templates included as attachments to this OPB, and may include other risk elements, as determined by the EIC. For example, the EIC's risk assessment may include information relating to governance, model risk management, compliance, or internal control for financial reporting.

The EIC may update the risk assessment as appropriate to address developments that affect the Enterprise's current or projected financial condition or resilience. A mid-year risk assessment may be referenced to support a change to an assigned rating. Any changes to a rating must be approved by the Deputy Director, DER, and must be communicated in writing to the board of directors of the Enterprise.

The risk assessment informs Enterprise supervision in various ways. In addition to providing the EIC with a tool for review of the ratings, it is available to the examiners in preparing examination plans and in performing examination activities (for example, developing scope and procedures documents). The risk assessment may also inform risk and policy analysts in the development of guidance and supervisory expectations for risk management by the Enterprises.

Risk assessments must include input from the respective executive heading the Office of Model, Credit and Market Risk (OMCMR) and the Office of Governance, Compliance and Operational Risk (OGCOR) about credit, market, or operational risks. Input must be provided on Part One of the attached templates in accordance with template instructions. Part One includes descriptions of risks, relevant quantitative and qualitative measures, and applicable or relevant risk management standards or sound practices. Completed Part One of each template should be provided to the EIC following the issuance of the ROE and no later than June 30.

The EIC for each Enterprise is responsible for completion of Part Two of the credit, market, and operational risk templates in accordance with template instructions. Part Two of the templates and instructions provide for documentation of the EIC's conclusions on the overall inherent risk rating (low, moderate, high) for credit, market, and operational risk; the quality of risk management (strong, satisfactory, insufficient, weak); residual risk (low, moderate, high); and the direction of risk (decreasing, stable, increasing). There are also executive-level summaries supporting the EIC's conclusions for inherent risk, quality of risk management, residual risk, and direction of risk.

The completed mid-year risk assessment for each Enterprise must include Parts One and Two of the credit, market, and operational risk templates and any additional information as determined by the EIC. Each mid-year risk assessment must be sent through a DER standard workflow for review and documentation of approval by the appropriate EIC, the executives heading OMCMR and OGCOR, and the Deputy Director, DER. The approved mid-year risk assessments must be maintained in the appropriate folders.

EFFECTIVE DATE

This OPB is effective immediately. The mid-year risk assessment templates and related instructions are effective immediately, and may be updated periodically.

Nina A. Nichols, Deputy Director
Division of Enterprise Regulation

ATTACHMENTS:

Mid-Year Risk Assessments: General Instructions
Mid-Year Risk Assessments:
 Credit Risk template and instructions
 Market Risk template and instructions
 Operational Risk template and instructions

Division of Enterprise Regulation
Mid-Year Risk Assessment
General Instructions for Credit, Market, and Operational Risk Templates

General Instructions

Pursuant to operating procedures of the Division of Enterprise Regulation (DER), the Examiners-in-Charge (EICs) of Fannie Mae and Freddie Mac (the Enterprises) prepare mid-year risk assessments for the Enterprises. See DER-OPB-01 (*Enterprise Supervision: Mid-Year Risk Assessments*) (May 25, 2016). Each mid-year risk assessment must include a completed template for credit, market, and operational risk. Each template comprises a risk analysis section (Part One) and a risk assessment section (Part Two). The mid-year risk assessment for each Enterprise must be submitted in a workflow for formal approvals and documentation by the EIC, the executives heading the DER Offices of Model, Credit and Market Risk (OMCMR) and Governance, Compliance and Operational Risk (OGCOR), and the Deputy Director, DER, by September 30. The final risk assessment must be saved in the appropriate folder.

The risk assessment should be based on current information about Enterprise operations and risks. The conclusions derived through the risk assessment process will be used to support development of the examination plan. The EICs may consider the information presented and any knowledge gaps in determining whether amendments to the risk-based examination plans are necessary.

Part One: Risk Analysis

The executives heading OMCMR and OGCOR are responsible for providing input for analysis of credit, market, and operational risks to the EICs. The completed Part One of each template should be provided to the EICs as soon as practicable following the issuance of the report of examination and no later than June 30.

Risk Type and Description: The risk analysis section provides more detailed information about risks, that is, the potential that events will have an adverse effect on the Enterprise's current or projected financial condition or resilience. Part One includes identification and description of particular risks to be considered. Descriptions should include an explanation of how risks could affect the Enterprises' financial condition or resilience.

Risk Measures: Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise.

- Credit risk measures include metrics for assessing credit quality of Enterprise assets, for quantifying the probability and size of potential credit losses associated with borrower and counterparty default risk, and for assessing an Enterprise's process for determining the level of reserves needed in the event of credit losses.

- Market risk measures include metrics for assessing an Enterprise's ability to meet its financial obligations and its vulnerability of current and future earnings and capital to interest rate changes.

- Operational risk measures include metrics for assessing the quantity of operational risk and the quality of operational risk management.

<u>Risk Management Standards and Guidance</u>: Part One of each template includes references to (or summaries of, as appropriate) relevant and applicable FHFA risk management standards and guidance. Guidance of other regulators or controls that represent industry sound practices may be referenced or described for information, although they do not establish risk management criteria of FHFA.

Part Two: Risk Assessment

Each EIC is responsible for completion of Part Two of each template, an Enterprise-specific assessment for credit, market, or operational risk.

<u>Risk Type</u>: Each Enterprise-specific template should include in Part Two under “Risk Type” applicable risks identified and described in Part One. If additional risk types are added, descriptions should be provided.

<u>Risk Levels:</u>

1. Inherent Risk (Low, Moderate, High)

Inherent risks are those internal or external risks to which the Enterprise is exposed, knowingly or unknowingly, as a result of the business activities in which it engages, and the external environment in which the activities take place. The summary should discuss which risk types are inherently manifested at the Enterprise and how, but should not include commentary relating to controls and risk management.

- **High inherent risk** exists where there is potential for a significant and harmful loss. In general, indicia of high risk are present when positions are very large in relation to the Enterprise’s resources, where there are a substantial number of transactions, where the nature of the activity is unusual, and/or where metrics are difficult to define or model.

- **Moderate inherent risk** exists where potential losses, though present, could likely be absorbed by the Enterprise in the normal course of business. In general, indicia of moderate risk are present when the volume of transactions is not large in relation to the Enterprise’s resources, where activity is routine, and/or where reliable metrics are readily available.

- **Low inherent risk** exists where if a loss were to occur it would have an inconsequential material negative impact on the Enterprise. In general, indicia of low inherent risk are present when the volume, size, or nature of the activity is such that, even if the internal controls have weaknesses, the risk of loss is remote.

2. Quality of Risk Management (Strong, Satisfactory, Insufficient, Weak)

Part Two includes a discussion of the risk management practices and controls implemented by the Enterprise to manage the specific risks identified. Information about risk controls may include effectiveness of board and senior management oversight; policies, procedures, and limits; risk monitoring and management information systems; and internal controls. Part Two includes an assessment of the quality of risk management (strong, satisfactory, insufficient, weak) and summary of analysis. In general, the characteristics of risk management practices outlined by the CAMELSO rating system inform the assessment of the quality of risk management, including how an Enterprise identifies, measures, controls, and monitors risks.

3(a). Residual Risk (Low, Moderate, High)

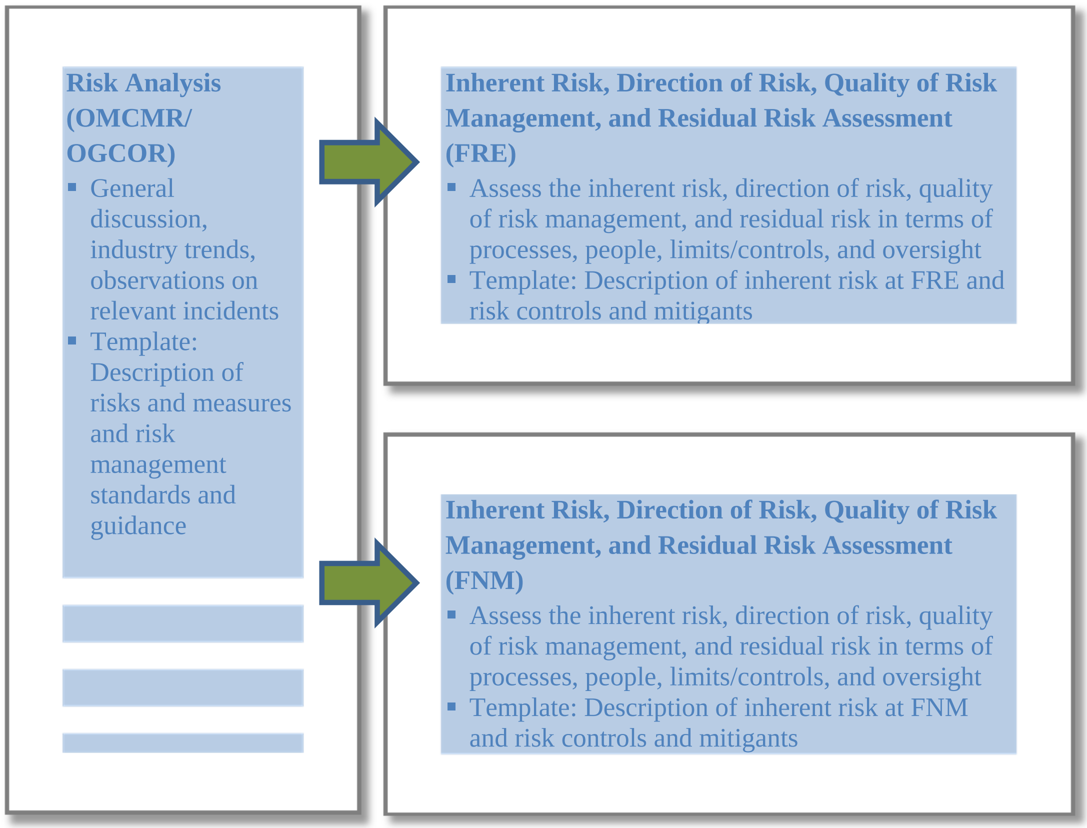
Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, as well as summary observations for the risk area. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Risk (Decreasing, Stable, Increasing)

Part Two includes a prospective assessment of the probable movement in inherent risk over the next 12 months, characterized as decreasing, stable, or increasing. An assessment of "decreasing" indicates that the EIC expects, based on current or best available information, that inherent risk will decline over the next 12 months. If risk is stable, the EIC expects inherent risk to remain unchanged. If risk is increasing, the EIC expects inherent risk to be higher in 12 months.

An expectation that inherent risk will increase or decrease does not necessarily mean that the movement is expected to be sufficiently large to change the inherent risk level within 12 months. An EIC can expect movement within the risk level. For example, inherent risk can be high and decreasing even though the decline is not anticipated to change the level of inherent risk to moderate. In such circumstances, the summary should indicate why a change in the risk level is not expected.

Mid-Year Risk Assessment Process Flow



Risk Type and Description	Risk Measures	Applicable FHFA Risk Management Standards and Guidance; Other Regulatory/Industry Issuances (*for information only*)

Risk Type	Inherent Risk	Risk Controls and Mitigants

1. Inherent credit risk: ☐ **Low** ☐ **Moderate** ☐ **High**
Summary:

2. Quality of credit risk management: ☐ **Strong** ☐ **Satisfactory** ☐ **Insufficient** ☐ **Weak**
Summary:

3(a). Residual credit risk: ☐ **Low** ☐ **Moderate** ☐ **High**
3(b). Direction of credit risk: ☐ **Decreasing** ☐ **Stable** ☐ **Increasing**
Summary:

Risk Measures

Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise. Examples of credit risk measures may include measures of credit portfolio quality; single-family mortgage performance, delinquency indicators, and loss rate data; multifamily mortgage performance and delinquency indicators; allowance for loan losses (*e.g.,* allowance level, charge-offs, recovery, coverage ratios, asset classifications based on mortgage performance and borrower characteristics); concentration levels; loss-mitigation measures; defect rates; and measures of counterparty risk and exposure.

1. **Inherent Credit Risk** (Low, Moderate, High)

In general, credit risk is the potential that a borrower or counterparty will fail to meet its obligations in accordance with agreed terms. Credit risk includes the decline in measured quality of a credit exposure that might result in increased capital costs, provisioning expenses, and a reduction in economic return. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighed differently in contributing to the rating.

- **Low:** Current or prospective credit risk of loss of earnings or capital is minimal. Credit risk reflects conservative risk selection, underwriting, and structures. The volume of substantive exceptions or overrides to underwriting standards poses minimal risk. Credit risk represents a well-diversified distribution by credit quality of borrower and borrower leverage. Risk of loss from concentrations is minimal. There is limited sensitivity due to deteriorating economic, industry, competitive, regulatory, and technological factors. Portfolio growth presents minimal concern and new initiatives are conservative. Refinancing practices are sound and pose minimal increased risk. The volume of troubled credits is low and can be resolved in the normal course of business. Credit-related losses do not meaningfully affect current reserves and result in modest provisions relative to earnings.

- **Moderate:** Current or prospective credit risk of loss of earnings or capital does not materially affect financial condition. Credit risk reflects acceptable risk selection, underwriting, and structures. Substantive exceptions or overrides to underwriting standards pose minimal risk. There are limited declines in borrower credit quality or increases in borrower leverage. Credit risk does not reflect significant concentrations. Vulnerability may exist due to deteriorating economic, industry, competitive, regulatory, and technological factors. While advanced portfolio growth may exist within specific products or sectors, it is in accordance with a reasonable plan. Refinancing practices are satisfactory. The volume of troubled credits does not pose undue risk relative to capital and can be resolved within realistic time frames. Credit-related losses do not seriously deplete current reserves or necessitate large provisions relative to earnings.

- **High:** Current or prospective credit risk of loss of earnings or capital is material. Credit risk reflects aggressive risk selection, underwriting, and structures. A large volume of substantive exceptions or overrides to sound underwriting standards exists. Credit risk is skewed toward lower credit quality borrower or highly leveraged borrowers. Credit risk reflects significant concentrations. Significant vulnerability exists due to deteriorating economic, industry, competitive, regulatory, and technological factors. Portfolio growth, including products or sectors within the portfolio, is aggressive. Refinancing practices reflect a significant deviation from current underwriting standards. The volume of troubled borrowers may be large and require an extended time to resolve. Credit-related losses may seriously deplete current reserves or necessitate large provisions.

2. Quality of Credit Risk Management (Strong, Satisfactory, Insufficient, Weak)

- **Strong**: Asset quality and credit risk management practices are strong. Any identified weaknesses are minor in nature and risk exposure is minimal in relation to the Enterprise's capital protection and management's ability to identify, monitor, and mitigate risks.

- **Satisfactory**: Asset quality and credit risk management practices are satisfactory. Identified weaknesses, such as the level and severity of adversely-rated or classified assets, are moderate and in line with the Enterprise's capital protection and management's ability to identify, monitor, and mitigate risks.

- **Insufficient**: Asset quality or credit risk management practices are insufficient. Identified weaknesses, such as the level and severity of adversely-rated or classified assets, are significant and not in line with the Enterprise's capital protection or management's ability to identify, monitor, and mitigate risks.

- **Weak**: Asset quality or credit risk management practices are weak. Identified weaknesses, such as the level of problem assets are significant and inadequately controlled. The weaknesses subject the Enterprise to significant potential losses.

3(a). Residual Credit Risk (Low, Moderate, High)

Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, and the overall risk rating. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Credit Risk (Decreasing, Stable, Increasing)

The rating for direction of credit risk should indicate the Enterprise's current level relative to prior ratings or reflect best information currently available (such as expected future risks based on current and past information).

Risk Type and Description	Risk Measures	Applicable FHFA Risk Management Standards and Guidance; Other Regulatory/Industry Issuances (*for information only)*

Risk Type	Inherent Risk	Risk Controls and Mitigants

1. Inherent market risk: ☐ **Low** ☐ **Moderate** ☐ **High**
Summary:

2. Quality of market risk management: ☐ **Strong** ☐ **Satisfactory** ☐ **Insufficient** ☐ **Weak**
Summary:

3(a). Residual market risk: ☐ **Low** ☐ **Moderate** ☐ **High**
3(b). Direction of market risk: ☐ **Decreasing** ☐ **Stable** ☐ **Increasing**
Summary:

Risk Measures

Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise. Examples of market risk measures may include duration gap; convexity gap; implied volatility; option adjusted spread; portfolio market value sensitivity (parallel shocks); portfolio market sensitivity (non-parallel shocks); key rate duration; prepayment duration; spread duration; percent of agency MBS securities in retained portfolio; percent of whole loans in portfolio; percent of private label securities in portfolio; percent of distressed assets in portfolio; bid/ask spreads funding ladder- debt maturity schedule; surplus days cash (base case and stressed); short term debt/long term debt ratio; coverage ratio; callable debt to bullet debt ratio; agency/swap basis; and maturity liquidity investments portfolio.

1. Inherent Market Risk (Low, Moderate, High)

Overall inherent market risk should reflect all types of market risk but specifically liquidity and interest rate risk. The aggregate of all market risks will be given a level of low, moderate, or high.

Liquidity

Liquidity risk is the risk that an Enterprise is unable to meet its financial obligations as they come due or meet the credit needs of its customers in a timely and cost-efficient manner. The Enterprises must be financially sound to perform their public missions and should have a comprehensive liquidity risk management framework to limit and control liquidity risk exposures. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighed differently in contributing to the rating.

- **Low:** The Enterprise is not vulnerable to funding difficulties should a material adverse change in market perception occur. Exposure from the liquidity risk profile is negligible. Ample funding sources and the cash flows for assets and liabilities (with derivatives) match in all tenors.

- **Moderate:** The Enterprise is not excessively vulnerable to funding difficulties should a material adverse change in market perception occur. Exposure from the liquidity risk profile is manageable. Sources of funding are reasonably diverse but minor concentrations may exist. Some groups of providers may share common investment objectives or be subject to similar economic influences. Sufficient funding sources and matching asset and liability cash flows exist to provide stable, cost-effective liquidity in most environments, without significant disruption in strategic lines of business.

- **High:** The Enterprise's liquidity profile makes it vulnerable to funding difficulties should a material adverse change occur. Significant concentrations of funding may exist. Large funds providers may share common investment objectives or be subject to similar economic influences. Funding sources and balance-sheet structures may currently result in, or suggest, potential difficulty in sustaining long-term liquidity on a cost-effective basis. Potential exposure due to high liability costs or unplanned asset reduction may be substantial. Liquidity needs may trigger the necessity for funding alternatives under a contingency funding plan (CFP), including the sale of, or disruption in, a strategic line of business.

Interest Rate Risk

Interest rate risk is the vulnerability of current or future earnings and capital to interest rate changes. Fluctuations in interest rates affect earnings by altering interest-sensitive income and expenses. Interest rate changes also affect capital by changing the net present value (NPV) of future cash flows and the cash flows themselves. Excessive interest rate risk can threaten liquidity, earnings, capital, and solvency.

In general, the regulated entities manage interest rate risk with a combination of swapped and unswapped callable and non-callable debt, fixed- and floating-rate bullet debt, and derivative instruments. They use derivatives to limit downside earnings exposures, preserve upside earnings potential, increase yield, and minimize income or capital volatility. When used properly, derivatives are an effective risk management tool, but improper usage can allow interest rate changes to have a sudden and significant effect on the regulated entity's financial position. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighed differently in contributing to the rating.

- **Low**: Exposure reflects minimal repricing, basis, yield curve, and options risk. Positions used to manage interest rate risk exposure are well-correlated to underlying risks. No significant mismatches on longer-term positions exist. Interest rate movements would have minimal adverse effect on the financial performance of the Enterprise. The Enterprise is not exposed to material losses as a result of changes in market prices. Enterprise assets and liabilities that do not offset each other are accounted for at fair value (*e.g.*, lending pipelines and mortgage servicing rights).

- **Moderate**: Exposure reflects manageable repricing, basis, yield curve, and options risk. Positions used to manage interest rate risk exposure are somewhat correlated. Mismatches on longer-term positions exist but are managed. Interest rate movements would not have a significant adverse effect on the financial performance of the Enterprise. The Enterprise has access to a variety of risk management instruments and markets at reasonable costs, given the size, tenor, and complexity of open positions. Assets and liabilities that do not offset each other are accounted for at fair value (*e.g.*, lending pipelines and mortgage servicing rights) and are unlikely to materially affect the Enterprise's financial condition.

- **High**: Exposure reflects significant repricing, basis, yield curve, or options risk. Positions used to manage interest rate risk exposure are poorly correlated. Significant mismatches on longer-term positions exist. Interest rate movements could have a significant adverse effect on the financial performance of the Enterprise. A significant volume of assets and liabilities that do not offset each other are accounted for at fair value (*e.g.*, derivatives, lending pipelines, and mortgage servicing rights), and valuation changes have significant potential to adversely affect the Enterprise's condition.

2. Quality of Market Risk Management (Strong, Satisfactory, Insufficient, Weak)

The overall quality of market risk management should reflect all types of market risk but specifically the qualities of risk management below. The aggregate of all market risk management will be given a level of strong, satisfactory, insufficient, or weak.

Liquidity

- **Strong**: The level of liquidity and the Enterprise's management of its liquidity position are strong. Any identified weaknesses in its liquidity management practices are minor. The Enterprise has reliable access to sufficient sources of funds on favorable terms to meet current and anticipated liquidity needs. The Enterprise meets or exceeds regulatory guidance related to liquidity.

- **Satisfactory**: The level of liquidity and the Enterprise's management of its liquidity position are satisfactory. The Enterprise may have moderate weaknesses in its liquidity management practices, but these are correctable in the normal course of business. The Enterprise has reliable access to sufficient sources of funds on acceptable terms to meet current and anticipated liquidity needs. The Enterprise meets or exceeds regulatory guidance related to liquidity.

- **Insufficient**: The level of liquidity or the Enterprise's management of its liquidity position is insufficient. The Enterprise may evidence moderate weaknesses in funds management practices, or weaknesses that are not correctable in the normal course of business. The Enterprise may lack ready access to funds on reasonable terms. The Enterprise may not meet all regulatory guidance related to liquidity.

- **Weak**: The level of liquidity or the Enterprise's management of its liquidity position is weak. The Enterprise may not have or be able to obtain sufficient funds on reasonable terms. The Enterprise does not meet all regulatory guidance related to liquidity.

Interest Rate Risk

- **Strong**: Market risk sensitivity is well controlled and there is minimal potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are strong for the size, sophistication and market risk accepted by the Enterprise. Earnings and capital provide substantial support for the amount of market risk taken by the Enterprise.

- **Satisfactory**: Market risk sensitivity is satisfactorily controlled and there is moderate potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are satisfactory for the size, sophistication, and market risk accepted by the Enterprise. Earnings and capital provide adequate support for the amount of market risk taken by the Enterprise.

- **Insufficient**: Market risk sensitivity controls are insufficient or there is significant potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are insufficient given the size, sophistication, and market risk accepted by the Enterprise. Earnings and capital may not adequately support the amount of market risk taken by the Enterprise.

- **Weak**: Market risk sensitivity controls are weak or there is a high potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are weak for the size, sophistication, and market risk accepted by the Enterprise. Earnings and capital provide inadequate support for the amount of market risk taken by the Enterprise.

3(a). Residual Market Risk (Low, Moderate, High)

Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, and the overall risk rating. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Market Risk (Decreasing, Stable, Increasing)

The rating for direction of market risk should indicate the Enterprise's current level relative to prior ratings or reflect best information currently available (such as expected future risks based on current and past information).

Risk Type and Description	Risk Measures	Applicable FHFA Risk Management Standards and Guidance; Other Regulatory/Industry Issuances (*for information only*)

Risk Type	Inherent Risk	Risk Controls and Mitigants

1. Inherent operational risk: ☐ **Low** ☐ **Moderate** ☐ **High**
Summary:

2. Quality of operational risk management: ☐ **Strong** ☐ **Satisfactory** ☐ **Insufficient** ☐ **Weak**
Summary:

3(a). Residual operational risk: ☐ **Low** ☐ **Moderate** ☐ **High**
3(b). Direction of operational risk: ☐ **Decreasing** ☐ **Stable** ☐ **Increasing**
Summary:

Risk Measures

Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise. Examples of operational risk measures may be number and type of breaches; internal/external operational loss events; number and type of incidents; quality of third-parties; fraud exposures; vulnerability and patch management metrics; and number and types of suspicious activity reports (SARs) filed.

1. **Inherent Operational Risk** (Low, Moderate, High)

In general, operational risk is the potential that inadequate information systems, operational process failures, breaches in internal controls, fraud, or external events and unforeseen catastrophes will result in unexpected losses and this risk is present in all facets of the Enterprise's activity. When determining the level of inherent risk, examiners should consider the types of operational risks that are intrinsic in the entire Enterprise and those to significant business lines. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighted differently in contributing to the rating.

- **Low**: Operational loss events and control failures are expected to have little effect on the Enterprise's current or projected financial condition and resilience. The complexity of products and services, the volume of transaction processing, and the state of internal systems expose the Enterprise to minimal risk from fraud, errors, execution issues, or processing disruptions. The risks related to new products, outsourcing, accounting issues, technology changes, and external threats are minimal and well understood. Process and control breakdowns are rare and exceptions to risk appetite and limits are infrequent.

- **Moderate**: Operational loss events and control failures are expected to have a limited or manageable effect on the Enterprise's current or projected financial condition and resilience. The complexity of products and services, the volume of transaction processing, and the state of internal systems expose the Enterprise to increased risks from fraud, errors, execution issues, or processing disruptions. The risks related to new products, outsourcing, accounting issues, technology changes, and external threats are manageable. Process and control breakdowns and exceptions to risk appetite and limits are increasing.

- **High**: Operational loss events and control failures are expected to have a significant adverse effect on the Enterprise's current or projected financial condition and resilience. One significant loss or multiple large losses are more likely to materialize. The complexity of products and services, the volume of transaction processing, and the state of internal systems expose the Enterprise to significant risks from fraud, errors, execution issues, or processing disruptions. The risks related to new products, outsourcing, accounting issues, technology changes, and external threats are substantial and may not have been fully analyzed. Process and control breakdowns may be of significant concern. Exceptions to risk appetite and limits are frequent or routine.

2. Quality of Operational Risk Management (Strong, Satisfactory, Insufficient, Weak)

- **Strong:** Operational risk management is strong and the number and severity of operational risk events are low. There is minimal potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk.

- **Satisfactory**: Operational risk management is satisfactory and the number and severity of operational risk events are moderate. There is moderate potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk.

- **Insufficient**: Operational risk management is insufficient or there is significant potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk. The number and severity of operational risk events are moderate to serious.

- **Weak**: Operational risk management is weak or there is a high potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk. The number and severity of operational risk events are serious to critical.

3(a). Residual Operational Risk (Low, Moderate, High)

Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, and the overall risk rating. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Operational Risk (Decreasing, Stable, Increasing)

The rating for direction of operational risk should indicate the Enterprise's current level relative to prior ratings or reflect best information currently available (such as expected future risks based on current and past information).

Federal Housing Finance Agency

June 23, 2016

DIVISION OF ENTERPRISE REGULATION (DER)
OPERATING PROCEDURES BULLETIN

DER-OPB-02

QUALITY CONTROL REVIEWS

Purpose

This Operating Procedures Bulletin (OPB) sets forth the procedures that DER follows in implementing Supervision Directive (SD) 2013-01, March 25, 2103, *Quality Control Program for Examinations Conducted by the Division of Bank Regulation and the Division of Enterprise Regulation*. DER conducts independent Quality Control (QC) reviews of documentation for examination conclusions, findings, and closures of Matters Requiring Attention (MRAs) before written communication of such conclusions, findings, and closures to Fannie Mae and Freddie Mac (the Enterprises). DER staff ensures that issues identified in QC reviews are addressed and that QC review results are documented and maintained with examination files.

DER's QC reviews complement, but do not replace, existing management vetting and review of examination work products prepared in the execution of DER's supervision program. QC reviews are intended to (i) support greater consistency in documentation practices across DER branches, (ii) confirm that applicable DER and FHFA guidance is followed in preparation and storage of examination documentation, and (iii) ensure that input or review of relevant stakeholders is documented when examination activity involves multiple DER Offices.

Scope of QC Reviews

DER's QC process provides an independent review of certain examination work products to assess whether written communications to the Enterprises about examination findings and conclusions and MRA remediation activities are supported by documentation of examination work that meets DER standards and applicable FHFA guidance for preparation of written products. All Conclusion Letters (whether based on findings and conclusions from targeted examinations or ongoing monitoring) and Remediation Letters to the Enterprises should receive an independent QC review by staff outside of the team responsible for the written documents reviewed.

Certain written communications to the Enterprises are not subject to QC review following the procedures in this OPB, absent a specific request from the DER Deputy Director. These communications include letters from an EIC that announce the initiation of a targeted examination (*i.e.*, Request Letters), or communicate the EIC's non-objection or objection to an Enterprise remediation plan to address an MRA; and EIC approval of Enterprise-requested extension to expected remediation plan completion date. The Report of Examination (ROE) does not communicate conclusions, findings, or closures of MRAs, but reference prior communications to the Enterprises on conclusions, findings, or closures of MRAs. Therefore, ROEs are not subject to the QC process in this OPB and are vetted through a separate process.

QC reviews are completed prior to the review and approval of supervisory letters by DER's Deputy Director. QC reviews may only be waived by the DER Deputy Director, and DER's Office of Enterprise Supervision Operation, Oversight and Supervision Administration Branch (OSAB) must ensure that such waivers are documented in the QC review files.

QC Reviews

QC reviews should document the reviewer's assessment whether:

- Examination procedures appear reasonably consistent with the examination objectives and scope;
- Examination documentation adequately supports examination findings and conclusions to be communicated to the Enterprises; and
- Examination work products are consistent with DER standards and applicable Agency guidance for preparation of written products.

Staff performing DER QC reviews should have an understanding of FHFA examination procedures and guidance, should not have participated in the examination activity under review, and should not be assigned to the examination team for the Enterprise receiving the correspondence. OSAB is responsible for planning and leading DER QC reviews. Staff of other DER Offices may assist in performing reviews, provided the staff are independent as described above.

For each QC review, a QC review template should be completed, following review of draft correspondence and appropriate supporting documentation. QC reviewers should follow all instructions provided by OSAB for completing the appropriate templates.

Staff performing a QC review should (i) review all relevant documentation relating to the correspondence under review in light of DER guidance and Agency issuances relating to procedures for documenting examination activities; (ii) raise questions and apparent exceptions with the staff who prepared the documents for resolution, and (iii) ensure that the EIC has the QC results. QC results should be documented on the appropriate current approved QC review template prior to forwarding correspondence for review in the approval workflow. OESO will make available to staff performing QC reviews additional guidance and instructions for the approval workflow process.

Issues identified in a QC review relating to application and adherence to DER standards will be raised by QC reviewers for examiner consideration. Items of disagreement regarding application of guidance should be escalated to the appropriate Associate Director(s) and EIC as necessary to ensure prompt resolution of issues. OSAB should timely execute reviews and examination staff should timely respond to QC inquiries.

A completed QC template should accompany each draft Enterprise correspondence in the approval workflow and be stored with the examination workpapers. OSAB may periodically provide summary information to DER management regarding QC review results.

EFFECTIVE DATE

This OPB is effective immediately.

Nina A. Nichols

Nina A. Nichols, Deputy Director
Division of Enterprise Regulation

ATTACHMENT

STANDARDS FOR QC REVIEWS

DER QC reviews check that examination documentation is consistent with the following examination program-related standards and supervision policies:

- Examination Program Module
- DER Operating Procedures Bulletins
  - 2016-DER-OPB-01: Enterprise Supervision: Mid-Year Risk Assessments
  - 2014-DER-OPB-02: Use of the Work of the Enterprise's Internal Auditor (10/31/2014)
  - 2014-DER-OPB-01: Guidelines For Preparing Supervisory Products and Examination Workpapers (1/29/2014)
  - 2013-DER-OPB-01: Matters Requiring Attention Process (04/23/2013)
  - 2013-DER-OPB-02.1: Information Sharing of Counterparty Performance Issues (05/30/2013)
  - 2013-DER-OPB-03.1: Supervisory Planning Process (10/29/2013)
  - 2013-DER-OPB-04: DER Supervisory Activities (9/20/2013)
- FHFA Supervision Directives
  - SD 2013-01: Quality Control Policy (03/25/2013)
- FHFA Advisory Bulletins
  - AB-2012-01: Categories for Examination Findings (04/02/2012)
- DER Examination Documentation Templates

Additionally, QC reviews check that examination documentation is completed in accordance with FHFA guidance that is applicable to DER's supervision program, including:

- FHFA Comprehensive Records Schedule, as it pertains to records retention of examination and evaluation activities records; and supervision and oversight activities records; and,
- FHFA Style Guide.

Note: This list is not all-inclusive and may be revised as examination standards and FHFA policy revisions are approved. Refer to FHFA Intranet Guidance and Supervision Policies for the most updated list of examination standards and supervision policies.

Federal Housing Finance Agency

May 25, 2016

DIVISION OF ENTERPRISE REGULATION (DER) OPERATING PROCEDURES BULLETIN

DER-OPB-01

ENTERPRISE SUPERVISION: MID-YEAR RISK ASSESSMENTS

PURPOSE

DER's risk assessments are critical components of effective risk-based supervision of the Enterprises. Enterprise supervision staff's assessment of risks in key areas is a foundation for the annual examination plan for each Enterprise and a basis for evaluating the Enterprises' risk management in those areas and their overall safety and soundness.

This Operating Procedures Bulletin (OPB) sets forth procedures for the preparation, approval, and documentation of mid-year risk assessments. The procedures include formats to improve consistency of definitions and use of key terms and risk measures. While the assessment of risk by supervision staff is an ongoing process, specific documentation and approval requirements apply to the mid-year risk assessment, as described in this OPB.

This OPB supersedes Supervision Directive SD-2013-02 (*Division of Enterprise Regulation: Periodic Risk Assessments)* (December 3, 2013).

GUIDANCE

The Examiner-in-Charge (EIC) at each Enterprise annually assigns a composite rating and component ratings to the Enterprise in accordance with FHFA's Examination Rating System (AB 2012-03, December 19, 2012). The ratings are assigned as of December 31 each year and are included in the annual report of examination (ROE), which includes the examination work and findings for the calendar year. The ratings and ROE must be approved by the Deputy Director, DER, and they are transmitted to the Enterprise's board of directors in the first quarter of the following calendar year.

Each EIC is responsible for risk assessment for their respective Enterprise, and the overall risk assessment supports the composite rating and component ratings of each Enterprise. The EIC completes the mid-year risk assessment, with documentation to be finalized and approved in accordance with DER's standard workflow approval practices by September 30. Documentation of the mid-year risk assessment must include credit, market, and operational risk components in the templates included as attachments to this OPB, and may include other risk elements, as determined by the EIC. For example, the EIC's risk assessment may include information relating to governance, model risk management, compliance, or internal control for financial reporting.

The EIC may update the risk assessment as appropriate to address developments that affect the Enterprise's current or projected financial condition or resilience. A mid-year risk assessment may be referenced to support a change to an assigned rating. Any changes to a rating must be approved by the Deputy Director, DER, and must be communicated in writing to the board of directors of the Enterprise.

The risk assessment informs Enterprise supervision in various ways. In addition to providing the EIC with a tool for review of the ratings, it is available to the examiners in preparing examination plans and in performing examination activities (for example, developing scope and procedures documents). The risk assessment may also inform risk and policy analysts in the development of guidance and supervisory expectations for risk management by the Enterprises.

Risk assessments must include input from the respective executive heading the Office of Model, Credit and Market Risk (OMCMR) and the Office of Governance, Compliance and Operational Risk (OGCOR) about credit, market, or operational risks. Input must be provided on Part One of the attached templates in accordance with template instructions. Part One includes descriptions of risks, relevant quantitative and qualitative measures, and applicable or relevant risk management standards or sound practices. Completed Part One of each template should be provided to the EIC following the issuance of the ROE and no later than June 30.

The EIC for each Enterprise is responsible for completion of Part Two of the credit, market, and operational risk templates in accordance with template instructions. Part Two of the templates and instructions provide for documentation of the EIC's conclusions on the overall inherent risk rating (low, moderate, high) for credit, market, and operational risk; the quality of risk management (strong, satisfactory, insufficient, weak); residual risk (low, moderate, high); and the direction of risk (decreasing, stable, increasing). There are also executive-level summaries supporting the EIC's conclusions for inherent risk, quality of risk management, residual risk, and direction of risk.

The completed mid-year risk assessment for each Enterprise must include Parts One and Two of the credit, market, and operational risk templates and any additional information as determined by the EIC. Each mid-year risk assessment must be sent through a DER standard workflow for review and documentation of approval by the appropriate EIC, the executives heading OMCMR and OGCOR, and the Deputy Director, DER. The approved mid-year risk assessments must be maintained in the appropriate folders.

EFFECTIVE DATE

This OPB is effective immediately. The mid-year risk assessment templates and related instructions are effective immediately, and may be updated periodically.

Nina A. Nichols, Deputy Director
Division of Enterprise Regulation

ATTACHMENTS:

Mid-Year Risk Assessments: General Instructions
Mid-Year Risk Assessments:
- Credit Risk template and instructions
- Market Risk template and instructions
- Operational Risk template and instructions

Division of Enterprise Regulation
Mid-Year Risk Assessment
General Instructions for Credit, Market, and Operational Risk Templates

General Instructions

Pursuant to operating procedures of the Division of Enterprise Regulation (DER), the Examiners-in-Charge (EICs) of Fannie Mae and Freddie Mac (the Enterprises) prepare mid-year risk assessments for the Enterprises. See DER-OPB-01 (*Enterprise Supervision: Mid-Year Risk Assessments*) (May 25, 2016). Each mid-year risk assessment must include a completed template for credit, market, and operational risk. Each template comprises a risk analysis section (Part One) and a risk assessment section (Part Two). The mid-year risk assessment for each Enterprise must be submitted in a workflow for formal approvals and documentation by the EIC, the executives heading the DER Offices of Model, Credit and Market Risk (OMCMR) and Governance, Compliance and Operational Risk (OGCOR), and the Deputy Director, DER, by September 30. The final risk assessment must be saved in the appropriate folder.

The risk assessment should be based on current information about Enterprise operations and risks. The conclusions derived through the risk assessment process will be used to support development of the examination plan. The EICs may consider the information presented and any knowledge gaps in determining whether amendments to the risk-based examination plans are necessary.

Part One: Risk Analysis

The executives heading OMCMR and OGCOR are responsible for providing input for analysis of credit, market, and operational risks to the EICs. The completed Part One of each template should be provided to the EICs as soon as practicable following the issuance of the report of examination and no later than June 30.

Risk Type and Description: The risk analysis section provides more detailed information about risks, that is, the potential that events will have an adverse effect on the Enterprise's current or projected financial condition or resilience. Part One includes identification and description of particular risks to be considered. Descriptions should include an explanation of how risks could affect the Enterprises' financial condition or resilience.

Risk Measures: Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise.

- Credit risk measures include metrics for assessing credit quality of Enterprise assets, for quantifying the probability and size of potential credit losses associated with borrower and counterparty default risk, and for assessing an Enterprise's process for determining the level of reserves needed in the event of credit losses.

- Market risk measures include metrics for assessing an Enterprise's ability to meet its financial obligations and its vulnerability of current and future earnings and capital to interest rate changes.

- Operational risk measures include metrics for assessing the quantity of operational risk and the quality of operational risk management.

<u>Risk Management Standards and Guidance</u>: Part One of each template includes references to (or summaries of, as appropriate) relevant and applicable FHFA risk management standards and guidance. Guidance of other regulators or controls that represent industry sound practices may be referenced or described for information, although they do not establish risk management criteria of FHFA.

Part Two: Risk Assessment

Each EIC is responsible for completion of Part Two of each template, an Enterprise-specific assessment for credit, market, or operational risk.

<u>Risk Type</u>: Each Enterprise-specific template should include in Part Two under "Risk Type" applicable risks identified and described in Part One. If additional risk types are added, descriptions should be provided.

<u>Risk Levels:</u>

1. Inherent Risk (Low, Moderate, High)

Inherent risks are those internal or external risks to which the Enterprise is exposed, knowingly or unknowingly, as a result of the business activities in which it engages, and the external environment in which the activities take place. The summary should discuss which risk types are inherently manifested at the Enterprise and how, but should not include commentary relating to controls and risk management.

- **High inherent risk** exists where there is potential for a significant and harmful loss. In general, indicia of high risk are present when positions are very large in relation to the Enterprise's resources, where there are a substantial number of transactions, where the nature of the activity is unusual, and/or where metrics are difficult to define or model.

- **Moderate inherent risk** exists where potential losses, though present, could likely be absorbed by the Enterprise in the normal course of business. In general, indicia of moderate risk are present when the volume of transactions is not large in relation to the Enterprise's resources, where activity is routine, and/or where reliable metrics are readily available.

- **Low inherent risk** exists where if a loss were to occur it would have an inconsequential material negative impact on the Enterprise. In general, indicia of low inherent risk are present when the volume, size, or nature of the activity is such that, even if the internal controls have weaknesses, the risk of loss is remote.

2. Quality of Risk Management (Strong, Satisfactory, Insufficient, Weak)

Part Two includes a discussion of the risk management practices and controls implemented by the Enterprise to manage the specific risks identified. Information about risk controls may include effectiveness of board and senior management oversight; policies, procedures, and limits; risk monitoring and management information systems; and internal controls. Part Two includes an assessment of the quality of risk management (strong, satisfactory, insufficient, weak) and summary of analysis. In general, the characteristics of risk management practices outlined by the CAMELSO rating system inform the assessment of the quality of risk management, including how an Enterprise identifies, measures, controls, and monitors risks.

3(a). Residual Risk (Low, Moderate, High)

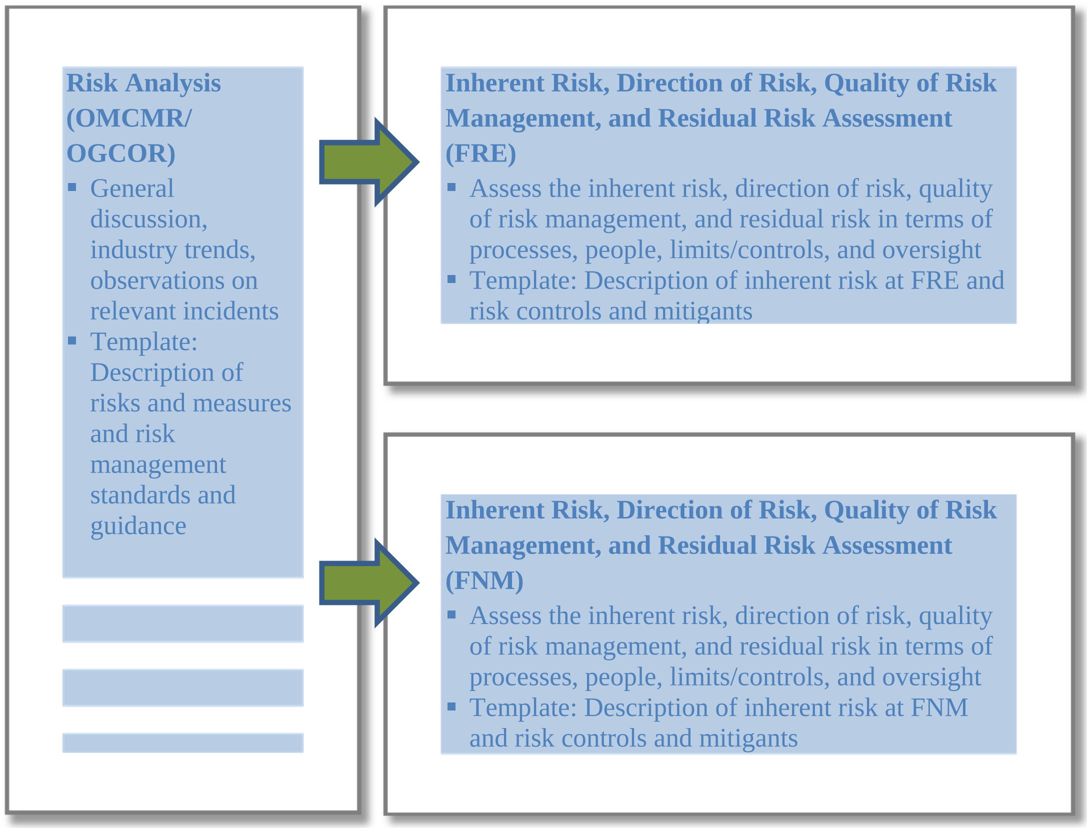
Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, as well as summary observations for the risk area. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Risk (Decreasing, Stable, Increasing)

Part Two includes a prospective assessment of the probable movement in inherent risk over the next 12 months, characterized as decreasing, stable, or increasing. An assessment of "decreasing" indicates that the EIC expects, based on current or best available information, that inherent risk will decline over the next 12 months. If risk is stable, the EIC expects inherent risk to remain unchanged. If risk is increasing, the EIC expects inherent risk to be higher in 12 months.

An expectation that inherent risk will increase or decrease does not necessarily mean that the movement is expected to be sufficiently large to change the inherent risk level within 12 months. An EIC can expect movement within the risk level. For example, inherent risk can be high and decreasing even though the decline is not anticipated to change the level of inherent risk to moderate. In such circumstances, the summary should indicate why a change in the risk level is not expected.

Mid-Year Risk Assessment Process Flow



Risk Type and Description	Risk Measures	Applicable FHFA Risk Management Standards and Guidance; Other Regulatory/Industry Issuances (*for information only*)

Risk Type	Inherent Risk	Risk Controls and Mitigants

1. Inherent credit risk: ☐ **Low** ☐ **Moderate** ☐ **High**
Summary:

2. Quality of credit risk management: ☐ **Strong** ☐ **Satisfactory** ☐ **Insufficient** ☐ **Weak**
Summary:

3(a). Residual credit risk: ☐ **Low** ☐ **Moderate** ☐ **High**
3(b). Direction of credit risk: ☐ **Decreasing** ☐ **Stable** ☐ **Increasing**
Summary:

Risk Measures

Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise. Examples of credit risk measures may include measures of credit portfolio quality; single-family mortgage performance, delinquency indicators, and loss rate data; multifamily mortgage performance and delinquency indicators; allowance for loan losses (*e.g.,* allowance level, charge-offs, recovery, coverage ratios, asset classifications based on mortgage performance and borrower characteristics); concentration levels; loss-mitigation measures; defect rates; and measures of counterparty risk and exposure.

1. **Inherent Credit Risk** (Low, Moderate, High)

In general, credit risk is the potential that a borrower or counterparty will fail to meet its obligations in accordance with agreed terms. Credit risk includes the decline in measured quality of a credit exposure that might result in increased capital costs, provisioning expenses, and a reduction in economic return. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighed differently in contributing to the rating.

- **Low:** Current or prospective credit risk of loss of earnings or capital is minimal. Credit risk reflects conservative risk selection, underwriting, and structures. The volume of substantive exceptions or overrides to underwriting standards poses minimal risk. Credit risk represents a well-diversified distribution by credit quality of borrower and borrower leverage. Risk of loss from concentrations is minimal. There is limited sensitivity due to deteriorating economic, industry, competitive, regulatory, and technological factors. Portfolio growth presents minimal concern and new initiatives are conservative. Refinancing practices are sound and pose minimal increased risk. The volume of troubled credits is low and can be resolved in the normal course of business. Credit-related losses do not meaningfully affect current reserves and result in modest provisions relative to earnings.

- **Moderate:** Current or prospective credit risk of loss of earnings or capital does not materially affect financial condition. Credit risk reflects acceptable risk selection, underwriting, and structures. Substantive exceptions or overrides to underwriting standards pose minimal risk. There are limited declines in borrower credit quality or increases in borrower leverage. Credit risk does not reflect significant concentrations. Vulnerability may exist due to deteriorating economic, industry, competitive, regulatory, and technological factors. While advanced portfolio growth may exist within specific products or sectors, it is in accordance with a reasonable plan. Refinancing practices are satisfactory. The volume of troubled credits does not pose undue risk relative to capital and can be resolved within realistic time frames. Credit-related losses do not seriously deplete current reserves or necessitate large provisions relative to earnings.

- **High:** Current or prospective credit risk of loss of earnings or capital is material. Credit risk reflects aggressive risk selection, underwriting, and structures. A large volume of substantive exceptions or overrides to sound underwriting standards exists. Credit risk is skewed toward lower credit quality borrower or highly leveraged borrowers. Credit risk reflects significant concentrations. Significant vulnerability exists due to deteriorating economic, industry, competitive, regulatory, and technological factors. Portfolio growth, including products or sectors within the portfolio, is aggressive. Refinancing practices reflect a significant deviation from current underwriting standards. The volume of troubled borrowers may be large and require an extended time to resolve. Credit-related losses may seriously deplete current reserves or necessitate large provisions.

2. Quality of Credit Risk Management (Strong, Satisfactory, Insufficient, Weak)

- **Strong**: Asset quality and credit risk management practices are strong. Any identified weaknesses are minor in nature and risk exposure is minimal in relation to the Enterprise's capital protection and management's ability to identify, monitor, and mitigate risks.

- **Satisfactory**: Asset quality and credit risk management practices are satisfactory. Identified weaknesses, such as the level and severity of adversely-rated or classified assets, are moderate and in line with the Enterprise's capital protection and management's ability to identify, monitor, and mitigate risks.

- **Insufficient**: Asset quality or credit risk management practices are insufficient. Identified weaknesses, such as the level and severity of adversely-rated or classified assets, are significant and not in line with the Enterprise's capital protection or management's ability to identify, monitor, and mitigate risks.

- **Weak**: Asset quality or credit risk management practices are weak. Identified weaknesses, such as the level of problem assets are significant and inadequately controlled. The weaknesses subject the Enterprise to significant potential losses.

3(a). Residual Credit Risk (Low, Moderate, High)

Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, and the overall risk rating. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Credit Risk (Decreasing, Stable, Increasing)

The rating for direction of credit risk should indicate the Enterprise's current level relative to prior ratings or reflect best information currently available (such as expected future risks based on current and past information).

Risk Type and Description	Risk Measures	Applicable FHFA Risk Management Standards and Guidance; Other Regulatory/Industry Issuances (*for information only)*

Risk Type	Inherent Risk	Risk Controls and Mitigants

1. Inherent market risk: ☐ **Low** ☐ **Moderate** ☐ **High**
Summary:

2. Quality of market risk management: ☐ **Strong** ☐ **Satisfactory** ☐ **Insufficient** ☐ **Weak**
Summary:

3(a). Residual market risk: ☐ **Low** ☐ **Moderate** ☐ **High**
3(b). Direction of market risk: ☐ **Decreasing** ☐ **Stable** ☐ **Increasing**
Summary:

Risk Measures

Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise. Examples of market risk measures may include duration gap; convexity gap; implied volatility; option adjusted spread; portfolio market value sensitivity (parallel shocks); portfolio market sensitivity (non-parallel shocks); key rate duration; prepayment duration; spread duration; percent of agency MBS securities in retained portfolio; percent of whole loans in portfolio; percent of private label securities in portfolio; percent of distressed assets in portfolio; bid/ask spreads funding ladder- debt maturity schedule; surplus days cash (base case and stressed); short term debt/long term debt ratio; coverage ratio; callable debt to bullet debt ratio; agency/swap basis; and maturity liquidity investments portfolio.

1. **Inherent Market Risk** (Low, Moderate, High)

Overall inherent market risk should reflect all types of market risk but specifically liquidity and interest rate risk. The aggregate of all market risks will be given a level of low, moderate, or high.

Liquidity

Liquidity risk is the risk that an Enterprise is unable to meet its financial obligations as they come due or meet the credit needs of its customers in a timely and cost-efficient manner. The Enterprises must be financially sound to perform their public missions and should have a comprehensive liquidity risk management framework to limit and control liquidity risk exposures. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighed differently in contributing to the rating.

- **Low:** The Enterprise is not vulnerable to funding difficulties should a material adverse change in market perception occur. Exposure from the liquidity risk profile is negligible. Ample funding sources and the cash flows for assets and liabilities (with derivatives) match in all tenors.

- **Moderate:** The Enterprise is not excessively vulnerable to funding difficulties should a material adverse change in market perception occur. Exposure from the liquidity risk profile is manageable. Sources of funding are reasonably diverse but minor concentrations may exist. Some groups of providers may share common investment objectives or be subject to similar economic influences. Sufficient funding sources and matching asset and liability cash flows exist to provide stable, cost-effective liquidity in most environments, without significant disruption in strategic lines of business.

- **High:** The Enterprise's liquidity profile makes it vulnerable to funding difficulties should a material adverse change occur. Significant concentrations of funding may exist. Large funds providers may share common investment objectives or be subject to similar economic influences. Funding sources and balance-sheet structures may currently result in, or suggest, potential difficulty in sustaining long-term liquidity on a cost-effective basis. Potential exposure due to high liability costs or unplanned asset reduction may be substantial. Liquidity needs may trigger the necessity for funding alternatives under a contingency funding plan (CFP), including the sale of, or disruption in, a strategic line of business.

Interest Rate Risk

Interest rate risk is the vulnerability of current or future earnings and capital to interest rate changes. Fluctuations in interest rates affect earnings by altering interest-sensitive income and expenses. Interest rate changes also affect capital by changing the net present value (NPV) of future cash flows and the cash flows themselves. Excessive interest rate risk can threaten liquidity, earnings, capital, and solvency.

In general, the regulated entities manage interest rate risk with a combination of swapped and unswapped callable and non-callable debt, fixed- and floating-rate bullet debt, and derivative instruments. They use derivatives to limit downside earnings exposures, preserve upside earnings potential, increase yield, and minimize income or capital volatility. When used properly, derivatives are an effective risk management tool, but improper usage can allow interest rate changes to have a sudden and significant effect on the regulated entity's financial position. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighed differently in contributing to the rating.

- **Low**: Exposure reflects minimal repricing, basis, yield curve, and options risk. Positions used to manage interest rate risk exposure are well-correlated to underlying risks. No significant mismatches on longer-term positions exist. Interest rate movements would have minimal adverse effect on the financial performance of the Enterprise. The Enterprise is not exposed to material losses as a result of changes in market prices. Enterprise assets and liabilities that do not offset each other are accounted for at fair value (*e.g.*, lending pipelines and mortgage servicing rights).

- **Moderate**: Exposure reflects manageable repricing, basis, yield curve, and options risk. Positions used to manage interest rate risk exposure are somewhat correlated. Mismatches on longer-term positions exist but are managed. Interest rate movements would not have a significant adverse effect on the financial performance of the Enterprise. The Enterprise has access to a variety of risk management instruments and markets at reasonable costs, given the size, tenor, and complexity of open positions. Assets and liabilities that do not offset each other are accounted for at fair value (*e.g.*, lending pipelines and mortgage servicing rights) and are unlikely to materially affect the Enterprise's financial condition.

- **High**: Exposure reflects significant repricing, basis, yield curve, or options risk. Positions used to manage interest rate risk exposure are poorly correlated. Significant mismatches on longer-term positions exist. Interest rate movements could have a significant adverse effect on the financial performance of the Enterprise. A significant volume of assets and liabilities that do not offset each other are accounted for at fair value (*e.g.*, derivatives, lending pipelines, and mortgage servicing rights), and valuation changes have significant potential to adversely affect the Enterprise's condition.

2. Quality of Market Risk Management (Strong, Satisfactory, Insufficient, Weak)

The overall quality of market risk management should reflect all types of market risk but specifically the qualities of risk management below. The aggregate of all market risk management will be given a level of strong, satisfactory, insufficient, or weak.

Liquidity

- **Strong**: The level of liquidity and the Enterprise's management of its liquidity position are strong. Any identified weaknesses in its liquidity management practices are minor. The Enterprise has reliable access to sufficient sources of funds on favorable terms to meet current and anticipated liquidity needs. The Enterprise meets or exceeds regulatory guidance related to liquidity.

- **Satisfactory**: The level of liquidity and the Enterprise's management of its liquidity position are satisfactory. The Enterprise may have moderate weaknesses in its liquidity management practices, but these are correctable in the normal course of business. The Enterprise has reliable access to sufficient sources of funds on acceptable terms to meet current and anticipated liquidity needs. The Enterprise meets or exceeds regulatory guidance related to liquidity.

- **Insufficient**: The level of liquidity or the Enterprise's management of its liquidity position is insufficient. The Enterprise may evidence moderate weaknesses in funds management practices, or weaknesses that are not correctable in the normal course of business. The Enterprise may lack ready access to funds on reasonable terms. The Enterprise may not meet all regulatory guidance related to liquidity.

- **Weak**: The level of liquidity or the Enterprise's management of its liquidity position is weak. The Enterprise may not have or be able to obtain sufficient funds on reasonable terms. The Enterprise does not meet all regulatory guidance related to liquidity.

Interest Rate Risk

- **Strong**: Market risk sensitivity is well controlled and there is minimal potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are strong for the size, sophistication and market risk accepted by the Enterprise. Earnings and capital provide substantial support for the amount of market risk taken by the Enterprise.

- **Satisfactory**: Market risk sensitivity is satisfactorily controlled and there is moderate potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are satisfactory for the size, sophistication, and market risk accepted by the Enterprise. Earnings and capital provide adequate support for the amount of market risk taken by the Enterprise.

- **Insufficient**: Market risk sensitivity controls are insufficient or there is significant potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are insufficient given the size, sophistication, and market risk accepted by the Enterprise. Earnings and capital may not adequately support the amount of market risk taken by the Enterprise.

- **Weak**: Market risk sensitivity controls are weak or there is a high potential that the Enterprise's earnings performance or capital position will be adversely affected by market risk sensitivity. Risk management practices are weak for the size, sophistication, and market risk accepted by the Enterprise. Earnings and capital provide inadequate support for the amount of market risk taken by the Enterprise.

3(a). Residual Market Risk (Low, Moderate, High)

Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, and the overall risk rating. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Market Risk (Decreasing, Stable, Increasing)

The rating for direction of market risk should indicate the Enterprise's current level relative to prior ratings or reflect best information currently available (such as expected future risks based on current and past information).

Risk Type and Description	Risk Measures	Applicable FHFA Risk Management Standards and Guidance; Other Regulatory/Industry Issuances (*for information only*)

Risk Type	Inherent Risk	Risk Controls and Mitigants

1. Inherent operational risk: ☐ **Low** ☐ **Moderate** ☐ **High**
Summary:

2. Quality of operational risk management: ☐ **Strong** ☐ **Satisfactory** ☐ **Insufficient** ☐ **Weak**
Summary:

3(a). Residual operational risk: ☐ **Low** ☐ **Moderate** ☐ **High**
3(b). Direction of operational risk: ☐ **Decreasing** ☐ **Stable** ☐ **Increasing**
Summary:

Risk Measures

Part One identifies potential qualitative and quantitative measures useful in assessing the magnitude of a particular risk and how it could affect an Enterprise. Examples of operational risk measures may be number and type of breaches; internal/external operational loss events; number and type of incidents; quality of third-parties; fraud exposures; vulnerability and patch management metrics; and number and types of suspicious activity reports (SARs) filed.

1. **Inherent Operational Risk** (Low, Moderate, High)

In general, operational risk is the potential that inadequate information systems, operational process failures, breaches in internal controls, fraud, or external events and unforeseen catastrophes will result in unexpected losses and this risk is present in all facets of the Enterprise's activity. When determining the level of inherent risk, examiners should consider the types of operational risks that are intrinsic in the entire Enterprise and those to significant business lines. The inherent risk rating should take into account all risk types identified and described on the template (absent controls and mitigants). Risk types may be weighted differently in contributing to the rating.

- **Low**: Operational loss events and control failures are expected to have little effect on the Enterprise's current or projected financial condition and resilience. The complexity of products and services, the volume of transaction processing, and the state of internal systems expose the Enterprise to minimal risk from fraud, errors, execution issues, or processing disruptions. The risks related to new products, outsourcing, accounting issues, technology changes, and external threats are minimal and well understood. Process and control breakdowns are rare and exceptions to risk appetite and limits are infrequent.

- **Moderate**: Operational loss events and control failures are expected to have a limited or manageable effect on the Enterprise's current or projected financial condition and resilience. The complexity of products and services, the volume of transaction processing, and the state of internal systems expose the Enterprise to increased risks from fraud, errors, execution issues, or processing disruptions. The risks related to new products, outsourcing, accounting issues, technology changes, and external threats are manageable. Process and control breakdowns and exceptions to risk appetite and limits are increasing.

- **High**: Operational loss events and control failures are expected to have a significant adverse effect on the Enterprise's current or projected financial condition and resilience. One significant loss or multiple large losses are more likely to materialize. The complexity of products and services, the volume of transaction processing, and the state of internal systems expose the Enterprise to significant risks from fraud, errors, execution issues, or processing disruptions. The risks related to new products, outsourcing, accounting issues, technology changes, and external threats are substantial and may not have been fully analyzed. Process and control breakdowns may be of significant concern. Exceptions to risk appetite and limits are frequent or routine.

2. Quality of Operational Risk Management (Strong, Satisfactory, Insufficient, Weak)

- **Strong:** Operational risk management is strong and the number and severity of operational risk events are low. There is minimal potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk.

- **Satisfactory**: Operational risk management is satisfactory and the number and severity of operational risk events are moderate. There is moderate potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk.

- **Insufficient**: Operational risk management is insufficient or there is significant potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk. The number and severity of operational risk events are moderate to serious.

- **Weak**: Operational risk management is weak or there is a high potential that the Enterprise's earnings performance or capital position will be adversely affected by the level of operational risk. The number and severity of operational risk events are serious to critical.

3(a). Residual Operational Risk (Low, Moderate, High)

Terms have the same descriptions as for inherent risk. The rating for residual risk should take into account the risk types identified and described on the template, and the overall risk rating. Risk types may be weighed differently in how they affect the rating. The residual risk rating should also take into account the quality of risk management, controls, and mitigants.

3(b). Direction of Operational Risk (Decreasing, Stable, Increasing)

The rating for direction of operational risk should indicate the Enterprise's current level relative to prior ratings or reflect best information currently available (such as expected future risks based on current and past information).