Description of document: **Four Department of the Treasury Office of Thrift Supervision (OTS) reports to Congress, 2006 - 2009**

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Source of document: The Office of Thrift Supervision
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Office of Thrift Supervision
Department of the Treasury
1700 G Street, N.W., Washington, DC 20552 • (202) 906-6000

January 28, 2010

VIA ELECTRONIC MAIL

Re: FOIA No. 10-113

This is in response to your request, sent by first class mail and received in this office on November 24, 2009, for processing under the Freedom of Information Act ("FOIA"), 5 U.S.C. § 552. You requested a copy of each report produced for Congress by the Office of Thrift Supervision ("OTS") during the past three years, and which are not posted on the OTS public internet website.

Your request is granted in full. Enclosed are four reports to Congress, which are in addition to the three reports that are currently posted on the OTS website.

If you have any questions, please feel free to call me at (202) 906-6467 or e-mail me at marilyn.burton@ots.treas.gov.

Sincerely,

Marilyn K. Burton
Supervisory Paralegal Specialist

Enclosures

Office of Thrift Supervision
Department of the Treasury
1700 G Street, N.W., Washington, DC 20552 • (202) 906-6590

John M. Reich
Director

APR 10 2006

The Honorable John Dugan
Comptroller of the Currency
Office of the Comptroller of the Currency
Independence Square
250 E Street, S.W.
Washington, DC 20219

Dear Mr. Dugan:

The purpose of this letter is to notify you of the details of the Office of Thrift Supervision's 2006 compensation plan, as required by section 1206 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Based on consultations with the other federal banking regulatory agencies, we implemented the following in our compensation plan for 2006.

- An average merit budget of 5 percent of actual aggregate salaries.
- Payout of the merit budget to employees as a pay adjustment from within a range depending on the rating level of the employee.
- The maximum of the base salary range was increased by 3 percent.
- Geographic differentials adjusted for changes in the costs of goods and services for OTS duty locations.

If you desire further information, please do not hesitate to contact Kevin Petrasic, Managing Director of External Affairs, on (202) 906-6288.

Sincerely,

John M. Reich

Office of Thrift Supervision
Department of the Treasury
1700 G Street, N.W., Washington, DC 20552 • (202) 906-6590

John M. Reich
Director

MAR 20 2007

The Honorable Nancy Pelosi
Speaker of the House
U.S. House of Representatives
Washington, DC 20515

Dear Madam Speaker:

The purpose of this letter is to notify you of the details of the Office of Thrift Supervision's 2007 compensation plan, as required by section 1206 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Based on consultations with the other federal banking regulatory agencies, we implemented the following in our compensation plan for 2007.

- An average merit budget of 5 percent of actual aggregate salaries.
- Payout of the merit budget to employees from within a range depending on the rating level of the employee.
- No adjustments were made to the salary ranges.

If you desire further information, please do not hesitate to contact Kevin Petrasic, Managing Director of External Affairs, on (202) 906-6288.

Sincerely,

John M. Reich

Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency
Office of Thrift Supervision

April 11, 2007

The Honorable Richard C. Shelby
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Senator:

We are pleased to transmit the enclosed report on differences in accounting and capital standards among the federal banking agencies. This is the fifth joint annual report on the topic prepared by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision (collectively, "the federal banking agencies") as required by section 37(c) of the Federal Deposit Insurance Act (12 U.S.C. 1831n(c)), as amended.

The report describes the differences among the federal banking agencies' accounting and capital standards as of December 31, 2006. The report will be published in the Federal Register. If you or members of your staff have questions regarding this report, please do not hesitate to contact us.

Sincerely,

Randall S. Kroszner, Governor
Board of Governors of the
Federal Reserve System

Sheila C. Bair, Chairman
Federal Deposit Insurance Corporation

John C. Dugan
Comptroller of the Currency

John M. Reich, Director
Office of Thrift Supervision

Enclosure

REPORT TO THE COMMITTEE ON FINANCIAL SERVICES
OF THE UNITED STATES HOUSE OF REPRESENTATIVES
AND TO THE COMMITTEE ON BANKING, HOUSING,
AND URBAN AFFAIRS OF THE UNITED STATES SENATE
REGARDING DIFFERENCES IN ACCOUNTING AND
CAPITAL STANDARDS AMONG THE
FEDERAL BANKING AGENCIES

Introduction

The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS) ("the federal banking agencies" or "the agencies") must jointly submit an annual report to the Committee on Financial Services of the U.S. House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate describing differences between the accounting and capital standards used by the agencies. The report must be published in the *Federal Register*.

This report, which covers differences existing as of December 31, 2006, is the fifth joint annual report on differences in accounting and capital standards to be submitted pursuant to Section 37(c) of the Federal Deposit Insurance Act (12 U.S.C. 1831n(c)), as amended. Prior to the agencies' first joint annual report, Section 37(c) required a separate report from each agency.

Since the agencies filed their first reports on accounting and capital differences in 1990, the agencies have acted in concert to harmonize their accounting and capital standards and eliminate as many differences as possible. Section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994 (12 U.S.C. 4803) also directed the agencies to work jointly to make uniform all regulations and guidelines implementing common statutory or supervisory policies. The results of these efforts must be "consistent with the principles of safety and soundness, statutory law and policy, and the public interest." In recent years, the agencies have revised their capital standards to address changes in credit and certain other risk exposures within the banking system and to align the amount of capital institutions are required to hold more closely with the credit risks and certain other risks to which they are exposed. These revisions have been made in a uniform manner whenever possible and practicable to minimize interagency differences.

While the differences in capital standards have diminished over time, a few differences remain. Some of the remaining capital differences are statutorily mandated. Others were significant historically but now no longer affect in a measurable way, either individually or in the aggregate, institutions supervised by the federal banking agencies. In this regard, the OTS plans to eliminate two such de minimis differences during 2007 that have been fully discussed in previous joint annual reports ((i) covered assets and (ii) pledged deposits, nonwithdrawable accounts, and certain certificates), and these differences have been excluded from this annual report.

In addition to the specific differences in capital standards noted below, the agencies may have differences in how they apply certain aspects of their rules. These differences usually arise as a result of case-specific inquiries that have only been presented to one agency. Agency staffs seek to minimize these occurrences by coordinating responses to the fullest extent reasonably practicable.

The federal banking agencies have substantially similar capital adequacy standards. These standards employ a common regulatory framework that establishes minimum leverage and risk-based capital ratios for all banking organizations (banks, bank holding companies, and savings associations). The agencies view the leverage and risk-based capital requirements as minimum standards, and most institutions are expected to operate with capital levels well above the minimums, particularly those institutions that are expanding or experiencing unusual or high levels of risk.

The OCC, the FRB, and the FDIC, under the auspices of the Federal Financial Institutions Examination Council, have developed uniform Reports of Condition and Income (Call Reports) for all insured commercial banks and state-chartered savings banks. The OTS requires each OTS-supervised savings association to file the Thrift Financial Report (TFR). The reporting standards for recognition and measurement in the Call Reports and the TFR are consistent with U.S. generally accepted accounting principles (GAAP). Thus, there are no significant differences in regulatory accounting standards for regulatory reports filed with the federal banking agencies. Only one minor difference remains between the accounting standards of the OTS and those of the other federal banking agencies, and that difference relates to push-down accounting, as more fully explained below.

Differences in Capital Standards Among the Federal Banking Agencies

Financial Subsidiaries

The Gramm-Leach-Bliley Act (GLBA) establishes the framework for financial subsidiaries of banks.[1] GLBA amends the National Bank Act to permit national banks to conduct certain expanded financial activities through financial subsidiaries. Section 121(a) of the GLBA (12 U.S.C. 24a) imposes a number of conditions and requirements upon national banks that have financial subsidiaries, including specifying the treatment that applies for regulatory capital purposes. The statute requires that a national bank deduct from assets and tangible equity the aggregate amount of its equity investments in financial subsidiaries. The statute further requires

[1] A national bank that has a financial subsidiary must satisfy a number of statutory requirements in addition to the capital deduction and deconsolidation requirements described in the text. The bank (and each of its depository institution affiliates) must be well capitalized and well managed. Asset size restrictions apply to the aggregate amount of assets of all of the bank's financial subsidiaries. Certain debt rating requirements apply, depending on the size of the national bank. The national bank is required to maintain policies and procedures to protect the bank from financial and operational risks presented by the financial subsidiary. It is also required to have policies and procedures to preserve the corporate separateness of the financial subsidiary and the bank's limited liability. Finally, transactions between the bank and its financial subsidiary generally must comply with the Federal Reserve Act's (FRA) restrictions on affiliate transactions and the financial subsidiary is considered an affiliate of the bank for purposes of the anti-tying provisions of the Bank Holding Company Act. *See* 12 U.S.C. § 5136A.

that the financial subsidiary's assets and liabilities not be consolidated with those of the parent national bank for applicable capital purposes.

State member banks may have financial subsidiaries subject to all of the same restrictions that apply to national banks.[2] State nonmember banks may also have financial subsidiaries, but they are subject only to a subset of the statutory requirements that apply to national banks and state member banks.[3] Finally, national banks, state member banks, and state nonmember banks may not establish or acquire a financial subsidiary or commence a new activity in a financial subsidiary if the bank, or any of its insured depository institution affiliates, has received a less than satisfactory rating as of its most recent examination under the Community Reinvestment Act.[4]

The OCC, the FDIC, and the FRB adopted final rules implementing their respective provisions of Section 121 of GLBA for national banks in March 2000, for state nonmember banks in January 2001, and for state member banks in August 2001. GLBA did not provide new authority to OTS-supervised savings associations to own, hold, or operate financial subsidiaries, as defined.

Subordinate Organizations Other Than Financial Subsidiaries

Banks supervised by the OCC, the FRB, and the FDIC generally consolidate all significant majority-owned subsidiaries other than financial subsidiaries for regulatory capital purposes. This practice assures that capital requirements are related to the aggregate credit (and, where applicable, market) risks to which the banking organization is exposed. For subsidiaries other than financial subsidiaries that are not consolidated on a line-for-line basis for financial reporting purposes, joint ventures, and associated companies, the parent banking organization's investment in each such subordinate organization is, for risk-based capital purposes, deducted from capital or assigned to the 100 percent risk-weight category, depending upon the circumstances. The FRB's and the FDIC's rules also permit the banking organization to consolidate the investment on a pro rata basis in appropriate circumstances. These options for handling unconsolidated subsidiaries, joint ventures, and associated companies for purposes of determining the capital adequacy of the parent banking organization provide the agencies with the flexibility necessary to ensure that institutions maintain capital levels that are commensurate with the actual risks involved.

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[2] *See* 12 U.S.C. § 335 (state member banks subject to the "same conditions and limitations" that apply to national banks that hold financial subsidiaries).

[3] The applicable statutory requirements for state nonmember banks are as follows. The bank (and each of its insured depository institution affiliates) must be well capitalized. The bank must comply with the capital deduction and deconsolidation requirements. It must also satisfy the requirements for policies and procedures to protect the bank from financial and operational risks and to preserve corporate separateness and limited liability for the bank. Further, transactions between the bank and a subsidiary that would be classified as a financial subsidiary generally are subject to the affiliate transactions restrictions of the FRA. *See* 12 U.S.C. § 1831w.

[4] *See* 12 U.S.C. § 1841(*l*)(2).

Under the OTS's capital regulations, a statutorily mandated distinction is drawn between subsidiaries, which generally are majority-owned, that are engaged in activities that are permissible for national banks and those that are engaged in activities "impermissible" for national banks. Where subsidiaries engage in activities that are impermissible for national banks, the OTS requires the deduction of the parent's investment in these subsidiaries from the parent's assets and capital. If a subsidiary's activities are permissible for a national bank, that subsidiary's assets are generally consolidated with those of the parent on a line-for-line basis. If a subordinate organization, other than a subsidiary, engages in impermissible activities, the OTS will generally deduct investments in and loans to that organization.[5] If such a subordinate organization engages solely in permissible activities, the OTS may, depending upon the nature and risk of the activity, either assign investments in and loans to that organization to the 100 percent risk-weight category or require full deduction of the investments and loans.

Collateralized Transactions

The FRB and the OCC assign a zero percent risk weight to claims collateralized by cash on deposit in the institution or by securities issued or guaranteed by the U.S. Government, U.S. Government agencies, or the central governments of other countries that are members of the Organization for Economic Cooperation and Development (OECD). The OCC and the FRB rules require the collateral to be marked to market daily and a positive margin of collateral protection to be maintained daily. The FRB requires qualifying claims to be fully collateralized, while the OCC rule permits partial collateralization.

The FDIC and the OTS assign a zero percent risk weight to claims on qualifying securities firms that are collateralized by cash on deposit in the institution or by securities issued or guaranteed by the U.S. Government, U.S. Government agencies, or other OECD central governments. The FDIC and the OTS accord a 20 percent risk weight to such claims on other parties.

Noncumulative Perpetual Preferred Stock

Under the federal banking agencies' capital standards, noncumulative perpetual preferred stock is a component of Tier 1 capital. The capital standards of the OCC, the FRB, and the FDIC require noncumulative perpetual preferred stock to give the issuer the option to waive the payment of dividends and to provide that waived dividends neither accumulate to future periods nor represent a contingent claim on the issuer.

As a result of these requirements, if a bank supervised by the OCC, the FRB, or the FDIC issues perpetual preferred stock and is required to pay dividends in a form other than cash, e.g., stock, when cash dividends are not or cannot be paid, the bank does not have the option to waive or eliminate dividends, and the stock would not qualify as noncumulative. If an OTS-supervised savings association issues perpetual preferred stock that requires the payment of dividends in the form of stock when cash dividends are not paid, the stock may, subject to supervisory approval, qualify as noncumulative.

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[5] *See* 12 CFR § 559.2 for the OTS's definition of subordinate organization.

Equity Securities of Government-Sponsored Enterprises

The FRB, the FDIC, and the OTS apply a 100 percent risk weight to equity securities of government-sponsored enterprises (GSEs), other than the 20 percent risk weighting of Federal Home Loan Bank stock held by banking organizations as a condition of membership. The OCC applies a 20 percent risk weight to all GSE equity securities.

Limitation on Subordinated Debt and Limited-Life Preferred Stock

The OCC, the FRB, and the FDIC limit the amount of subordinated debt and intermediate-term preferred stock that may be treated as part of Tier 2 capital to 50 percent of Tier 1 capital. The OTS does not prescribe such a restriction. The OTS does, however, limit the amount of Tier 2 capital to 100 percent of Tier 1 capital, as do the other agencies.

In addition, for banking organizations supervised by the OCC, the FRB, and the FDIC, at the beginning of each of the last five years of the life of a subordinated debt or limited-life preferred stock instrument, the amount that is eligible for inclusion in Tier 2 capital is reduced by 20 percent of the original amount of that instrument (net of redemptions). The OTS provides thrifts the option of using either the discounting approach used by the other federal banking agencies, or an approach which, during the last seven years of the instrument's life, allows for the full inclusion of all such instruments, provided that the aggregate amount of such instruments maturing in any one year does not exceed 20 percent of the thrift's total capital.

Tangible Capital Requirement

Savings associations supervised by the OTS, by statute, must satisfy a 1.5 percent minimum tangible capital requirement. Other subsequent statutory and regulatory changes, however, imposed higher capital standards rendering it unlikely, if not impossible, for the 1.5 percent tangible capital requirement to function as a meaningful regulatory trigger. This statutory tangible capital requirement does not apply to institutions supervised by the OCC, the FRB, or the FDIC.

Market Risk Rules

In 1996, the OCC, the FRB, and the FDIC adopted rules requiring banks and bank holding companies with significant exposure to market risk to measure and maintain capital to support that risk. The OTS did not adopt a market risk rule because no OTS-supervised savings association engaged in the threshold level of trading activity addressed by the other agencies' rules. As the nature of many savings associations' activities has changed since 1996, market risk has become an increasingly more significant risk factor to consider in the capital management process. Accordingly, the OTS has joined the other agencies in proposing a revised market risk rule.[6]

[6] 71 FR 55958 (September 25, 2006).

Differences in Accounting Standards Among the Federal Banking Agencies

Push-Down Accounting

Push-down accounting is the establishment of a new accounting basis for a depository institution in its separate financial statements as a result of the institution becoming substantially wholly owned. Under push-down accounting, when a depository institution is acquired in a purchase, yet retains its separate corporate existence, the assets and liabilities of the acquired institution are restated to their fair values as of the acquisition date. These values, including any goodwill, are reflected in the separate financial statements of the acquired institution, as well as in any consolidated financial statements of the institution's parent.

The OCC, the FRB, and the FDIC require the use of push-down accounting for regulatory reporting purposes when an institution's voting stock becomes at least 95 percent owned by an investor or a group of investors acting collaboratively. This approach is generally consistent with accounting interpretations issued by the staff of the Securities and Exchange Commission. The OTS requires the use of push-down accounting when an institution's voting stock becomes at least 90 percent owned by an investor or investor group.

Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency
Office of Thrift Supervision

April 4, 2008

The Honorable Barney Frank
Chairman
Committee on Financial Services
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

The Board of Governors of the Federal Reserve System (Federal Reserve Board), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS) (collectively, the agencies) are submitting this joint report to Congress as required by Section 305 of the Riegle Community Development and Regulatory Improvement Act. This is the twelfth interagency report submitted under that section. The agencies submitted the eleventh report to Congress in April 2007.

The agencies remain committed to the mandate of Section 305 to improve the coordination of examinations and supervision of institutions that are subject to multiple regulators. The basic principles governing these activities are set forth in the Interagency Policy Statement on Examination Coordination, issued in 1993. As indicated in previous Section 305 reports, the agencies place high priority on working together to identify and reduce regulatory burden and on coordinating supervisory activities, not only with each other and state supervisors, but also with United States securities regulators, state insurance regulators, and foreign financial institution supervisors.

Mechanisms to Coordinate Supervision

The agencies, in conjunction with state supervisors, have a number of formal and informal mechanisms to foster continued coordination in examining and supervising banking organizations.

Federal Financial Institutions Examination Council

The Federal Financial Institutions Examination Council (FFIEC) is a legislatively established body responsible for promoting uniform supervisory policies and establishing uniform principles, standards, and report forms for examinations of depository institutions. The member agencies of the FFIEC are the agencies and the National Credit Union Administration (NCUA). As the result of legislation in 2006, the Chair of the FFIEC State Liaison Committee serves as a sixth member of the FFIEC. Through its State Liaison

Committee, the FFIEC serves as an important forum for dialogue between federal and state supervisory agencies.

To foster interagency cooperation, the FFIEC has established interagency task forces on consumer compliance, examiner education, information sharing, regulatory reports, surveillance systems, and supervision. These task forces share information and coordinate activities on a wide range of supervisory issues.

Joint Supervisory Training Courses and Conferences

The FFIEC's Examiner Education Office offers a variety of schools, conferences, and workshops for the agencies' examiners. These courses are also made available to examiners from the state supervisory agencies. A listing of course offerings and schedules is available on the FFIEC's website at http://www.ffiec.gov/exam/education.htm. Offerings in 2007 included:

- Anti-Money Laundering (AML) Workshops, which allow examiners to maintain up-to-date knowledge of laws and regulations, including the Bank Secrecy Act (BSA), USA PATRIOT Act, and Office of Foreign Assets Control (OFAC) sanctions programs. Fourteen sessions were held in 2007 and featured guest speakers from the Financial Crimes Enforcement Network (FinCEN), the Federal Bureau of Investigation, and OFAC.
- An Advanced BSA/AML Specialists Conference that is designed to provide continuing education to BSA compliance specialists and focuses on advanced BSA/AML topics and emerging supervisory issues related to higher risk institutions, products, services, customers, and geographic locations. The first conference was held in August 2007 and now will be held annually.
- Financial Crimes Seminars that provide commissioned examiners with a higher level of knowledge of fraudulent schemes and insider abuse. Three seminars were held in 2007.
- An advanced credit curriculum comprised of three separate schools that provided examiners with intensive training in cash flow concepts and credit analysis.
- Two International Banking Schools held for examiners who have supervisory responsibilities for regional or multinational financial institutions that are actively engaged in international banking activities and U.S. branches and agencies of foreign institutions.
- An Information Technology (IT) Symposium for senior IT examiners to discuss significant, current, or emerging issues related to information technology, to consult with external subject matter experts, and to develop recommendations for institutions, service providers, or examiners to address those issues.
- An annual IT Conference for middle and senior level IT examiners. The 2007 conference focused on information security issues such as data protection, customer authentication, identity theft, risk assessment, and network security. Pandemic planning efforts were also studied, along with emerging technologies such as remote deposit capture and wireless banking.
- An annual Asset Management Forum held for examiners and specialists involved in supervising financial institution trust and asset management activities.

- A Payments System Risk Conference that addressed the risks involved in emerging and existing payment systems, the means used to minimize these risks, and the methods of evaluating these risks in the examination process.
- A Capital Markets Conference held for those examiners who must integrate the risks inherent in capital markets activities into the overall risk profile of an institution during an examination or review of the institution. Two conferences were held in 2007. In addition, a Capital Markets Specialists conference was held to update examiners specializing in capital markets examination activities.
- A Community Financial Institutions Lending Forum that addressed credit-related issues affecting financial institutions whose asset size is under $1 billion. The training is intended to heighten examiner awareness and increase knowledge regarding important or emerging credit-related topics confronting the financial institution and regulatory communities.
- A Real Estate Appraisal School that provided examiners with the knowledge and skills required to review a commercial real estate appraisal and to determine compliance with agency appraisal regulations and the standards in the Uniform Standards of Professional Appraisal Practice.
- A Testifying School designed for commissioned examiners who will testify within three months of completion of the program. In the two sessions in 2007, participants learned to present findings as an expert witness through depositions and in-court testimony.
- An internet-based tutorial, which provided an update on the FedLine Advantage (FLA) communications platform and discussed the revised FLA Funds Transfer Examination Work program for the state supervisory agencies, as well as the FFIEC member agencies, the Farm Credit Administration, and the Federal Housing Finance Board.

The agencies sponsor other conferences to discuss emerging supervisory concerns. For example, the agencies' chief accountants sponsor an annual conference to discuss emerging accounting and auditing issues with the agencies' examiners and accounting staff. The 2007 conference, attended by approximately 375 participants, included discussions on fair value accounting, internal controls, and accounting for impaired assets, as well as updates from the Securities and Exchange Commission (SEC), the Financial Accounting Standards Board (FASB) and the Public Company Accounting Oversight Board (PCAOB). The agencies also offered five Basel II Advanced Measurement Approaches (AMA) Operational Risk seminars (three domestically and two for international supervisors), attended by 102 U.S. examiners involved in supervising large complex financial institutions that will be subject to the advanced approaches under the Basel II Capital Accord. The seminars addressed the challenges of capital quantification associated with operational risk, industry progress and the range of practice, and supervisory processes for evaluating implementation efforts. The international seminars were provided to approximately 45 supervisors from 20 countries.

In October 2007, the second Interagency Consumer Complaints Conference was attended by approximately 200 participants, including representatives from eleven state banking departments. The agencies convened this conference to discuss financial institution regulatory issues affecting consumers, to determine more effective means for sharing complaint information among the agencies, and to identify best practices for enhancing the agencies' interaction with the public. The agencies have agreed to hold such conferences regularly to discuss issues that are common among the agencies. The next conference will be held in April 2009.

Common Reporting Forms and Examination Tools

The agencies routinely collaborate on and adopt common reporting forms and examination tools, with a goal of streamlining and reducing burden where possible. For example, the agencies use interagency forms with respect to filings under the Bank Merger Act and the Change in Bank Control Act. In addition, the FDIC, OCC, and OTS have adopted a common form for granting deposit insurance and federal charters.

The FDIC, Federal Reserve Board, and state supervisory agencies have an automated examination support system that includes a common risk-focused supervision framework and loan review tool. Similarly, the agencies, in partnership with the Conference of State Bank Supervisors (CSBS), have developed a standardized electronic loan file format that examiners can use to facilitate community and mid-size bank safety and soundness examinations. The Federal Reserve, in consultation with the other FFIEC agencies, revised the FLA Funds Transfer Examination Work program and made it available to the state supervisory agencies, as well as to the FFIEC member agencies.

Supervisory Information Sharing and Coordination

To the extent possible, the agencies build upon each other's supervisory reviews and databases to minimize regulatory burden. The agencies routinely share reports of examination, inspection reports, and other agency-institution communications. The agencies also provide each other with access to their organizations' structural, financial, and supervisory information. Meetings and discussions take place among the agencies throughout the year, and when appropriate, the agencies hold joint meetings with institutions involving matters of mutual interest. This approach extends to periodic coordinated reviews or examinations where a business activity is conducted across legal entities.

The agencies extensively coordinate their supervision of large, complex entities to reduce duplication of effort and minimize regulatory burden. To ensure effective coordination, the agencies: (1) share institution risk profiles and other supervisory information regarding the entities they supervise; (2) exchange information on proposed examination and supervisory activities for the coming year; and (3) coordinate the planning and execution of those activities to minimize or eliminate overlap or duplication.

As discussed more fully in the "Other 2007 Accomplishments" section of this report, the agencies closely collaborated in their efforts to monitor and respond to the recent turmoil in the mortgage and credit markets. These efforts have included periodic meetings among the agencies' senior supervisory staffs to share information on conditions in key market sectors and about financial institutions, to identify potential issues, and to coordinate regulatory responses. Similarly, the agencies' examination staffs are coordinating efforts on various information requests, as appropriate, so as to obtain needed information with the least amount of burden.

The FFIEC's Task Force on Information Sharing serves as a vehicle to enhance and improve the exchange of electronic information among the agencies. This group is responsible for establishing principles that protect the privacy, security, and integrity of shared information. It also oversees the development of data management standards to improve consistency and encourages the development of compatible technical architectures among the agencies to ensure that information can be shared efficiently.

The FFIEC's Task Force on Consumer Compliance oversees the agencies' collection, processing, and dissemination of information collected pursuant to the Home Mortgage Disclosure Act (HMDA) and Community Reinvestment Act (CRA).

The FDIC, Federal Reserve, and state bank supervisors continue to coordinate their efforts via a protocol for the prudential supervision of state-chartered banks. Under this protocol, the home state supervisor and appropriate federal regulator coordinate the supervision of interstate state-chartered banks to ensure a risk-focused process and to reduce regulatory burden. The OTS works closely with individual state supervisors to coordinate the supervision and examination of state savings institutions.

The agencies have executed memoranda of understanding (MOUs) regarding the sharing of confidential supervisory information with state insurance regulators in order to allow the agencies to rely, to the fullest extent possible, on the functional regulators of insurance activities, pursuant to mandates established in the Gramm-Leach-Bliley Act. The agencies have exercised their authority under these MOUs in the context of the supervision of institutions with regulated insurance entities.

Emergency Preparedness and Response

As noted in previous years, through the FFIEC's Task Force on Supervision, the agencies have established a protocol for supervisory communications to be used in emergency situations, the FFIEC Supervisory Emergency Communications Protocol. This protocol is updated quarterly and tested at least annually with key supervisory personnel to ensure its ongoing effectiveness. The protocol was recently enhanced to include information that would facilitate coordination during a pandemic event.

The agencies, together with other federal and state financial regulators, are members of the Financial Banking Information Infrastructure Committee (FBIIC), which was formed to address and coordinate issues related to the security and resilience of the U.S. financial sector. From September 24 through October 12, the FBIIC and the Financial Services Sector Coordinating Council (FSSCC), an organization of financial services trade associations and individual firms, conducted a pandemic flu exercise for the financial services sector in the United States. Objectives of this exercise were to enhance the understanding of systemic risks to the sector, to provide an opportunity for firms to test their pandemic plans, and to examine how the effect of a pandemic flu on other critical infrastructures could impact the financial services sector. A total of 2,775 organizations registered for the exercise, of which approximately 62 percent were banks, thrifts, and credit unions. The FFIEC as well as the individual agencies publicized the test to encourage participation, which was voluntary. Organizations conducted the exercise anonymously from their own locations through electronic mail and a secure website. Nearly all of the participating institutions identified opportunities to improve their contingency plans for a pandemic.

The FFIEC's Task Force on Supervision formed a Pandemic Working Group in 2006 to help coordinate planning and supervisory efforts that may be needed during a pandemic event. The Working Group engaged in several projects designed to help the agencies prepare for supervision through a pandemic event. In February 2007, the Working Group hosted a tabletop exercise with the Task Force and in December, issued guidance for use by financial institutions in identifying the continuity planning that should be in place to minimize the potential adverse effects of a pandemic event. This guidance expands upon the Interagency Advisory on Influenza Pandemic Preparedness issued in March 2006. The guidance was also incorporated into an update of the FFIEC Business Continuity Planning Handbook for use by examiners and the industry. The Handbook, which is greatly expanded from the 2003 version, was published in March 2008.

Other Coordinated Supervisory Activities

Where applicable, the agencies coordinate their supervisory activities related to insurance, securities, and banking businesses with functional regulators, such as the SEC and state insurance regulators. Periodic cross-sector meetings with representatives of the agencies, the SEC, state banking, insurance, and securities supervisors, and the Commodity Futures Trading Commission (CFTC) are held to identify areas that may require supervisory attention and coordination. For example, the OCC, FDIC and Federal Reserve have been working with the SEC and other international regulators to improve the trade and settlement processing systems that support the global derivatives market. In addition, in November 2007, the Federal Reserve and SEC issued their joint final rule that implements the bank broker provisions of the Gramm-Leach-Bliley Act (GLBA). In developing the final rules, the SEC and the Federal Reserve consulted with the OCC, FDIC, and OTS.

The agencies, together with FinCEN and OFAC, and the CSBS, are fully committed to preventing the inappropriate use of the financial system by criminals and terrorists. Under the auspices of the FFIEC's BSA/AML Working Group, the agencies, NCUA, FinCEN, OFAC, and the CSBS collaborated in the development of the FFIEC's BSA/AML Examination Manual, which was initially released in 2005. In 2007, the manual was updated to further clarify supervisory expectations, incorporate new regulatory issuances, and respond to industry requests for additional guidance. The agencies continued to share information with FinCEN under the interagency MOU that was finalized in 2005, and with OFAC under the interagency MOU that was finalized in 2006. An interagency BSA Enforcement Policy statement, which complements the FFIEC BSA/AML Examination Manual, was developed and issued in 2007. The statement was designed to promote consistency among the agencies with regard to BSA-related enforcement decisions, and to make standards used by regulators in such cases more transparent.

In addition, the agencies participate in other BSA/AML interagency forums. The Bank Secrecy Act Advisory Group is a public-private partnership devoted to evaluating all BSA matters and exchanging information and recommendations for making the reporting requirements more efficient. Members include representatives from the agencies, FinCEN, federal and state law enforcement agencies, self-regulatory organizations, some state regulatory agencies, and members of the financial services industry subject to BSA regulation, including trade groups and practitioners representing the industry. Through this partnership, the agencies will continue to conduct outreach to obtain input for future updates of the FFIEC BSA/AML Examination Manual.

Insurance specialists from the agencies communicate regularly on an interagency basis with staff of the National Association of Insurance Commissioners, the organization that supports the insurance regulatory officials of the 50 states, the District of Columbia, and the five U.S. territories, on topics of mutual interest to the agencies and state insurance regulators.

International Supervision Coordination

The agencies participate on a number of international supervisory groups, including the Basel Committee on Banking Supervision (BCBS), and the Joint Forum of banking, securities, and insurance regulators, which promote more consistent and uniform supervision of internationally active financial services firms. These groups have a number of work streams underway to evaluate lessons learned and to assess whether additional policy actions are needed in response to recent market events. The agencies also participate in the Association of Supervisors of Banks of the Americas (ASBA), which promotes international standards for effective banking supervision in the Americas region.

The agencies provide training for staff and officials from non-U.S supervisory authorities and foreign central banks. During the year, the agencies offered training courses exclusively for foreign supervisory authorities in Washington, D.C. and in a number of foreign jurisdictions. Staff at the agencies also took part in technical assistance and training missions led by the International Monetary Fund, the World Bank, the Asian Development Bank, the BCBS, the Financial Stability Institute, South East Asian Central Banks Research and Training Center (SEACEN) and ASBA. This training was concentrated in Latin America, Asia, the Middle East and North Africa, and Eastern Europe.

In support of the United States Partnership for Financial Excellence in the Middle East and North Africa (MENA), the agencies worked with the U.S. Treasury Department, the U.S. State Department, and the U.S. Agency for International Development to design and deliver training programs aimed at improving banking supervision in the MENA region. Additionally, through the Treasury Department, the agencies participated in the Third United States – Middle East & North Africa Private Sector Dialogue Conference in the United Arab Emirates and the US-LA Private Sector Dialogue Conference, in

Colombia, with the primary focus of addressing global money laundering risks and related controls and risk mitigants.

The agencies also supported training activities delivered under the Asia Pacific Economic Cooperation Financial Regulators Training Initiative, which was launched by the Treasury Department shortly after the Asian crisis. Administrative and funding support for this initiative is provided by the Asian Development Bank. Also, the agencies have supported the State Department through the Terrorist Finance Working Group by providing training for foreign supervisors and technical assistance to designated countries related to money laundering and terrorist financing risks.

Federal and state supervisory agencies coordinate the supervision of U.S. operations of foreign banking organizations through the Foreign Banking Organizations Supervision Program, which involves extensive interagency information sharing and supervisory collaboration. In addition, staffs at the agencies participate in an annual interagency international supervision conference. The annual conference brings together senior supervisors from across the agencies to discuss emerging international supervisory developments, as well as the implications of these developments on the supervisory strategies for the U.S. operations of internationally active financial institutions and the international operations of U.S. banking organizations.

The agencies also coordinate with numerous foreign regulatory authorities in the supervision of internationally active companies and, when appropriate, jointly enter into multilateral statements of cooperation with foreign bank supervisors. For example, the agencies are working closely with foreign supervisors to coordinate home/host issues associated with the implementation of the Basel II Capital Accord and in monitoring and assessing the potential effects that recent market disruptions may have on global financial institutions and market operations.

The agencies represent the United States annually at an international information sharing conference focused on technology risks and risk management practices. The 2007 Information Technology Supervisors Group (ITSG) Conference convened in Toronto, Canada, and included financial institution supervisory agencies from sixteen countries. Discussion topics included information security, outsourcing, IT auditing, pandemic event planning, and Basel II AMA for operational risk preparedness.

Formal Joint Examination Programs

In addition to the coordination mechanisms discussed above, the agencies also have three formal joint examination programs that allow them to leverage and share examination resources and provide consistent supervisory evaluations of activities that often cut across financial institutions.

Shared National Credit Program

The Shared National Credit (SNC) program is a joint effort of the FDIC, Federal Reserve Board, OCC, and the OTS as an assisting agency to collaborate on reviewing large syndicated loans held by multiple banks. The SNC program reviews selected borrowers using interagency teams to avoid duplicate reviews of the same credit and to ensure consistent treatment. The agencies release to the public aggregate statistical data from the SNC program, which provides a unique perspective on credit quality trends in the banking industry. In 2007, this program covered 7,686 credits totaling $2.3 trillion in credit commitments to 5,264 borrowers.

The agencies implemented an enhanced sampling methodology beginning with the 2003 SNC review process. The goal of this methodology was to promote efficiency and effectiveness through a more focused, risk-based review of SNCs. The immediate impact has been a decrease in the number of facilities selected for examiner review as well as a reduced dollar amount of SNCs reviewed. This has resulted in a significant reduction in the overall cost and burden of the SNC program.

The agencies are continuing their work on a SNC modernization initiative to standardize the SNC data collection process, expand SNC data collected from large reporting institutions, apply advanced credit risk benchmarking techniques for common SNC borrowers/portfolios, and provide reporting banks with feedback on their commonly held SNC portfolios. A Notice for Public Comment on SNC Modernization was published in the *Federal Register* on December 20, 2004. Final specifications and related procurement and development activities are planned for 2008.

Multi-Regional Data Processing Servicer and Shared Application Software Review Programs

Under the auspices of the FFIEC's IT Subcommittee of the Task Force on Supervision, the FFIEC member agencies administer two joint programs that support the assessment of the technology environment for institutions that 1) outsource their technology services and automated processing activities, or 2) rely on off-the-shelf applications to run their core banking systems. Examinations of service providers under the Multi-Regional Data Processing Servicer (MDPS) program are coordinated on a national level and target organizations considered by the agencies to present the most risk to the financial system due to the mission-critical nature of their services and the breadth of their client base, or because a provider processes work from operations over a sufficiently diverse geographic footprint.

Conducting the service provider examinations jointly is a more efficient and effective utilization of the agencies' IT examiners. In an effort to enhance the agencies' risk-focused supervisory approach for examining the providers in the MDPS program, the IT Subcommittee sponsored an Interagency MDPS Supervisory Strategy Meeting in both 2006 and 2007. Examiners assigned to each MDPS entity across the agencies collaboratively assess each firm's key risks and discuss appropriate supervisory responses. The result is a risk-focused exam approach for each firm that addresses its unique risk profile while promoting consistency of supervision across the MDPS firms. Given the initial positive results, the agencies are planning a 2008 meeting and expect to continue holding annual meetings.

In 2007, the IT Subcommittee also conducted a member agency-based survey on the foreign-based outsourcing activities of supervised financial institutions. The survey information provided all FFIEC agencies with current data on the financial institutions that utilize foreign-based technology service providers, including the volume and types of outsourcing activities.

The Shared Application Software Review program provides a tool for the agencies to review and share assessments of mission-critical software systems and applications, such as wire transfers, capital markets, loans, deposits, and general ledger systems that are used by a large number of financial institutions. These assessments are designed to reduce the time and resources needed to examine mission-critical processing activities at each of the user financial institutions.

Interagency Country Exposure Review Committee (ICERC)

The FDIC, Federal Reserve Board, and OCC formed ICERC in 1979 to ensure consistent treatment of the transfer risk associated with financial institutions' foreign exposures to public and private sector entities. The OTS joined ICERC in 2006 as an observing non-voting agency. New York State banking regulators also regularly attend the annual ICERC meeting.

At their October 2007 ICERC meeting, the agencies approved changes to the ICERC procedures and rating systems that would make the supervision of cross-border exposures more efficient and risk-focused. Such changes maintain strict regulatory attention to areas of transfer risk, but now also include discussions of regional and global macro trends that might indicate future areas of risk. ICERC continues to determine the appropriate classification and level of reserves for countries that are in default. ICERC decisions and analytical write-ups are used by the agencies to help examination teams assess individual institutions' cross-border risk.

Other 2007 Accomplishments

Throughout 2007, the agencies continued their efforts to coordinate examination and supervisory activities and to reduce unnecessary regulatory burden. In addition to those programs and efforts already noted in this report, highlights of the agencies' other 2007 efforts are outlined below.

Initiatives to Promote Sound Lending Practices and Respond to Recent Credit Market Events

As noted in the last two previous reports, the agencies undertook efforts starting in 2005 to address concerns about weakening underwriting standards and inadequate risk management practices for certain residential and commercial real estate lending products. These efforts culminated in the issuance of final interagency guidance on home equity lending in May 2005, on nontraditional mortgage products in September 2006, and on concentrations in commercial real estate lending in December 2006.

Continued weaknesses in the U.S. housing and mortgage markets, manifested in increased residential mortgage delinquencies and foreclosures and attendant fallout in various capital market instruments such as structured debt obligations, have been a major concern and focus for the agencies throughout the past year. The agencies have actively worked with Congressional leaders, other regulators, and industry and community groups to address these problems.

The agencies published for comment a proposed Statement on Subprime Mortgage Lending in March 2007 and issued final guidance in June to address risk management practices and consumer disclosures related to certain subprime adjustable rate mortgage (ARM) products. These products generally reset following an initial "teaser" rate, have high (or no) payment or rate caps, have substantial prepayment penalties, or have features likely to result in frequent refinancing to maintain affordable monthly payments. The subprime statement applies to all depository institutions, their subsidiaries, and non-depository affiliates, but not to state-regulated independent mortgage companies. Because non-federally regulated lenders are major originators of subprime mortgages, the agencies coordinated the development of the statement with the CSBS, which also has endorsed adoption of the subprime statement by the States.

As in the agencies' 2006 guidance on nontraditional mortgage products, the subprime statement specifies that an institution's analysis of a borrower's repayment capacity should include an evaluation of the borrower's ability to repay the debt by its final maturity at the fully indexed rate, assuming a fully amortizing repayment schedule. The statement also emphasizes the additional risks that these products can pose to an institution and a borrower when combined with other risk layering features, such as simultaneous second lien mortgages and little or no documentation of the borrower's income or assets. The statement underscores that communications with consumers, including advertisements, oral statements, and promotional materials, should provide clear and balanced information about the relative benefits and risks of the products. This information should be provided in a timely manner to assist consumers in their product selection process, not only upon submission of an application or at consummation of the loan.

Throughout 2007, the agencies encouraged lenders and mortgage servicers to appropriately work with mortgage borrowers who may be facing difficulties. In April 2007, the agencies issued an interagency Statement on Working with Mortgage Borrowers to encourage financial institutions to work constructively with borrowers who are financially unable to make their contractual payment obligations on their home loans. This interagency statement does not limit the terms of specific workout arrangements and recognizes that they can vary widely based on the borrower's specific circumstances. The agencies advised that institutions that follow prudent underwriting practices when engaging in workouts would not be criticized by the agencies for pursuing reasonable arrangements with borrowers. The statement also noted that lenders may receive favorable Community Reinvestment Act (CRA) consideration for programs that transition low- and moderate-income borrowers from higher cost loans to lower cost loans, provided that the loans are made in a safe and sound manner. The CSBS issued a similar statement.

The agencies also worked closely with the SEC, the FASB, and the American Securitization Forum to explore and clarify actions that mortgage servicers can take to assist borrowers whose mortgages have been securitized and sold to third party investors. Also a series of forums, hosted by the FDIC, were held with regulators and market participants to highlight and discuss these issues. Following these efforts, in September 2007, the agencies and the CSBS issued a statement encouraging federally regulated financial institutions and state-supervised entities that service securitized residential mortgages to pursue strategies to mitigate losses while preserving homeownership to the extent possible and appropriate. The statement encourages servicers of securitized mortgages to review the governing documents for the securitization trusts to determine the full extent of their authority to restructure loans that are delinquent, in default, or are in imminent risk of default. The governing documents may allow servicers to proactively contact borrowers at risk of default, assess whether default is reasonably foreseeable, and, if so, apply loss mitigation strategies designed to achieve sustainable mortgage obligations.

In December 2007, the OTS hosted a National Housing Forum that brought together regulatory agencies and some of the nation's foremost housing and economic experts to discuss the most significant current housing finance issues. The all-day event, attended by approximately 300 participants, featured panel discussions on: the outlook for the U.S. housing market and its potential effect on financial institutions; challenges and risks in the home mortgage market; consumer protection issues, including the growing problem of foreclosures; and the effect of capital markets on housing finance. The agencies will continue to work with lenders, community groups and members of Congress in the months ahead to address these issues.

In addition to these policy efforts, the agencies' examination staffs are coordinating supervisory efforts to address other related issues that may have a broad impact on the industry, including various accounting, disclosure, valuation, capital and liquidity issues.

Pilot Projects to Improve Supervision of Subprime Mortgage Lenders

In July 2007, the Federal Reserve Board, the OTS, the Federal Trade Commission (FTC), the CSBS, and the American Association of Residential Mortgage Regulators announced a pilot project to conduct targeted consumer-protection compliance reviews of selected non-depository lenders with significant mortgage operations. The pilot will focus on non-depository subsidiaries of bank and thrift holding companies, as well as mortgage brokers doing business with, or working for these entities. Additionally, the states will conduct coordinated examinations of independent state-licensed subprime lenders and their associated mortgage brokers.

Revisions to Risk-Based Capital Standards

The agencies work together closely to discuss and coordinate complex capital rulings, interpretations, and initiatives. During 2007, the agencies continued their implementation of the advanced approaches under the Basel II Capital Accord, issued in final form by the BCBS in June 2006. As reported last year, the agencies issued a notice of proposed rulemaking in September 2006 to implement the Basel II advanced approaches. In December 2006, the agencies issued a notice of proposed rulemaking with several revisions to the existing U.S. risk-based capital rules (Basel IA proposal). The comment period for both of these initiatives ended on March 26, 2007.

Over most of 2007, the agencies focused on issuing a final rule related to the Basel II advanced approaches. That final rule was published in the *Federal Register* on December 7, 2007. Institutions may begin transitioning to the new rules after they adopt an implementation plan and have systems that comply with the final rule's qualification requirements. In January 2008, the agencies published for approval by the Office of Management and Budget, final reporting requirements and reporting templates for institutions that will be adopting the Basel II advanced approaches.

The agencies decided not to finalize the Basel IA proposal and have agreed, instead, to issue a new notice of proposed rulemaking that would implement the standardized approach under Basel II.

Accounting and Audit Initiatives and Guidance

The agencies recognize the importance of high quality accounting and auditing standards to the continued safe and sound operation of insured depository institutions and work closely with the SEC, the FASB, the International Accounting Standards Board (IASB), the American Institute of Certified Public Accountants (AICPA), the PCAOB, and the International Auditing and Assurance Standards Board (IAASB) on matters of mutual interest. The agencies routinely collaborate on supervisory guidance to address safety and soundness concerns that arise from accounting and auditing matters. The agencies also work together to provide commentary on proposals by the various accounting and auditing standards setters that may have a significant impact on the banking industry. The agencies are working closely with the SEC and the FASB on various issues related to the recent market disruptions, including various interpretations and application of guidance related to mortgage loan servicing agreements, fair value measurement in illiquid markets, and accounting for asset-backed commercial paper and structured financial instruments.

Initiatives to Enhance Consumer Disclosures and Safeguards

The agencies continued their work to improve financial disclosures to consumers. In May 2007, the agencies issued final illustrations of consumer information intended to help institutions implement the consumer protection portion of the nontraditional mortgage guidance. The consumer protection section of the guidance sets forth recommended practices to ensure that consumers have clear and balanced information about nontraditional mortgages before choosing a mortgage product or before selecting a payment option for an existing mortgage.

In August 2007, the agencies issued proposed illustrations of consumer information for certain ARM products described in the agencies' subprime mortgage lending statement. The subprime statement recommends that communications ensure that consumers have clear, balanced, and timely information about the relative benefits and risks of certain ARM products. The illustrations are intended to assist institutions in providing this information.

In March 2007, the FFIEC agencies, in conjunction with the CFTC, the SEC, and the FTC, issued for comment a proposed model privacy form that financial institutions could use for their privacy notices to consumers as required under the GLBA.

In 2007, the agencies also closely coordinated rulemaking efforts under the Fair and Accurate Credit Transaction Act of 2003 to enhance the ability of consumers to combat identity theft, to increase the accuracy of consumer reports, and to allow consumers to exercise greater control over the type and amount of certain marketing solicitations they receive. The late 2007 rulemakings made by the FFIEC agencies and, in some cases, made with the FTC, are as follows:

- Final rules on identity theft "red flags." The new rules require each financial institution and creditor that holds any consumer account, or other account for which there is a reasonably foreseeable risk of identity theft, to develop and implement an Identity Theft Prevention Program for combating identity theft in connection with new and existing accounts.

- Proposed rules and guidelines for ensuring the accuracy and integrity of information furnished to consumer reporting agencies. The proposed rules also would identify the circumstances when an entity would be required to investigate a dispute concerning the accuracy of certain consumer report information, based on a direct request of a consumer.

- Final rules requiring credit and debit card issuers to develop policies and procedures to assess the validity of a request for a change of address that is followed closely by a request for an additional or replacement card. The agencies also issued final rules requiring users of consumer reports to develop reasonable policies and procedures to apply when they receive a notice of address discrepancy from a consumer reporting agency.

- Final rules that provide consumers with an opportunity to "opt out" before a financial institution uses information provided by an affiliated company to make certain marketing solicitations about its products and services to the consumer.

In other consumer protection activities, in September 2007, the FFIEC agencies issued for comment a proposed statement encouraging financial institutions to follow best practices to protect federal benefit payments from garnishment orders. The proposed guidance was developed to encourage financial institutions to have policies and procedures in place with respect to handling garnishment orders and sets forth best practices, including procedures designed to expedite notice to the consumer of the garnishment process and release of funds to the consumer as quickly as possible.

The agencies encourage financial institutions to work directly with their customers to resolve complaints or inquiries. There are instances, however, where a consumer may seek the assistance of the regulator in such matters and each of the agencies has phone numbers, web sites, and processes in place to offer such assistance. The agencies recognize that there may be opportunities to enhance their consumer complaint and inquiry programs. In December 2007, the FFIEC approved the recommendations of an interagency consumer complaint working group to engage a third party vendor to evaluate the feasibility, options and benefits associated with a number of interagency initiatives to enhance the consumer's experience, including for example, a process for routing consumer calls, letters, and emails to the appropriate agency. As part of this work, the vendor would be asked to conduct consumer focus groups to gather information regarding the consumer complaints process. Additionally, the vendor would be charged with evaluating the benefit and the feasibility of initiatives that would leverage agency resources. The working group proposed a time line that would result in a report of the vendor's recommendations by September 2008.

Updated Supervisory Guidance

The agencies continually work together to promote the goals of the CRA. In July 2007, the agencies issued for comment a series of new and revised interagency questions and answers pertaining to the CRA. Some of the proposed revisions are intended to encourage institutions to work with homeowners who are unable to make mortgage payments by highlighting that the institutions can receive CRA consideration for foreclosure prevention programs for low- and moderate-income homeowners, consistent with the April 2007 interagency Statement on Working with Mortgage Borrowers. Other revisions relate to CRA consideration of investments in, and joint ventures with, minority- and women-owned financial institutions.

In June 2007, the agencies released a list of distressed or underserved non-metropolitan middle-income geographies in which bank revitalization or stabilization activities will receive CRA consideration as "community development."

Finally, in September 2007, the FFIEC agencies approved updated examination procedures for Regulation DD (Truth in Savings). The changes include procedures for the disclosure requirements for institutions advertising the payment of overdrafts.

Initiatives to Reduce Unnecessary Regulatory Burden and Enhance Efficiency

In 2003, the agencies initiated an interagency project to review their regulations to identify and eliminate those regulations that are outdated, unnecessary, or unduly burdensome on insured depository institutions, pursuant to Section 2222 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA). EGRPRA requires the agencies to categorize the regulations, publish the categories for comment, report to Congress on any significant issues raised by the comments, eliminate unnecessary regulations, and analyze whether legislative change is required to reduce burden. The agencies completed and submitted the report to Congress in the fall of 2007.

In September 2007, the agencies issued final rules that raised the \$250 million ceiling for 18-month examinations to \$500 million for qualified, well-managed depository institutions. The rule implements section 605 of Financial Services Regulatory Relief Act (FSRRA) of 2006 and related legislation.

Section 604 of FSRRA requires the agencies to review the content of "Reports of Condition" within one year of enactment and then to use the results as a basis for eliminating or reducing any unnecessary or inappropriate information collected in these reports. The FFIEC's Task Force on Reports surveyed 165 user groups within the agencies and CSBS to identify the purposes for which each group uses each reported data item, the extent of usage for each item, and the frequency with which each item is needed. The survey was completed in August and the results were evaluated and reported to the FFIEC principals in October 2007. In 2008, the Task Force will consider the information received from the survey to determine where possible burden-reducing revisions may be made in the reports of condition.

During the fourth quarter of 2007, the FFIEC BSA/AML Working Group began an interagency dialogue to evaluate the agencies' current risk-based BSA examination approach, and to identify possible areas to reduce regulatory burden for financial institutions that have a lower BSA risk.

Conclusion

The agencies are committed to maintaining regulatory and supervisory processes that maximize efficiency, while eliminating unnecessary costs to institutions, maintaining safety and soundness, and safeguarding consumers. The agencies have worked in the past year—and will continue to work—to improve the supervisory process by reducing regulatory burden, promoting consistency, eliminating duplicative activities in the examination process, and promoting greater efficiency in the use of resources. Coordination and streamlining efforts have been successful thus far, and we intend to continue exploring ways in which the agencies can work together, leverage each other's efforts, and ease the regulatory burden on the financial institutions the agencies supervise.

Sincerely,

Randall S. Kroszner, Governor
Board of Governors of the
Federal Reserve System

Sheila C. Bair, Chairman
Federal Deposit Insurance Corporation

John C. Dugan
Comptroller of the Currency

John M. Reich, Director
Office of Thrift Supervision

Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency
Office of Thrift Supervision

June 25, 2009

The Honorable Christopher J. Dodd
Chairman
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

The Board of Governors of the Federal Reserve System (Federal Reserve Board), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS) (collectively, the agencies) are submitting this joint report to Congress as required by Section 305 of the Riegle Community Development and Regulatory Improvement Act. This is the thirteenth interagency report submitted under that section.

The agencies remain committed to the mandate of Section 305 to improve the coordination of examinations and supervision of institutions that are subject to multiple regulators. The basic principles governing these activities are set forth in the Interagency Policy Statement on Examination Coordination, issued in 1993. As indicated in previous Section 305 reports, the agencies place high priority on working together to identify and reduce regulatory burden and on coordinating supervisory activities, not only with each other and state supervisors, but also with United States securities regulators, state insurance regulators, and foreign financial institution supervisors.

Coordinating Responses to Recent Market Events

Much of the agencies' supervisory and policy efforts over the past year have focused on monitoring and responding to the unprecedented market turmoil and associated dislocations in global credit and funding markets. In responding to these events, the agencies have drawn heavily on the established protocols and coordinating mechanisms discussed in this report. The agencies are holding frequent meetings among their senior supervisory staffs and with agency principals to share information, identify potential issues, and coordinate regulatory responses. Key supervisory staffs from each agency meet on a regular basis to exchange information on potential troubled institutions and to coordinate resolution strategies for those institutions. For institutions where failure may be imminent, the primary federal agency works closely with the FDIC to ensure an orderly receivership or liquidation.

The agencies are working closely with the U.S. Treasury Department to implement provisions of the Emergency Economic Stabilization Act of 2008 (EESA). These efforts include providing technical assistance to the U.S. Treasury Department on the design and operation of asset and capital purchase programs under its Troubled Asset Relief Program (TARP) facility. Treasury coordinated with the agencies in developing a uniform application form for qualified financial institutions (QFIs) that want to participate in the TARP Capital Purchase Program (CPP) and are using common evaluation factors and decision forms to review and provide recommendations on those applications to Treasury. Representatives of the agencies also serve on the TARP CPP Council that is an advisory body to Treasury to ensure that recommendations for CPP participation are applied effectively and consistently across the federal banking agencies and QFI applicants. The agencies are also working with the U.S. Treasury to develop reporting mechanisms to monitor and assess the use and effectiveness of TARP CPP proceeds by QFIs and to conduct forward looking assessments of the potential capital needs of the largest CPP recipients. Similar coordinating efforts are taking place among the federal banking agencies to ensure a smooth implementation of the FDIC's Temporary Liquidity Guarantee Program (TLGP).

In July 2008, the FDIC sponsored and the Federal Reserve Board, the OCC, the OTS, and the U.S. Treasury participated in the Forum on Mortgage Lending for Low- and Moderate-Income (LMI) Households. The purpose of the Forum was to explore a framework for LMI mortgage lending in the future, including the identification of market and regulatory incentives for encouraging responsible LMI mortgage lending. The Forum featured speakers and participants from banking, investing, government, academia, and the nonprofit community.

The agencies have issued several rulemakings and guidance in response to the recent market turmoil. In October 2008, the agencies issued an interagency statement and reporting instructions to allow banking organizations to recognize the effect of the tax change enacted in Section 301 of the EESA in their third quarter 2008 regulatory capital calculations. The agencies also finalized a joint rulemaking that would permit a banking organization to make the required deduction from tier 1 capital of goodwill net of any associated deferred tax liability.

In November 2008, the agencies issued the *Interagency Statement on Meeting the Needs of Creditworthy Borrowers*. In implementing this Statement, institutions are encouraged to lend prudently and responsibly to creditworthy borrowers, work with borrowers to preserve homeownership and avoid preventable foreclosures, adjust dividend policies to preserve capital and lending capacity, and employ compensation structures that encourage prudent lending. In an effort to make key aspects of mortgage loan data more transparent and publicly available, the OTS and OCC in September began publishing joint quarterly reports on loan performance, delinquencies and foreclosures. The reports present data from fourteen national banks and thrifts with the largest mortgage portfolios and can be used by examiners to assess emerging trends, evaluate asset quality and loan loss reserve needs, identify anomalies, and evaluate loss mitigation actions.

In December, the regulatory agencies met at the National Housing Forum with some of the nation's foremost housing and economic experts to discuss the most significant current housing finance issues. This all-day event was hosted by the OTS and featured panel discussions on: U.S. housing and residential mortgage markets; the regulators' efforts to deal with industry challenges and market uncertainties; the mortgage-backed securities market; and regulation of the mortgage lending industry. The agencies will continue to work with lenders, community groups and members of Congress in the months ahead to address these issues.

The agencies are also working closely with other domestic and international supervisors, including the President's Working Group, the Joint Forum of banking, securities, and insurance regulators, and the Senior Supervisors' Group, to identify and coordinate actions aimed at both restoring functioning markets and strengthening risk management and disclosure practices. For example, the Federal Reserve Board and the OCC are working with the Federal Reserve Bank of New York, the Securities and Exchange Commission (SEC), and other key global regulators and market participants to strengthen the operational infrastructure and backroom processes used for various over-the-counter derivative transactions. In September 2008, the agencies joined other global supervisors in endorsing the Basel Committee on Banking Supervision's (BCBS) *Principles for Sound Liquidity Risk Management and Supervision*. The principles underscore the importance of establishing a robust liquidity risk management framework that is well integrated into the bank-wide risk management process. The agencies plan to issue for comment guidance on the application of these principles to U.S. depository institutions later this year.

The recent market turmoil has highlighted areas where the current Basel II capital framework may need to be strengthened and the agencies are actively involved in these efforts. Among the refinements that are recommended in the consultative paper that the BCBS issued in January 2009 are higher capital requirements for re-securitizations, such as collateralized debt obligations comprised of asset-backed securities; a Pillar 2 capital requirement that is an add-on to the Pillar 1 capital requirement; and additional disclosures related to securitizations. These recommendations focused on structured securities as these securities experienced significant losses during the recent market turmoil. The capital treatment of liquidity facilities that support asset-backed commercial paper conduits is also under review. The current market risk capital framework, based on 1996 amendments to Basel I, is also being reexamined. These proposed changes are designed to better reflect potential exposures arising from the larger portion of complex, less liquid credit products that institutions now hold in their trading portfolios and to further reduce the incentive for regulatory arbitrage between the banking and trading books. Once the BCBS finalizes these and other changes to the Basel II Accord, the U.S. agencies will jointly consider their adoption in the U.S. through the agencies' notice and comment process.

Building on discussions begun in 2008, the BCBS also announced in early 2009 that it believes the level of capital in the banking system needs to be strengthened to raise its resilience to future episodes of stress. The Committee indicated that this would be achieved by a combination of measures such as introducing standards to promote the build-up of capital buffers that can be drawn down in periods of stress, strengthening the quality of bank capital, improving the risk-coverage of the capital framework and introducing a non-risk based supplementary capital measure. The agencies are actively involved in these initiatives.

The agencies are working closely with the SEC and the Financial Accounting Standards Board (FASB) on various accounting and disclosure issues related to the recent market disruptions, including various interpretations and application of guidance related to mortgage loan modifications, fair value measurement in illiquid markets, and accounting for asset-backed commercial paper and structured financial instruments. The agencies provided input as needed to the FASB as it developed revised accounting and disclosure standards governing securitization transactions, off-balance sheet entities, and various aspects of fair value measurement and other-than-temporary impairment of investment securities. The FASB issued exposure drafts of those revised standards on September 15, 2008. The agencies are participating in a number of roundtable meetings with various market participants in order to ensure that they have a thorough understanding of how the proposed accounting changes would affect banking organizations from a regulatory perspective.

In June 2008, the Federal Reserve Board and the OCC joined with the SEC to issue a letter to certain public banking organizations encouraging better disclosures of off-balance sheet risk. The statement encourages banking organizations that make significant use of off-balance sheet entities to review, assess, and as appropriate enhance the risk disclosures they make to the public in line with recommendations made in an April 7, 2008, report by the Financial Stability Forum titled, *Enhancing Market and Institutional Resilience*.

Mechanisms to Coordinate Supervision

The agencies, in conjunction with state supervisors, have a number of formal and informal mechanisms to foster continued coordination in examining and supervising banking organizations.

Federal Financial Institutions Examination Council

The Federal Financial Institutions Examination Council (FFIEC) is a legislatively established body responsible for promoting uniform supervisory policies and establishing uniform principles, standards, and report forms for examinations of depository institutions. The member agencies of the FFIEC are the agencies and the National Credit Union Administration (NCUA). As the result of legislation in 2006, the Chair of the FFIEC State Liaison Committee serves as a sixth member of the FFIEC. The State Liaison Committee is composed of five representatives of State agencies that supervise financial institutions. Through its State Liaison Committee, the FFIEC serves as an important forum for promoting uniform examination principles and standards by federal and state supervisory agencies.

To foster interagency cooperation, the FFIEC has established interagency task forces on consumer compliance, examiner education, information sharing, reports, surveillance systems, and supervision. These task forces share information and coordinate activities on a wide range of supervisory issues.

Joint Supervisory Training Courses and Conferences

The FFIEC's Examiner Education Office offers a variety of schools, conferences, and workshops for the agencies' examiners. These courses are also made available to examiners from the state supervisory agencies. A listing of course offerings and schedules is available on the FFIEC's website at www.ffiec.gov/exam/education.htm.

The agencies also sponsor conferences to discuss emerging supervisory concerns. For example, the agencies' chief accountants sponsor an annual conference to discuss emerging accounting and auditing issues with the agencies' examiners and accounting staff. The 2008 conference, attended by approximately 360 participants, included discussions on fair value accounting, accounting for impaired assets, and other accounting issues associated with market disruption, as well as updates from the SEC, the FASB and the Public Company Accounting Oversight Board (PCAOB). In August 2008, the agencies also sponsored the annual Information Technology conference, which was attended by over 225 federal and state examiners. This conference provided advanced training on emerging issues in data security, identity theft, pandemic planning, and remote deposit capture. The agencies also sponsored the second Advanced Bank Secrecy Act/Anti-Money Laundering (BSA/AML) Specialists Conference which was attended by over 200 participants. Topics of the conference included emerging payments, remote deposit capture and trade finance.

Common Reporting Forms and Examination Tools

The agencies routinely collaborate on and adopt common reporting forms and examination tools, with a goal of streamlining and reducing burden where possible. For example, the agencies use interagency forms with respect to filings under the Bank Merger Act and the Change in Bank Control Act. Furthermore, through the FFIEC Task Force on Reports, the agencies have established a number of common reporting forms filed by commercial and state-chartered savings banks and by U.S. branches and agencies of foreign banks.

The FDIC, Federal Reserve Board, and state supervisory agencies have an automated examination support system that includes a common risk-focused supervision framework and loan review tool. Similarly, the agencies, in partnership with the Conference of State Bank Supervisors (CSBS), have developed a standardized electronic loan file format that examiners can use to facilitate community and mid-size bank safety and soundness examinations. The Federal Reserve, in consultation with the other FFIEC agencies, maintains the Funds Transfer Examination Work program and makes it available to the state supervisory agencies, as well as to the FFIEC member agencies.

Supervisory Information Sharing and Coordination

To the extent possible, the agencies build upon each other's supervisory reviews and databases to promote comprehensive supervision and to minimize regulatory burden. The agencies routinely share reports of examination, inspection reports, and other agency-institution communications. The agencies also provide each other with access to their organizations' structural, financial, and supervisory information. Meetings and discussions take place among the agencies throughout the year and, when appropriate, the agencies hold joint meetings with institutions involving matters of mutual interest. This approach extends to periodic coordinated reviews or examinations where a business activity is conducted across legal entities.

The agencies coordinate supervisory efforts related to large, complex entities to ensure consistency in supervisory approaches and to reduce duplication of effort. The agencies routinely share institution risk profile information and other supervisory data regarding the entities they supervise and exchange information on proposed examination and supervisory activities. Agency staffs also meet periodically to discuss issues related to complex financial institutions, and select staffs participate in joint examinations or targeted reviews.

As discussed earlier in this report, the agencies closely collaborated in their efforts to monitor and respond to the recent turmoil in the mortgage and credit markets. These efforts have included periodic meetings among the agencies' senior supervisory staffs to share information on conditions in key market sectors and about financial institutions, to identify potential issues, and to coordinate regulatory responses. Similarly, the agencies' examination staffs are coordinating efforts on various information requests, as appropriate, so as to obtain needed information while minimizing unnecessary burden.

The FFIEC's Task Force on Information Sharing serves as a vehicle to enhance and improve the exchange of electronic information among the agencies. This group is responsible for establishing principles that protect the privacy, security, and integrity of shared information. It also oversees the development of data management standards to improve consistency and encourages the development of compatible technical architectures among the agencies to ensure that information can be shared efficiently.

The FFIEC's Task Force on Consumer Compliance oversees the agencies' collection, processing, and dissemination of information collected pursuant to the Home Mortgage Disclosure Act (HMDA) and Community Reinvestment Act (CRA).

The FFIEC's Task Force on Supervision Information Technology Subcommittee (ITS) collaboratively manages the implementation of policies and procedures, such as stronger internet authentication and general information technology security standards, to ensure consistent treatment for institutions across all charters. The ITS additionally manages the coordinated supervision of financial institution technology service providers and publishes extensive standard examination tools.

The FDIC, Federal Reserve, and state bank supervisors continue to coordinate their efforts via a protocol for the prudential supervision of state-chartered commercial and savings banks. Under this protocol, the home state supervisor and appropriate federal regulator coordinate the supervision of interstate state-chartered banks to ensure a risk-focused process and to reduce regulatory burden. The OTS works closely with individual state supervisors to coordinate the supervision and examination of state savings institutions.

The agencies have executed Memoranda of Understanding (MOUs) regarding the sharing of confidential supervisory information with state insurance regulators to allow the agencies to rely, to the fullest extent possible, on the functional regulators of insurance activities, pursuant to mandates established in the Gramm-Leach-Bliley Act. The agencies have exercised their authority under these MOUs in the context of the supervision of institutions with regulated insurance entities.

Emergency Preparedness and Response

Through the FFIEC's Task Force on Supervision, the agencies have established a protocol for supervisory communications to be used in emergency situations, the FFIEC

Supervisory Emergency Communications Protocol. This protocol is updated quarterly and tested at least annually with key supervisory personnel to ensure its ongoing effectiveness. The protocol includes information that would facilitate coordination during a pandemic event.

The agencies, together with other federal and state financial regulators, are members of the Financial Banking Information Infrastructure Committee (FBIIC), which was formed to address and coordinate issues related to the security and resilience of the U.S. financial sector. In January 2008, the FBIIC and the Financial Services Sector Coordinating Council (FSSCC), an organization of financial services trade associations and individual firms, published an after-action report from a pandemic flu exercise held in September and October 2007 for the financial services sector in the United States. Objectives of this exercise were to enhance the understanding of systemic risks to the sector, to provide an opportunity for firms to test their pandemic plans, and to examine how the effect of a pandemic flu on other critical infrastructures could impact the financial services sector. A total of 2,775 organizations participated in the exercise, of which approximately 62 percent were banks, thrifts, and credit unions. The after-action report noted that the majority of participants had made significant progress in preparing for a pandemic; however, nearly all of the participating institutions identified opportunities to improve their contingency plans. The exercise revealed several key themes that are important to pandemic planning: communications plans, infrastructure dependency plans, cross-trained employees, telecommuting, human resources issues, and second wave pandemic plans.

In addition, the FBIIC has established emergency communication protocols to maintain effective communication among members in the event of an emergency. The agencies, as members of the FBIIC, will convene via conference call no later than 90 minutes following the first public report of an event to share situational and operational status reports. Each FBIIC member is then responsible for establishing and maintaining communication with the institutions for which they have primary supervisory authority as well as to ensure coordination between public affairs and media relations staffs. The FBIIC protocols have been activated in 2008 for the Midwest flooding event, all significant hurricanes that made landfall in the United States, and the white powder HazMat incident.

The FFIEC's Task Force on Supervision established a Pandemic Working Group to coordinate planning and supervisory efforts that may be needed during a pandemic event. Throughout 2008, the Working Group engaged in several projects designed to help the agencies prepare for supervision through a pandemic event. The Working Group sponsored a Roundtable on Pandemic Planning, which had approximately 170 industry attendees, including some international participants. The FFIEC's *Business Continuity Planning Booklet* was updated in March 2008 to include guidance on identifying the continuity planning that should be in place to minimize the potential adverse effects of a pandemic event. The Working Group also engaged in dialogue with the industry surrounding potential industry needs for regulatory relief in the event of a pandemic. An emergency preparedness, response, and recovery meeting was held in March 2008 among the FFIEC members and industry trade group representatives. A second meeting was held in September 2008.

Other Coordinated Supervisory Activities

Where applicable, the agencies coordinate their supervisory activities related to insurance, securities, and banking businesses with functional regulators, such as the SEC and state insurance regulators. Periodic cross-sector meetings with representatives of the agencies, the SEC, state banking, insurance, and securities supervisors, and the CFTC are held to identify areas that may require supervisory attention and coordination. In 2008, the agencies consulted with the SEC on the development of recordkeeping rules under the bank broker provisions of the Gramm-Leach-Bliley Act.

The agencies recognize the importance of high quality accounting and auditing standards to the continued safe and sound operation of insured depository institutions and work closely with the SEC, the FASB, the International Accounting Standards Board (IASB), the American Institute of Certified Public Accountants (AICPA), the PCAOB, and the International Auditing and Assurance Standards Board (IAASB) on matters of mutual interest. The agencies routinely collaborate on supervisory guidance to address safety and soundness concerns that arise from accounting and auditing matters. The agencies also work together to provide commentary on proposals by the various accounting and auditing standards setters that may have a significant impact on the banking industry.

The agencies and state banking regulators coordinate supervisory efforts relating to BSA/AML, counter-terrorist financing, and Office of Foreign Assets Control (OFAC) sanctions compliance. These efforts include refining the agencies' risk-focused approach to BSA/AML examinations and working toward increased consistency in supervision across the agencies. The agencies and CSBS meet regularly under the auspices of the FFIEC's BSA/AML Working Group, which is responsible for updating the FFIEC BSA/AML Examination Manual and the content of interagency BSA/AML training. The agencies maintain regular communication with the Treasury Department's Financial Crimes Enforcement Network (FinCEN) and OFAC regarding BSA/AML matters and sanctions developments, respectively; the agencies are required to provide supervisory information to those Treasury offices in accordance with existing MOUs. The agencies also participate actively in the Bank Secrecy Act Advisory Group, a Treasury-led group with representatives from industries subject to the BSA, regulators, and law enforcement that provides feedback and recommendations on the administration of the BSA.

Insurance specialists from the agencies communicate regularly on an interagency basis with staff of the National Association of Insurance Commissioners, the organization that supports the insurance regulatory officials of the 50 states, the District of Columbia, and the five U.S. territories/commonwealths, on topics of mutual interest to the agencies and state insurance regulators.

International Supervision Coordination

The agencies participate on a number of international supervisory groups, including the BCBS and the Joint Forum, which promote more consistent and uniform supervision of internationally active financial services firms. These groups have a number of work streams underway to evaluate lessons learned and to assess whether additional policy actions are needed in response to recent market events. The agencies also participate in the Association of Supervisors of Banks of the Americas (ASBA), which promotes international standards for effective banking supervision in the Americas region. In 2008, under the auspices of the BCBS, the biennial International Conference of Bank Supervisors was held in Brussels, Belgium, with all agencies actively participating.

The agencies provide training for staff and officials from non-U.S supervisory authorities and foreign central banks. During the year, the agencies offered training courses exclusively for foreign supervisory authorities in Washington, D.C., and in a number of foreign jurisdictions. Staff at the agencies also took part in technical assistance and training missions led by the International Monetary Fund, the World Bank, the Asian Development Bank, the BCBS, the Financial Stability Institute, South East Asian Central Banks Research and Training Center (SEACEN) and ASBA. This training was concentrated in Latin and South America, Asia, the Middle East, Africa, and Eastern Europe.

In support of the United States Partnership for Financial Excellence in the Middle East and North Africa (MENA), the agencies worked with the U.S. Treasury Department, the U.S. State Department, and the U.S. Agency for International Development to design and deliver training programs aimed at improving banking supervision in the MENA region.

In 2008, the agencies participated in the third annual bi-lateral meeting with representatives of the China Bank Regulatory Commission which focused on sharing supervisory concerns and practices. The agencies also met collectively with the Peoples Bank of China on issues related to bank secrecy and development of methods for deposit insurance and oversight of credit rating agencies. The agencies have also assisted the U.S. Treasury Department in the U.S.-Latin America Private Sector Dialogues. In 2008, two sessions were held in Miami, Florida, and Sao Paulo, Brazil. The meetings focused on developing a communication between U.S. and Latin American banks regarding common issues related to money laundering and terrorist financing.

The agencies supported training activities delivered under the Asia Pacific Economic Cooperation Financial Regulators Training Initiative, which was launched by the U.S. Treasury Department shortly after the Asian crisis. Administrative and funding support for this initiative is provided by the Asian Development Bank. Also, the agencies have supported the State Department through the Terrorist Finance Working Group by providing training for foreign supervisors and technical assistance to designated countries related to money laundering and terrorist financing risks.

Federal and state supervisory agencies coordinate the supervision of U.S. operations of foreign banking organizations through the Foreign Banking Organizations Supervision Program, which involves extensive interagency information sharing and supervisory collaboration. The agencies coordinate with numerous foreign regulatory authorities in the supervision of internationally active companies and, when appropriate, jointly enter into multilateral statements of cooperation with foreign bank supervisors. For example, the agencies are working closely with foreign supervisors to coordinate home/host issues associated with the implementation of the Basel II Capital Accord and in monitoring and assessing the potential effects that recent market disruptions may have on global financial institutions and market operations.

The agencies represent the United States annually at an international information sharing conference focused on technology risks and risk management practices. The 2008 Information Technology Supervisors Group (ITSG) Conference convened in Rome, Italy, and included financial institution supervisory agencies from seventeen countries. Discussion topics included information security, outsourcing, IT auditing, pandemic event planning, and Basel II AMA for operational risk preparedness.

Formal Joint Examination Programs

In addition to the coordination mechanisms discussed above, the agencies also have three formal joint examination programs that allow them to leverage and share examination resources and provide consistent supervisory evaluations of activities that often cut across financial institutions.

Shared National Credit Program

The Shared National Credit (SNC) program is a joint effort of the agencies to collaborate on reviewing large syndicated loans held by multiple regulated entities. The SNC program reviews selected borrowers using interagency teams to avoid duplicate reviews of the same credit and to ensure consistent treatment. The agencies release to the public aggregate statistical data from the SNC program, which provides a unique perspective on credit quality trends across supervised institutions. In 2008, this program covered 8,746 credits totaling $2.8 trillion in credit commitments to 5,742 borrowers.

The agencies are continuing their work on a SNC modernization initiative to standardize the SNC data collection process, expand SNC data collected from large reporting institutions, apply advanced credit risk benchmarking techniques for common SNC borrowers and portfolios, and provide reporting banks with feedback on their commonly held SNC portfolios. Activities continue on efforts to improve and modernize the program.

Multi-Regional Data Processing Servicer and Shared Application Software Review Programs

Under the auspices of the FFIEC's IT Subcommittee of the Task Force on Supervision, the FFIEC member agencies administer two programs that support the assessment of the technology environment for institutions that (1) outsource their technology services and automated processing activities, or (2) rely on off-the-shelf applications to run their core banking systems. Examinations of service providers under the Multi-Regional Data Processing Servicer (MDPS) program are coordinated on a national level. The program targets organizations considered by the agencies to present the most risk to the financial system due to the mission-critical nature of their services and the breadth of their client base, or because a provider processes work from operations over a sufficiently diverse geographic footprint. Conducting the service provider examinations jointly is a more efficient and effective utilization of the agencies' IT examiners. Administration by the IT Subcommittee results in a risk-focused exam approach for each firm that addresses its unique risk profile while promoting consistency of supervision across the MDPS firms. Interagency examinations of smaller regional technology service providers are also conducted based on principles of the MDPS program and *FFIEC IT Examination Handbook*, but are administered at a regional level.

In 2008, the IT Subcommittee also updated an agency-based inventory of the foreign-based outsourcing activities of supervised financial institutions. The inventory provided current data on the financial institutions that utilize foreign-based technology service providers, including the volume and types of outsourcing activities, and whether they have access to confidential information.

The Shared Application Software Review program provides a tool for the agencies to review and share assessments of mission-critical software packages, such as wire transfers, capital markets, loans, deposits, and general ledger applications that are used by a large number of financial institutions. These assessments are designed to reduce the time and resources needed to examine mission-critical processing activities at each of the user financial institutions. The IT Subcommittee has initiated a project to enhance this program.

Interagency Country Exposure Review Committee (ICERC)

The FDIC, Federal Reserve Board, and OCC formed ICERC in 1979 to ensure consistent treatment of the transfer risk associated with financial institutions' foreign exposures to public and private sector entities. The OTS joined ICERC in 2006 as an observing non-voting agency. New York State banking regulators also regularly attend the annual ICERC meeting.

At their October 2008 ICERC meeting, the agencies approved changes to the ICERC procedures and rating systems that will make the supervision of cross-border exposures more efficient and risk-focused. Such changes maintain strict regulatory attention to areas of transfer risk, but now also include discussions of regional and global macro trends that might indicate future areas of risk. ICERC continues to determine the appropriate classification and level of reserves for countries that are in default. ICERC decisions and analytical write-ups are used by the agencies to help examination teams assess individual institutions' cross-border risk.

Other 2008 Activities

Revisions to Risk-Based Capital Standards

In addition to the capital-related actions discussed previously, the agencies continued their implementation of the advanced approaches under the Basel II Capital Accord, issued in final form by the BCBS in June 2006. The agencies issued a final rule implementing the advanced approaches of Basel II on December 7, 2007. The rule went into effect on April 1, 2008. Institutions may begin transitioning to the new rules after they adopt an implementation plan and have systems that comply with the final rule's qualification requirements. In January 2008, the agencies published final reporting requirements and reporting templates for institutions that will be adopting the Basel II advanced approaches.

On June 26, 2008, the agencies issued a notice of proposed rulemaking to adopt the standardized approaches of the Basel II Capital Accord. The comment period ended on October 27, 2008. The agencies are reviewing and considering the comments received.

Joint Residential Mortgage Lending Initiatives

In 2007, the Federal Reserve Board, the OTS, the Federal Trade Commission (FTC), the CSBS, and the American Association of Residential Mortgage Regulators announced a pilot project to conduct targeted consumer-protection compliance reviews of selected non-depository lenders with significant mortgage operations. The agencies concluded the onsite portion of these reviews during 2008 and are working together to ensure consistent treatment of any issues identified. The agencies plan to continue to collaborate in determining the lessons learned from these reviews and in seeking ways to improve enforcement for all categories of mortgage lenders. The agencies also issued guidance extending CRA consideration in the Hurricanes Rita and Katrina disaster areas for an additional 36 months.

More generally, the agencies continue to support efforts by depository institutions and other groups to assist borrowers who may be facing difficulties with their mortgage obligations. These efforts include those initiated by the American Securitization Forum and HOPE NOW Alliance, as well as activities pursuant to the Housing and Economic Recovery Act of 2008. The agencies, in response to the industry's adoption of streamlined loan and modification programs, implemented revised tracking procedures to monitor their institutions' progress relative to loan modifications. In addition, as part of the revised CRA Questions and Answers, the agencies have confirmed that lending activities that are likely to be responsive in helping to meet the credit needs of communities include loan programs that provide relief to homeowners who are facing foreclosure on their primary residences. The agencies also participated in several regional CRA-focused roundtables. Topics discussed included strategies for encouraging lower-income households to save and small business development.

As previously noted, the OCC and OTS implemented a standard reporting framework for the nine national banks and five savings associations with the largest mortgage servicing portfolios. Combined, these portfolios represent approximately 60 percent of all first-lien residential mortgages in the United States. This information is used to provide quarterly reports to the public and key stakeholders on mortgage delinquencies, loss mitigation actions and foreclosures.

Throughout 2008, the agencies participated in a series of foreclosure prevention symposiums. These day-long sessions provided valuable information to financial institutions and other community stakeholders on how to facilitate individuals at risk of foreclosure contacting their servicers or legitimate foreclosure counseling agencies.

Finally, the agencies continued efforts to improve disclosures that consumers receive about various mortgage products. In May 2008, the agencies issued *Final Illustrations of Consumer Information for Hybrid Adjustable-Rate Mortgage Products*. The illustrations, intended to help consumers understand these mortgage products, consist of: (1) an explanation of some key features of products covered by the agencies' *Statement on Subprime Mortgage Lending*, which became effective in July 2007; and (2) three charts with examples of the potential payment shock accompanying these types of loans. In August 2008, the Federal

Reserve Board and the OTS published a substantially revised brochure called *A Consumer's Guide to Mortgage Refinancing* to guide consumers on mortgage refinancing. The publication was prepared in response to a request from the House Committee on Financial Services and in consultation with more than a dozen regulatory agencies and national organizations.

Revisions to Appraisal and Evaluation Guidelines

In November, the agencies and NCUA jointly issued for public comment proposed *Interagency Appraisal and Evaluation Guidelines,* which would replace the current version, dated October 27, 1994. The proposed guidelines incorporate recent supervisory issuances and reflect changes in industry practice, uniform appraisal standards and available technologies. The initiative is intended to respond to heightened concerns over appraisals and credit quality.

Building on the existing federal framework, the proposed guidelines clarify risk management principles and internal controls for ensuring depository institutions' real estate collateral valuations (appraisals and evaluations) are reliable and support their real estate-related transactions. Volatility within certain real estate markets and associated credit risk underscore the importance of independent and reliable collateral valuations. Among other revisions, the proposal includes additional detail on the agencies' expectations for an independent appraisal and evaluation program. It also includes an expanded discussion of portfolio management techniques. The public comment period ended on January 20, 2009.

Initiatives to Support the Preservation of Minority Depository Institutions

In 2008, the agencies sponsored the Interagency Annual Minority Depository Institutions National Conference for minority depository institutions to address a wide range of issues regarding the challenges these institutions face. The conference included discussions with agency principals, senior level policymakers, and industry speakers on current and emerging issues such as the state of the economy as it relates to mortgage markets and the current credit environment. Several breakout sessions were conducted on topics such as credit risk, credit administration, developing profitable lines of business, and the Community Development Financial Institutions Fund certification process. The event provided a unique opportunity for bankers, regulatory officials, and private industry representatives to engage in a comprehensive discourse on challenges, best practices, and upcoming developments relative to ensuring the long-term success and preservation of minority-depository institutions.

Initiatives to Enhance Consumer Protection Safeguards and Disclosures

In 2008, the agencies continued to closely coordinate rulemaking and other initiatives to enhance various consumer protection safeguards and disclosures. These included the following:

- <u>Proposed Revisions to Interagency Questions and Answers Regarding Flood Insurance</u>. In March 2008, the agencies, along with the NCUA and Farm Credit System, requested public comment on new and revised interagency questions and answers regarding flood insurance. The agencies proposed substantive as well as technical revisions to existing guidance to help financial institutions meet their responsibilities under federal flood insurance legislation and to increase public understanding of the flood insurance regulations. Final action on these proposed revisions is expected this year.

- Regulations and Guidelines of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act).
    - In November 2007, the agencies, along with the FTC, issued final regulations and guidance to help prevent identity theft. These regulations and guidelines were effective on January 1, 2008, with compliance required by November 1, 2008.
    - The agencies and the FTC also proposed regulations and guidelines intended to enhance the accuracy and integrity of information furnished to consumer reporting agencies (CRAs) in December 2007. The agencies and the FTC expect to finalize these issuances in 2009.
    - In May 2008, the Federal Reserve Board and the FTC proposed regulations that generally would require a creditor to provide a consumer with a risk-based pricing notice when, based in whole or in part on the consumer's credit report, the creditor offers or provides credit to the consumer on terms less favorable than the term it offers or provides to other consumers. The agencies expect to finalize these regulations in 2009.
- Final Regulations on Unfair or Deceptive Acts or Practices. In December 2008, using their authority under the Federal Trade Commission Act, the Federal Reserve Board, the OTS, and the NCUA finalized regulations that prohibit certain unfair credit card practices. For example, the rules will protect consumers from unexpected interest charges, including increases in the rate during the first year after account opening and increases in the rate charged on pre-existing card balances, forbid banks from imposing interest charges using the "two-cycle" billing method, require that consumers receive a reasonable amount of time to make their credit card payments, prohibit the use of payment allocation methods that unfairly maximize interest charges, and address subprime credit cards by limiting the fees that reduce the amount of available credit. Compliance is required by July 1, 2010, although the agencies strongly encouraged institutions to implement them as soon as reasonably possible.
- Updated Distressed and Underserved Nonmetropolitan Middle Income Geographies. In May 2008, the agencies announced the availability of the 2008 list of distressed or underserved nonmetropolitan middle-income geographies where bank revitalization or stabilization activities will receive CRA consideration as "community development." As in past releases, the 2008 list incorporates a one-year lag period for geographies that were designated as distressed or underserved in 2007, but were not designated as such in the 2008 release. Geographies subject to the one-year lag period are eligible to receive consideration for community development activities for the 12 months following publication of the 2008 list. "Distressed nonmetropolitan middle-income geographies" and "underserved nonmetropolitan middle-income geographies" are designated by the agencies in accordance with their CRA regulations.
- Improved Financial Privacy Notices. The agencies are working with the CFTC, the FTC, and the SEC on an interagency initiative to design and test a financial privacy notice that is clear and that consumers can understand and use to exercise their preferences for information sharing. The interagency working group initiated a project to develop a prototype privacy notice and test the effectiveness of that notice. The design work was completed in 2006. The agencies then arranged to test the effectiveness of the newly-designed form; this work was done in the late summer 2008, and results are forthcoming. The agencies are in the process of finalizing the model form, which is a part of the privacy rules that implement requirements of the Gramm-Leach-Bliley Act.

- Report to Congress on Information Sharing Practices with Affiliates. Section 214(e) of the Fair and Accurate Credit Transaction Act of 2003 directs the agencies, as well as the FTC, to report to the Congress on the information sharing practices of financial institutions, creditors, or users of consumer reports with their affiliates. These agencies are required to jointly submit the report together with any recommendations for legislative or regulatory action. During 2008, each agency conducted a survey of a limited number of regulated entities under its supervision. The agencies will review the survey results and report to the Congress later this year.
- Identity Theft Brochure. In December, the agencies and NCUA published a brochure titled: *You Have the Power to Stop Identity Theft.* The brochure illustrates a method of identity theft called phishing and provides a number of measures consumers should take to minimize their risks of victimization. The brochure further informs consumers of actions to take should they become victim to identity theft.

Improving Consumer Complaint Service

In 2008, the Interagency Consumer Complaint Working Group, under the auspices of the FFIEC, continued efforts to simplify the complaint filing process for consumers. These efforts have included the establishment of a "Consumer Information Center" through the addition of a consumer webpage to the existing FFIEC website. The webpage will assist consumers in identifying the appropriate regulator and will provide links to the appropriate regulator's consumer complaint webpage. This new webpage became operational on December 1, 2008. The agencies also have issued a Request for Information to solicit information from federal government and private sector third party vendors for the implementation of a call center using a unique 1-800 number to assist consumers in identifying the appropriate banking regulator. The call center number would not replace existing agency 1-800 numbers but will merely direct all calls to the appropriate regulator.

In addition, the working group continues to meet regularly to share complaint data and discuss potential ways that the data might be used to identify emerging issues and aid in the development of consumer education materials. The group, which includes representatives from the CSBS, developed and held a national conference in April 2009.

Updated Interagency Examination Procedures

The agencies published a number of new or updated examination procedures. These included the following:

- FFIEC Business Continuity Planning Booklet. In March 2008, the FFIEC issued an update to this booklet, which is included in the series of booklets that form the *FFIEC Information Technology Examination Handbook.* The revised booklet includes enhancements to the business impact analysis and testing discussions and addresses emerging threats such as pandemic planning and lessons learned from Hurricanes Katrina and Rita. The booklet also stresses the responsibilities of each institution's board and management to address business continuity planning with an enterprise-wide perspective by considering technology, business operations, communications, and testing strategies for the entire institution.
- FFIEC Guidance on Risk Management of Remote Deposit Capture. In January 2009, the FFIEC issued guidance on remote deposit capture (RDC) systems. The guidance addresses

the essential elements of RDC risk management: identifying, assessing, and mitigating risk, as well as measuring and monitoring residual risk exposure. The guidance also discusses the responsibilities of senior managers in overseeing the development, implementation, and operation of RDC in their financial institutions

- Talent Amendment. In July 2008, the agencies finalized and issued examination procedures to be used when determining compliance with regulations issued by the Department of Defense (DoD) regarding limitations on consumer credit extended to service members and their dependents. The regulations implement the consumer protection provisions of the John Warner National Defense Authorization Act for Fiscal Year 2007. The DoD regulations cover payday loans, motor vehicle title loans, and tax refund anticipation loans, as defined by DoD, and apply to all persons engaged in the business of extending such credit and their assignees.
- Truth in Savings Act. In July 2008, the agencies updated examination procedures for Regulation DD (Truth in Savings). The updated procedures incorporated amendments to the regulation related to electronic disclosures and changes to address recommendations made by the Government Accountability Office in its Report on Bank Fees issued in January 2008.
- Fair Credit Reporting Act. In 2008, the agencies approved examination procedures for regulations implementing several sections of the FCRA, as amended by the FACT Act. The examination procedures addressed regulatory provisions that focused on the duties of users of consumer reports regarding address discrepancies; duties of financial institutions and creditors regarding the detection, prevention, and mitigation of identity theft; duties of card issuers regarding changes of address; and duties of financial institutions regarding affiliate marketing practices.
- Updated Procedures for Electronic Consumer Disclosures. In August 2008, examination procedures were updated for Regulations E (Electronic Fund Transfers), Z (Truth in Lending) and M (Consumer Leasing) to reflect regulatory changes that clarified requirements for electronic consumer disclosures.

Initiatives to Reduce Unnecessary Regulatory Burden and Enhance Efficiency

Section 604 of the Financial Services Regulatory Relief Act of 2006 requires the agencies to review the content of "Reports of Condition" within one year of enactment and then to use the results as a basis for eliminating or reducing any unnecessary or inappropriate information collected in these reports. The FFIEC's Task Force on Reports surveyed 165 user groups within the agencies and CSBS to identify the purposes for which each group uses each reported data item, the extent of usage for each item, and the frequency with which each item is needed. The survey results were evaluated and reported to the FFIEC principals in October 2007. In 2008, the Task Force considered the information received from the survey to determine where possible burden-reducing revisions may be made in the reports of condition. Based on the Task Force's evaluation, in September 2008, the agencies proposed reductions to the Reports of Condition and Income that became effective as of March 31, 2009.

Conclusion

The agencies are committed to maintaining regulatory and supervisory processes that maximize efficiency, while eliminating unnecessary costs to institutions, maintaining safety and soundness, and safeguarding consumers. The agencies have worked in the past year—and will continue to work—to improve the supervisory process by reducing regulatory burden, promoting consistency, eliminating duplicative activities in the examination process, and promoting greater efficiency in the use of resources. Coordination and streamlining efforts have been successful thus far, and we intend to continue exploring ways in which the agencies can work together, leverage each other's efforts, and ease the regulatory burden on the financial institutions the agencies supervise.

Sincerely,

Daniel K. Tarullo, Governor
Board of Governors of the
Federal Reserve System

Sheila C. Bair, Chairman
Federal Deposit Insurance Corporation

John C. Dugan
Comptroller of the Currency

John E. Bowman, Acting Director
Office of Thrift Supervision