



**BOARD OF GOVERNORS**  
OF THE  
**FEDERAL RESERVE SYSTEM**

WASHINGTON, D.C. 20551

DIVISION OF BANKING  
SUPERVISION AND REGULATION

**SR 16-8**

**April 19, 2016**

**TO THE OFFICER IN CHARGE OF SUPERVISION  
AT EACH FEDERAL RESERVE BANK**

**SUBJECT: Off-site Review of Loan Files**

**Applicability to Community Banking Organizations:** This letter applies to all state member banks and U.S. branches and agencies of foreign banking organizations with less than \$50 billion in total assets.

The purpose of this letter is to announce to state member banks (SMBs) and U.S. branches and agencies of foreign banking organizations (FBOs) with less than \$50 billion in total assets that there is an option to have Federal Reserve examiners review loan files off-site during full-scope or target examinations. Federal Reserve examiners may conduct an off-site loan review provided the SMB or FBO is amenable to such an arrangement, and the SMB or FBO can send legible and sufficiently comprehensive loan information to the Reserve Bank in a secure manner.

To date, most of the Federal Reserve's off-site examination work has focused on financial performance analyses and the review of bank policies, procedures and certain bank internal reports.<sup>1</sup> However, with technological advancements, such as secure data transmission and electronic file imaging, examiners now have the ability to collect and review loan file information off-site without compromising the effectiveness of the examination process. As a result, Federal Reserve examiners may use the off-site loan review program when leading examinations of SMBs and FBOs with less than \$50 billion in total assets where the bank has communicated its willingness to participate in the program and is able to appropriately image and send its loan documents to the Reserve Bank in a secure manner.

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<sup>1</sup> Refer to SR letter 95-13, "Recommendations to Increase the Portion of Examinations and Inspections Conducted in Reserve Bank Offices."

## **Process for Determining if an SMB or FBO can Participate in the Off-Site Loan Review Program**

Reserve Banks should query an SMB or FBO prior to conducting an examination to confirm the institution's interest in participating in the off-site loan review program.<sup>2</sup> SMBs or FBOs interested in participating in the program should be prepared to demonstrate their ability to appropriately image and send loan documents to the Reserve Bank in a secure manner. The Reserve Bank will consider the following when determining whether an off-site review of loan files is appropriate for a particular institution.

- Will the institution submit the loan file data using a secure transmission method such as cloud-based collaboration products, secure email services, encrypted removable media, virtual private networks, or remote desktop control services?
- Is the institution able to provide loan data and imaged loan documents that are legible, easily viewable, and properly organized to allow for timely review by examiners?
- Are the loan files comprehensive to allow an examiner to come to a conclusion as to the appropriate rating of a credit without having to request additional information from the institution?

For SMBs or FBOs that have demonstrated these technological capabilities, Reserve Banks should make all efforts to accommodate the request for an off-site loan review. However, the Reserve Bank may decline a request if it has justifiable reasons to believe that an off-site review would impede the examiners from efficiently and effectively assessing the institution's asset quality and credit risk management process.

## **Security of Loan File Data Submitted to the Reserve Banks**

Loan file data obtained from an SMB or FBO will be handled in accordance with existing Federal Reserve information security requirements. A Reserve Bank should explain its procedures and practices for safeguarding loan file data to an SMB or FBO considering participation in the off-site loan review program, including its procedures for coordinating off-site loan reviews with state banking agencies.

## **Adjustments to the Examination Process**

Reserve Banks will need to adjust the examination process in order to ensure successful execution of an off-site loan review. Generally, examiners should allocate adequate time prior to the start of the examination to confirm that an SMB or FBO has successfully transmitted its loan file data to the Reserve Bank. Further, examiners are expected to maintain ongoing communication with the institution's management during the examination process. Prior to the start of the examination, examiners should establish a schedule with the institution's management for status calls during the off-site portion of the examination. Typically, examiners should conduct regular calls with management to discuss loan file review and the status of other examination work.

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<sup>2</sup> In order for a Reserve Bank to be able to complete an off-site loan review, an SMB or FBO will need to submit all requested information in a timely manner, including confirming its interest in being considered for the off-site review program and providing all information needed for a Reserve Bank to confirm the institution's technological preparedness.

## **Scope of the Off-Site Examination Work**

As directed in SR 95-13, Reserve Banks should continue to conduct as much of the examination work off-site as feasible without compromising the effectiveness of the examination process. Specific to loan review, examiners should typically conduct the following portions of examination work off-site regardless of whether the SMB or FBO is participating in the off-site loan review program. This examination work includes:

- Determination of the scope of the loan review;
- Risk assessment to determine the areas to be emphasized (for example, management of credit concentrations and the loan approval process);
- Review of the bank's loan policies;
- Review of financial performance reports and management reports;
- Preliminary review of the loan loss reserve methodology;
- Determination of the loans to be reviewed, and the selection of individual credits;
- Grouping of loans to related obligors; and
- Preparation of loan line sheets.

In addition, for SMBs or FBOs participating in the off-site loan review program, the review of credit files for quality, documentation, and compliance with bank policy and laws and regulations will be performed off-site. Further, at the discretion of the examiners, Reserve Banks may hold either off-site or on-site discussions with the institution's management regarding preliminary loan review findings such as the appropriateness of individual credit ratings assigned by the SMB or FBO and the completeness of credit file documentation.

## **Scope of On-Site Examination Work**

On-site examination work remains an indispensable component of bank supervision that plays a critical role in ensuring the Federal Reserve fulfills its supervisory responsibilities. As directed in SR 95-13, Reserve Banks are expected to continue to perform on-site those activities that require physical observation such as transaction testing and direct monitoring of an institution's operations and internal controls. While on-site, examiners will also review documents such as meeting minute books of the board of directors that would be inappropriate or impractical for the SMB or FBO to send to the Reserve Bank. Further, Federal Reserve examiners should conduct exit meetings in-person with the institution's management to communicate final supervisory findings and conclusions, including the final supervisory findings from any off-site loan review examination work.

Questions regarding this letter and the attached examiner guidance may be directed to the following staff in the Board's Division of Banking Supervision and Regulation:

- Community Banking Organizations: Anthony Cain, Manager, at (202) 912-4377; and Laura A. Macedo, Senior Supervisory Financial Analyst, at (202) 452-5268.
- Regional Banking Organizations: Keith Coughlin, Manager, at (202) 452-2056.

- Foreign Banking Organizations: Celeste Molleur, Manager, at (202) 452-2783, and Kwayne Jennings, Manager, at (202) 452-3088.

In addition, questions may be sent via the Board's public website.<sup>3</sup>

Michael S. Gibson  
Director

**Cross reference to:**

- SR letter 95-13, "Recommendations to Increase the Portion of Examinations and Inspections Conducted in Reserve Bank Offices"

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<sup>3</sup> <http://www.federalreserve.gov/apps/contactus/feedback.aspx>