



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D.C. 20551

DIVISION OF SUPERVISION
AND REGULATION

SR 19-5

March 7, 2019

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

SUBJECT: Communication Expectations for Community Bank Examinations and Inspections

Applicability: This guidance applies to the supervision of state member banks, bank holding companies and savings and loan holding companies with less than \$10 billion in total consolidated assets, including those that are part of a foreign banking organization's U.S. operations.

The purpose of this letter is to reinforce the importance of effective communication practices during targeted and full-scope safety and soundness examinations of community state member banks.¹ This letter summarizes and consolidates existing communication practices outlined in the *Commercial Bank Examination Manual* (CBEM)² and describes communication expectations that are integrated into the Federal Reserve's examination technology tools. These practices are intended to minimize disruption to a bank's operations and promote coordination among Federal Reserve examination staff and with staff at the other federal and state banking agencies.

Background

In 2016, the Federal Financial Institutions Examination Council (FFIEC) and its member agencies performed a review of their regulations, as required by the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA). The purpose of the review was to identify outdated or otherwise unnecessary regulatory requirements that imposed unnecessary regulatory burden on insured depository institutions. During outreach sessions for the EGRPRA review, community bankers indicated that certain routine examination practices were

¹ While this letter is directed at community bank examinations, some portions may apply to holding company inspections and should be adapted as appropriate to inspections of community sized bank and savings and loan holding companies, including those that are part of a foreign banking organization's U.S. operations.

² The CBEM is available on the Board's public website at:
<https://www.federalreserve.gov/publications/files/cbem.pdf>.

unnecessarily burdensome and that communication practices during the examination process could be improved.

In response, the FFIEC initiated the Examination Modernization Project in 2017 to identify opportunities to improve the efficiency of the safety-and-soundness examination process and reduce unnecessary burden on community banks.³ At outreach sessions conducted as part of the project, a number of community bankers stressed that communication practices before, during, and after the examination needed improvement. As a result, each FFIEC member committed to issuing guidance to examination staff to reinforce the importance of transparent communication during the examination process beginning with examiners contacting the bank to schedule the examination and concluding with the agencies issuing the report of examination.

Effective communication with supervised institutions is a priority, and Federal Reserve examiners should make every effort to implement each of the effective communication practices outlined in this letter. In cases in which certain of the outlined communication practices cannot be implemented and an exception is necessary, examiners should communicate to the bank the reasons for deviating from the practices.

Scheduling the Examination

The Reserve Bank examination staff contacts community bank management prior to an on-site examination in order to provide bank management adequate time to plan for the examination and address logistical issues for the on-site examination team. The examiner in charge (EIC), or a designee, should contact bank management eight-to-twelve weeks prior to the start date of the examination in order to communicate the proposed examination start and close dates and ensure that bank management and key bank staff are available during the proposed dates.⁴ Contacting the bank with the appropriate lead time allows examiners and bank management to reschedule certain supervisory activities if there are conflicts with previously-scheduled regulatory, audit, or loan reviews. At that time, bank management may also request that examiners review loan files off-site and make the necessary arrangements for Reserve Bank staff to obtain the technical information necessary to confirm that the bank can support an off-site review.⁵

When scheduling examinations, examination staff should follow existing guidance for coordinating supervisory activities with the appropriate federal and state banking agencies. This includes conducting alternate or joint examinations and meetings, and completing joint

³ For more information see the FFIEC Press Release, “FFIEC Provides Update of Examination Modernization Project,” ([March 22, 2018](#)).

⁴ The “start date” is the date that Reserve Bank examiners and supervisory staff commence examination work, excluding pre-exam visitations and preparation. The “close date” of an on-site examination is defined as the last date that the examination team is physically on-site at the institution. For examinations for which all or a portion of the work is performed off-site, the “close date” is defined as the earlier of the following dates: (1) the date on which the analysis, including loan file review, is completed and ready for the EIC to review; or (2) the date on which the preliminary exit meeting is held with management.

⁵ See SR letter 16-8, “Off-site Review of Loan Files.”

examination reports when feasible in order to improve the efficiency of the examination process and reduce administrative burden for the bank.⁶ In cases in which the Federal Reserve is not the primary federal regulator of every subsidiary bank under a multi-bank holding company, examiners should attempt to coordinate with the primary regulator(s) of the other banks within the holding company structure. When feasible, examiners should examine sister banks concurrently and coordinate meetings and information requests for centralized risk management and operation functions, such as audit, compliance, or credit review.⁷

Scoping the Examination

The Federal Reserve's existing supervisory practice is for examiners to contact bank management prior to finalizing the scope of the examination. Examiners generally discuss with bank management local economic conditions, regulatory compliance practices, the bank's audit function, and any changes since the prior examination to the board of directors, senior management, policies, strategic direction, management information systems, and products or markets served.⁸ Examiners should continue to summarize the results of these discussions in a memo and include these notes in the examination workpapers.

The Federal Reserve recognizes that banks may need additional time to prepare for an examination, particularly for allocating appropriate bank staff to support heavily-reviewed areas. Once the scope memo is finalized, Federal Reserve staff should provide bank management with the contact information of key examination personnel. More specifically, the EIC should verbally provide bank management with an overview of the preliminary scope of review and the size and composition of the examination team, including names, roles and responsibilities, workspace needs, and whether staff members will be working on-site or off-site. The EIC should also inform bank management of the approximate number of trainees that will participate in the on-site examination. The EIC should communicate to bank management any subsequent material changes to the scope of review.

The First Day Letter

To allow bank management sufficient time to gather all requested information, examiners should transmit a "first day letter" to the bank four-to-eight weeks prior to the examination start date. In addition, when submitting the first day letter, examiners should specify the as-of date for the data requested and note if updated data should be made available on-site. Examiners should also provide contact information for questions regarding the request list and for technical assistance regarding data transmissions.

Preparation Week

On or before the start date of the examination, the EIC should meet with the bank president or management team to discuss examination communication expectations in order to

⁶ See SR letter 04-12, "Supervision of State-Chartered Banks" and the CBEM, section entitled, "Examination Strategy and Risk-Focused Examinations."

⁷ See SR letter 96-33, "State/Federal Protocol and Nationwide Supervisory Agreement."

⁸ See CBEM section entitled, "Examination Strategy and Risk-Focused Examinations."

facilitate information exchange between bank and examination staff. At this meeting, the EIC should confirm how frequently the bank's senior management team would prefer to meet with the examination team (for example, daily, weekly, or as needed) to discuss the status of work completed and identified areas of concern. These meetings provide bank management opportunities to ask examiners questions about the areas under review and to receive additional information or clarification before the conclusion of the on-site portion of the examination.

At the start of the examination, the EIC and bank management should also discuss how examiners generally coordinate meetings, preferences for scheduled versus ad hoc meetings, and the use of video or audio conferencing with off-site examination staff. To minimize disruption to the bank's daily operations, the examination team should make a concerted effort to combine meetings that involve the same bank staff.

Requesting Additional Information after the Start of the Examination

The EIC should have a process for requesting additional documentation from bank staff that avoids duplicative requests. Suggested methods include: (1) requiring examiners to first review information already submitted prior to requesting new information; and (2) centralizing information requests through one designated examiner who must verify whether the information has already been provided.

Preliminary Exit Meeting

As described in SR letter 13-14, "Timing Standards for the Completion of Safety-and-Soundness Examination and Inspection Reports for Community Banking Organizations," the EIC should hold a preliminary exit meeting or close-out meeting with bank management, which can be conducted either on-site or off-site via conference call. In the exit meeting, the EIC should communicate preliminary supervisory findings to bank management, and bank management should take this opportunity to correct inaccuracies and share additional information that might change the conclusion.

At this meeting, the EIC also should provide bank management with a timeframe for issuance of the report of examination. Banks should receive supervisory findings in a timely manner. Current policy directs the Reserve Bank to send reports to the institution no more than 90 calendar days after the start date of the examination and no more than 60 calendar days after the close date of the examination.⁹ The issuance period shortens to 45 calendar days after the close date of the examination if the bank's composite rating is "3" or worse. Bank management should be notified if the report will not be issued within this timeframe.

The EIC should document in the workpapers findings and conclusions delivered at the preliminary exit meeting. At a minimum, documentation should include: (1) a list of attendees; (2) a description of significant examination findings discussed, including preliminary ratings; (3) a summary of the bank management's views on the findings; (4) and, if applicable, the views of the board of directors.

⁹ See SR letter 13-14.

Final Exit Meeting

Bank management and directors should have sufficient opportunities to discuss supervisory findings with examination staff. Reserve Bank staff should meet with the board of directors of the bank if the examination will result in a composite rating of “4” or “5,” or if the examination will result in a composite rating of “3” and the bank’s condition is deteriorating or shows little improvement since the previous examination.¹⁰ For all other community banks, examiners should offer to meet with the institution’s management and/or board of directors to discuss and answer questions about the examination process and findings. This offer may be communicated in writing in the examination report or verbally to the institution’s management and its directors.

The CBEM section entitled, “Meetings with Board of Directors,” provides guidance on the appropriate level of information examiners should communicate to boards of directors. Examiners should document all meetings with boards of directors.

When finalizing the examination report, examiners should communicate to bank management verbally or in writing whether the report will include any supervisory conclusions that differ from what was provided at the preliminary exit meeting, including the reasons for the differences.¹¹ Moreover, examiners should promptly notify bank management of any differences in order to give management as much time as possible to respond or provide additional information as appropriate. Examiners should carefully consider any information provided by bank management with respect to these differences in finalizing the report and should document any discussions with bank management on these issues in the workpapers.

Appealing Examination Findings

In instances in which bank management or its board of directors disagree with the examination findings, the Reserve Bank should inform bank management of the option to appeal. The Federal Reserve Board’s ombudsman policy statement contains procedures that management of institutions supervised by the Federal Reserve should follow to appeal examination findings or communicate other problems resulting from regulatory activities.¹²

Contact Information

Reserve Banks should distribute this letter to supervised institutions in their districts, as well as to appropriate supervisory and examination staff. Questions regarding this letter should be directed to the following individuals in the Division of Supervision and Regulation: Laura Macedo, Lead Financial Institution Policy Analyst, at (202) 452-5268; Anthony Cain, Manager,

¹⁰ See CBEM section, “Meetings with Board Directors,” for more information.

¹¹ See SR letter 13-14 and SR letter 13-13/CA letter 13-10, “Supervisory Considerations for the Communication of Supervisory Findings.”

¹² The ombudsman website is available at: <https://www.federalreserve.gov/aboutthefed/ombudsman.htm>.

at (202) 912-4377, or Kwayne Jennings, Manager, at (202) 452-3088. In addition, questions may be sent via the Board’s public website.¹³

Michael S. Gibson
Director

Cross References:

- SR letter 16-8, “Off-site Review of Loan Files”
- SR letter 13-14, “Timing Standards for the Completion of Safety-and-Soundness Examination and Inspection Reports for Community Banking Organizations”
- SR letter 13-13 / CA letter 13-10, “Supervisory Considerations for the Communication of Supervisory Findings”
- SR letter 04-12, “Supervision of State-Chartered Banks”
- SR letter 96-33, “State/Federal Protocol and Nationwide Supervisory Agreement”

¹³ See <https://www.federalreserve.gov/apps/contactus/feedback.aspx>.