



FEDERAL RESERVE BANK  
OF DALLAS

ROBERT D. McTEER, JR.  
PRESIDENT  
AND CHIEF EXECUTIVE OFFICER

DALLAS, TEXAS  
75265-5906

November 7, 1997

**Notice 97-105**

**TO:** The Chief Executive Officer of each  
financial institution and others concerned  
in the Eleventh Federal Reserve District

**SUBJECT**

**Examination of State-Chartered Community Banks**

**DETAILS**

Effective October 1, 1997, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation (FDIC), and the state banking departments began full implementation of a common risk-focused process for the examination of state-chartered community banks.

The process targets the activities posing the highest level of risk at each institution and enhances examiners' ability to diagnose emerging problems. Implementation of this process will provide greater consistency in examinations conducted by the Federal Reserve, the FDIC, and the states. The process is expected to result in examinations that are more efficient and effective and less burdensome on institutions.

**ATTACHMENT**

A copy of the Board's and FDIC's press release is attached.

**MORE INFORMATION**

For more information, please contact Marion White, (214) 922-6155, at the Dallas Office or Richard Burda, (713) 652-1503, at the Houston Office. For additional copies of this Bank's notice, contact the Public Affairs Department at (214) 922-5254.

Sincerely yours,

*Robert D. McTeer, Jr.*

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For additional copies, bankers and others are encouraged to use one of the following toll-free numbers in contacting the Federal Reserve Bank of Dallas: Dallas Office (800) 333-4460; El Paso Branch *Intrastate* (800) 592-1631, *Interstate* (800) 351-1012; Houston Branch *Intrastate* (800) 392-4162, *Interstate* (800) 221-0363; San Antonio Branch *Intrastate* (800) 292-5810.

For immediate release

September 30, 1997

The Federal Reserve Board, the Federal Deposit Insurance Corporation (FDIC), and the state banking departments will begin full implementation of a common risk-focused process for the examination of state-chartered community banks effective October 1, 1997.

The process targets the activities posing the highest level of risk at each institution and enhances examiners' ability to diagnose emerging problems.

Implementation of this process will provide greater consistency in examinations conducted by the Federal Reserve, the FDIC, and the states, and is expected to result in examinations that are more efficient and effective and less burdensome on institutions.

Critical to the implementation of the risk-focused approach is the exercise of examiner judgment in determining the scope of the examination during the planning process. This allows examiners to customize, based on the bank's risk profile, procedures performed on-site.

The Federal Reserve and the FDIC have developed examination procedure modules to assist examiners in their analysis of seven of the most important activities of community banks including loan portfolio management, securities, management and internal controls, earnings, and capital.

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Six supplemental modules are provided for the review of activities such as electronic banking, mortgage banking, and international banking. Both agencies have conducted extensive field testing of the modules.

These modules emphasize evaluation of a bank's ability to manage the risks associated with a particular activity so that examiners can better diagnose emerging problems. The modules employ a tiered structure that permits an examiner to draw conclusions after completing a core analysis requiring a limited number of procedures. An expanded analysis involving further procedures would be performed only if the core analysis indicated more in-depth review is necessary.

The modules have been automated for use on virtually all laptop computers currently in field use through a stand-alone software program called "ELVIS" (Examiner Laptop Visual Information System).

ELVIS provides a documentation vehicle for work performed on an examination, as well as electronic access to the two agencies' examination manuals. Examiners at both agencies have been trained on the risk-focused examination process and the use of ELVIS.

The FDIC began work on developing a risk-focused examination process in 1996 as part of a Corporate Operating Plan project. When the FDIC examiners working on the project learned that the Federal Reserve had undertaken a similar effort, the two agencies

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decided to join in a cooperative effort. The state banking departments through the Conference of State Bank Supervisors (CSBS) provided input to the development work.

Training on the risk-based examination process has included examiners from all of the 50 state banking departments. Since all three groups conduct examinations of state-chartered banks, implementation of the risk-focused approach is expected to improve the consistency of examination procedures applied to state-chartered institutions.