

**FEDERAL RESERVE BANK
OF NEW YORK**

[Circular No. 10762]
[January 11, 1995]

**PROCEDURES FOR APPEALING AN ADVERSE
MATERIAL SUPERVISORY DETERMINATION**

Comments Invited by February 6, 1995

*To All Member Banks, Bank Holding Companies, and Branches and Agencies
of Foreign Banks in the Second Federal Reserve District, and Others Concerned:*

Following is the text of a statement issued by the Board of Governors of the Federal Reserve System:

The Federal Reserve Board has requested public comment on an internal appeals process for institutions wishing to appeal an adverse material supervisory determination.

Comment is requested by February 6, 1995.

The Riegle Community Development and Regulatory Improvement Act of 1994 requires the Board (as well as other Federal banking agencies) to establish an independent, intra-agency appellate process, which will be available to review material supervisory determinations made at insured depository institutions, such as an adverse examination report.

Printed on the following pages is the text of the Board's official notice and request for comments in this matter. Comments should be submitted by February 6, 1995, and may be sent to the Board, as indicated in the notice, or to our Domestic Banking Department. Questions regarding this matter may be directed, at this Bank, to Dean Ungar, Senior Examiner, Domestic Banking Department (Tel. No. 212-720-2198).

WILLIAM J. McDONOUGH,
President.

FEDERAL RESERVE SYSTEM

[Docket No. R-0867]

Internal Appeals Process

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Notice and request for comments.

SUMMARY: The Board is seeking public comment on an internal appeals process for institutions wishing to appeal an adverse material supervisory determination.

DATES: Comments must be received by February 6, 1995.

ADDRESSES: Comments should refer to Docket No. R-0867, and may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. Comments also may be delivered to room B-2222 of the Eccles Building between 8:45 a.m. and 5:15 p.m. weekdays, or to the guard station in the Eccles Building courtyard on 20th Street, N.W. (between Constitution Avenue and C Street) at any time. Comments may be inspected in room MP-500 between 9:00 a.m. and 5:00 p.m. weekdays, except as provided in 12 CFR 261.8 of the Board's rules regarding availability of information.

FOR FURTHER INFORMATION CONTACT: Gregory A. Baer, Managing Senior Counsel, Legal Division (202/452-3236); Shawn McNulty, Assistant Director, Division of Consumer and Community Affairs (202/452-3946); or Ann Marie Kohlligian, Senior Counsel/Manager, Division of Banking Supervision and Regulation (202/452-3528), Board of Governors of the Federal Reserve System. For the hearing impaired only, Telecommunication Device for the Deaf (TDD), Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION:**Background**

Section 309 of the Riegle Community Development and Regulatory Improvement Act of 1994 (the Act), 12 U.S.C. 4806, requires the Board (as well as the other Federal banking agencies) to establish an independent, intra-agency appellate process. This process shall be available to review material supervisory determinations made at insured depository institutions. Section 309 specifies various requirements that the appellate process must meet.

The Federal Reserve conducts its supervision of state member banks, bank holding companies, and branches and agencies of foreign banks through twelve regional Reserve Banks. The Federal Reserve Banks already administer appellate processes that the Board believes have worked well over the years and are generally consistent with section 309. The legislative history of the Act notes that "[s]ome of the Federal banking agencies have in place procedures to settle disputes between the agency and a financial institution that may satisfy the requirements of this provision." H.R. 103-652, 103d Cong., 2d Sess. § 309 (1994). The Board is proposing guidelines for appeals that are consistent with current practice at the Reserve Banks and the specific requirements of section 309.

The Board wishes to stress that the codification of an appeals process is not intended to affect the Federal Reserve System's longstanding practice of affording bank management and directors opportunities to express their views and concerns throughout the examination process. Bank management is encouraged to discuss examination findings and loan classifications during on-site examinations. Management may also express any concerns to senior supervisory staff at the Reserve Bank if a matter has not been resolved by the

examiner-in-charge. At the completion of all examinations, supervisory staff or officials meet with management to discuss the examination results and, in some instances, Federal Reserve officials will meet with an institution's board of directors to discuss examination findings.

The Board continues to believe that an institution is best served by raising questions or objections concerning an examination through these informal processes. Doing so permits issues to be discussed and resolved as soon as they arise, rather than after the close of an examination and the filing of an appeal.

Procedures

Section 309 requires the Board (1) to provide for appeals to be heard and decided expeditiously, (2) to protect appellants from retaliation by examiners, and (3) to guarantee that the appeal is heard by a disinterested person. The Board's proposed guidelines incorporate these statutory standards by requiring that each appeal be decided within 30 days by a disinterested person to be selected by the Reserve Bank, with a further right of appeal to the President of the Reserve Bank, also to be decided within 30 days.

The proposed guidelines also require that the reviewer be qualified to undertake the review. Generally, this means being trained in the area under review. For example, reviews should be conducted by qualified Reserve Bank officials in either the supervisory or consumer affairs area, as appropriate. The Board believes that the structure of the supervision and consumer functions at the Reserve Bank should allow for review by a trained but impartial person. In the unlikely event that all qualified personnel did participate in the contested examination, then staff from the Board or another Reserve Bank could be enlisted for this purpose.

Any supervised organization dissatisfied with the results of an appeal to a Reserve Bank President may appeal the Reserve Bank's decision to the Board of Governors. However, the Board expects that such appeals will occur only in unusual cases where serious or System-wide issues are raised.

Eligibility

The Federal Reserve's existing appeals process extends not only to state member banks but also to bank holding companies and their nonbank subsidiaries, branches and agencies of foreign banks, Edge and agreement corporations, and other entities examined or inspected by the Federal Reserve. Although section 309 requires an appellate process only for insured depository institutions, the Board is proposing to continue to extend the same opportunity of appeal to all entities examined or inspected by the Federal Reserve.

Material supervisory determination

Section 309 allows appeal of any "material supervisory determination." The statute does not define the term precisely, but instead states that it "includes" determinations relating to composite examination ratings, the adequacy of loan loss reserves, and significant loan classifications. The Act specifically notes that the term does not include a determination to appoint a conservator or receiver for an insured depository institution or a decision to take prompt corrective action pursuant to section 38 of the Federal Deposit Insurance Act. Existing procedures allow institutions to challenge these determinations.

As recognized by the Act, the Federal Reserve (like the other Federal banking agencies) already provides administrative rights of appeal for various supervisory actions. These include, in addition to the two identified by the statute, the issuance of capital directives; the issuance of administrative enforcement actions, including the imposition of cease and desist, removal and

prohibition, suspension and civil money penalty orders; and actions to terminate membership in the Federal Reserve System. Since these actions already involve administrative procedures far more extensive than those contemplated by section 309, the Federal Reserve is proposing to exclude these actions from the proposed appeals process established under section 309. The Federal Reserve believes that these enforcement or quasi-enforcement actions either are not "material supervisory determinations" for purposes of section 309 or, if they are, that existing procedures satisfy the Act's requirement of an appellate process. Allowing parallel rights of appeal would be confusing, duplicative, and wasteful.

Guidelines for Appeals of Material Supervisory Determinations

Section 309 of the Riegle Community Development and Regulatory Improvement Act of 1994 (the Act), 12 U.S.C. 4806, requires the Board and the other Federal banking agencies to establish an independent, intra-agency process to review appeals of material supervisory determinations.

The purpose of these guidelines is to allow each Reserve Bank to administer its own appellate process, but to establish the procedures under which each Bank's appellate process must operate. Doing so will ensure that each Reserve Bank's process is consistent with section 309 and that institutions will be granted the same appellate rights regardless of the Federal Reserve district in which they reside.

Procedures for Appealing a Material Supervisory Determination.

Any appeal of a material supervisory determination pursuant to section 309 shall be filed and considered pursuant to the following procedures.

(1) Any appeal shall be approved by the board of directors of the institution and filed in writing with the Secretary of the Federal Reserve Bank or other appropriate official within 30 calendar days of the material supervisory

determination, unless the time for filing is extended by the Reserve Bank. The Reserve Bank shall promptly provide a copy of the appeal to the appropriate division director of the staff of the Board of Governors.

(2) The appeal shall be considered in the first instance by a person or persons selected by the Reserve Bank (the review panel) who --

(A) did not participate in the material supervisory determination;

(B) do not directly or indirectly report to the person who made the material supervisory determination under review; and

(C) are qualified to review the material supervisory determination.

(3) The appellant institution may appear before the review panel in order to present testimony and, with the consent of the review panel, witnesses. The review panel shall also solicit the views of the Reserve Bank staff involved in the determination under appeal, Board staff, and, when appropriate, the staff of other supervisory agencies (for example, in the case of joint examinations or inspections).

(4) Any appeal shall be decided by the review panel within 30 calendar days of filing, unless the appellant and the review panel jointly agree to extend the time for decision.

(5) Any appellant institution dissatisfied with the decision of the review panel may, with the consent of its board of directors, appeal that decision to the Reserve Bank President by filing a written appeal with the Secretary of the Reserve Bank or other appropriate official. Such an appeal shall be decided within 30 calendar days of filing.

(6) Any appellant dissatisfied with the final decision of the Reserve Bank may, with the consent of its board of directors, appeal that decision to the director of the appropriate division of the Board of Governors, who in consultation with the

appropriate oversight Governor, may review an adverse determination by the Reserve Bank.

Safeguards Against Retaliation. Each Reserve Bank shall establish appropriate safeguards to protect appellants from retaliation. The Board's ombudsman will periodically contact institutions after their appeals have been decided in order to make certain that no retaliation has occurred.

Availability of Procedures. Each Reserve Bank shall make these guidelines and the Reserve Bank's process for selecting a review panel available to each institution in its district, any institution appealing a material supervisory determination, and any member of the public who requests them.

Eligible Institutions. Any institution about which the Federal Reserve makes a material supervisory determination is eligible for the appeals process. This includes state member banks, bank holding companies and their nonbank subsidiaries, branches and agencies of foreign banks, Edge and agreement corporations; and other entities examined or inspected by a Reserve Bank.

Material Supervisory Determination Defined. Whether an appealed action constitutes a "material supervisory determination" eligible for the appeals process shall be decided by the person or persons hearing the appeal, and a determination that the action is not appealable under these guidelines may be further appealed to the Reserve Bank President and Board staff in the same manner as any other adverse decision.

The term "material supervisory determination" includes, but is not limited to, material determinations relating to examination or inspection composite ratings, the adequacy of loan loss reserves, and significant loan classifications. The term does not include any material supervisory determination for which an independent right of appeal exists. Such actions include prompt corrective

action directives issued pursuant to section 38 of the Federal Deposit Insurance Act (FDI Act), contested actions to impose administrative enforcement actions under the FDI Act and Bank Holding Company Act of 1956 (the BHC Act), capital directives, and orders issued pursuant to applications under the BHC Act. Savings Provision. Section 309 expressly provides that it shall not affect the authority of the Board or any other agency to take enforcement or supervisory action against an institution. In such cases, the rights of appeal provided for in the statutes and regulations concerning these actions shall govern. The appeal of a material supervisory determination does not prevent the Federal Reserve from taking any supervisory or enforcement action -- formal or informal -- it deems appropriate to discharge the Federal Reserve System's supervisory responsibilities.

By order of the Board of Governors of the Federal Reserve System,
December 22, 1994.

(signed) William W. Wiles

William W. Wiles,
Secretary of the Board.