

FEDERAL RESERVE BANK OF NEW YORK

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CHESTER B. FELDBERG
EXECUTIVE VICE PRESIDENT

AT-10898
December 4, 1996

To All State Member Banks and Trust Companies, Bank Holding Companies, Branches and Agencies of Foreign Banks, Edge and Agreement Corporations, and Others Concerned, in the Second Federal Reserve District:

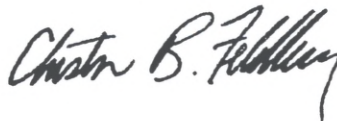
Subject: Disclosure of Individual Components of Supervisory Rating Systems to Management and Boards of Directors

Beginning January 1, 1997, Federal Reserve examination and inspection reports will include the numeric and alphabetic **component** ratings that we assign under the various supervisory rating systems that we use. This will be a change more of form than of substance, as it has been for some time our general practice to ensure, in effect, that all supervisory conclusions covering each area of focus are clearly communicated, following each examination or inspection, to senior management and boards of directors. However, we have tended to employ verbal descriptions rather than the ratings *per se*. The intended disclosure practices are detailed in the enclosed copy of a Federal Reserve Board staff letter dated November 15, 1996.

This more explicit disclosure of component ratings to institutions examined by the Federal Reserve, as well as by other bank supervisory authorities, is being undertaken in response to the growing number of recent statutory and regulatory initiatives -- such as the federal Economic Growth and Regulatory Paperwork Reduction Act and the FFIEC-proposed CAMELS rating system -- that create certain specific links between an examined institution's component ratings and the supervisory or regulatory treatment that it can expect to receive.

Questions concerning the disclosure of component ratings may be directed at this Bank to any member of your relationship management team in our Bank Supervision Group.

Sincerely,



Enclosure



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D. C. 20551

DIVISION OF BANKING
SUPERVISION AND REGULATION

SR 96-26 (SUP)

November 15, 1996

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

SUBJECT: Provision of Individual Components of Supervisory Rating Systems to Management and Boards of Directors

It is a longstanding policy of the Federal Reserve to discuss fully and clearly in examination and inspection reports, and in meetings with senior management and boards of directors, supervisory issues, problems, or concerns relating to the institutions under the System's supervision. It has also generally been Federal Reserve practice for some time to provide to senior management and directors the single word descriptions corresponding to the numeric component ratings assigned under the Uniform Financial Institutions Rating System (CAMEL). In an effort to further strengthen communication with supervised institutions, beginning January 1, 1997, the Federal Reserve will provide the numeric and alphabetic component ratings assigned under various supervisory rating systems to senior management and directors. Building upon existing practice, this step is intended to better focus management attention on possible areas of weakness and the need for timely corrective actions. This step is also consistent with a recent recommendation from the FFIEC regarding disclosure of the numeric component ratings assigned under CAMEL.

Each Reserve Bank should direct its examiners to begin disclosing component ratings as soon as possible, but no later than January 1, 1997, in summary sections of examination/inspection reports and directors' summaries, as necessary, and in meetings with senior management and directors. This directive applies to the following rating systems:

- CAMEL (state member banks);
- BOPEC (bank holding companies);
- CAMEO (Edge and agreement corporations and overseas subsidiaries of U.S. banks);
- ROCA (U.S. branches and agencies of foreign banking organizations);
- the Uniform Interagency Trust Rating System; and
- the Uniform Interagency Rating System for Data Processing Operations

It also applies to the alphabetic component ratings assigned to management under the BOPEC rating system and to the alphabetic components assigned under the Transfer Agent rating system. General guidance on the disclosure of composite and component ratings in examination and inspection reports is attached to this SR letter.

In the context of the exit meeting, the examiner should discuss key overall examination findings, including composite and component numeric ratings. Consistent with current practice, ratings are subject to a review by Reserve Bank supervisory officials, and final ratings should be included in the examination or inspection report. In disclosing composite and component ratings, the examiner-in-charge should remind management that the ratings assigned are a part of the findings of the examination or inspection and are privileged and confidential under applicable law. If composite and component ratings are changed between examinations and inspections as a result of off-site analysis, management and directors should be informed of the change.

Reserve Banks should inform state banking authorities in their districts of the decision to disclose component ratings and should explain the reasons for this change in Federal Reserve procedures prior to beginning disclosure of component ratings. Component ratings assigned under AEP arrangements by state agencies should be treated by the Reserve Banks in a manner that is consistent with the state's policy regarding disclosure.

The guidance included in this SR letter is to be applied going forward, consistent with the approach taken by the other banking agencies. In general, component ratings assigned in the past should be treated in accordance with the policy prevailing at the time.

A copy of this letter should be provided to each institution supervised by the Federal Reserve. If there are any questions relating to the disclosure of component ratings, please contact Connie Powell, Supervisory Financial Analyst, at (202-452-3506), or Kevin Bertsch, Supervisory Financial Analyst, at (202-452-5265).



Richard Spillenkothen
Director

Attachment

Cross references:

SR 88-37, "Disclosure of Numeric Composite Examination and Inspection Ratings to Examined/Inspected Institutions"

SR 90-21, "Rating System for International Exams"

SR 91-21, "EDP Interagency Examination, Scheduling and Distribution Policy"

SR 95-22, "Enhanced Framework for Supervising the U.S. Operations of Foreign Banking Organizations"

SR 95-51, "Rating the Adequacy of Risk Management Processes and Internal Controls at State Member Banks and Bank Holding Companies"

SR 96-10, "Risk-focused Fiduciary Examinations"

Guidance on Disclosure of Composite and Component Ratings in Examination and Inspection Reports

Page one of the report should list the composite rating for the current examination or inspection and for the two previous examinations or inspections at the top of the page as outlined below for bank examinations.

Uniform Financial Institutions Rating System

	<u>Cur. Exam</u>	<u>Prior Exam</u>	<u>Prior Exam</u>
Exam Date:	09-03-9X	10-19-9Y	10-22-9Z
Composite Rating:	2	2	2
Component Ratings:			
Capital	2	n/a	n/a
Asset Quality	2	n/a	n/a
Management	2	n/a	n/a
Earnings	2	n/a	n/a
Liquidity	2	n/a	n/a

This listing should be followed by the uniform definition of the assigned composite rating. The uniform definitions of the component ratings assigned need not be included in reports; however, they should be made available to management and directors upon request.

When combined examination/inspection report formats are used, similar matrices for each composite and component rating assigned should be included in the report.

Numeric and alphabetic component ratings should also be included on the pages of reports that discuss findings related to the components. For example, for bank examination reports, the numeric component rating assigned to capital should appear on the capital page of the report.

In the case of examinations of independent data processing servicers and financial institutions that provide servicing to other insured financial institutions, examination reports are sometimes provided not only to the examined data processing servicers but also to the institutions that receive servicing from these servicers. Accordingly, in these cases, the composite and component ratings assigned under the Uniform Interagency Rating System for Data Processing Operations should be provided to senior management and directors in the transmittal letter accompanying the examination report rather than in the open section of the examination report.¹

¹ Additional guidance on the disclosure of composite and component ratings for examinations of information systems will be issued by the FFIEC in the near future.