



Federal Deposit Insurance Corporation

550 17th Street NW, Washington, D.C. 20429-9990

Financial Institution Letter

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SUPERVISORY INSIGHTS JOURNAL

Summer 2005 Issue Now Available

Summary: The FDIC has announced the release of the Summer 2005 issue of ***Supervisory Insights***, a professional journal that promotes the practice of bank supervision. ***Supervisory Insights*** is available on the FDIC's Web site at www.fdic.gov.

Distribution:

FDIC-Supervised Banks

Suggested Routing:

Chief Executive Officer

Related Topics:

Interest rate risk
Enforcement actions
Credit scoring systems
Indirect automobile lending
Technology service providers
Other-than-temporary impairment of investment Securities

Attachment:

None

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Note:

FDIC financial institution letters (FILs) may be accessed from the FDIC's Web site at www.fdic.gov/news/news/financial/2005/index.html.

To receive FILs electronically, please visit <http://www.fdic.gov/about/subscriptions/fil.html>.

Paper copies of FDIC financial institution letters may be obtained through the FDIC's Public Information Center, 801 17th Street, NW, Room 100, Washington, DC 20434 (1-877-275-3342 or 202-416-6940).

Highlights:

- "A Changing Rate Environment Challenges Bank Interest Rate Risk Management" notes that aggregate industry trends – higher levels of exposure to long-term assets, concentrations in mortgage-related assets, and a greater reliance on non-core funding sources that exhibit optionality – raise concern during a period of rising rates about the potential for increasing levels of interest rate risk (IRR). The article emphasizes the importance of joining off-site analysis of bank balance sheet data with on-site examination of how well an institution manages IRR.
- "Fair Lending Implications of Credit Scoring Systems" recommends a framework for examiners to follow in a fair lending examination when a credit score is one of the criteria a bank considers when making credit decisions.
- "The Changing Landscape of Indirect Automobile Lending" describes the effects of increasing competition in automobile financing on underwriting practices and looks at how lax underwriting and internal controls are prompting closer regulatory scrutiny of portfolio performance.
- Other articles review the FDIC's enforcement action process as it relates to individuals, recommend tools examiners can use to strengthen their review of technology services providers, and describe accounting guidance for recognizing other-than-temporary impairments of investment securities.

SUPERVISORY INSIGHTS JOURNAL
Summer 2005 Issue Now Available

The Federal Deposit Insurance Corporation (FDIC) has announced the release of its Summer 2005 issue of *Supervisory Insights*, a professional journal that promotes the practice of bank supervision. Articles featured in this issue describe a number of areas of current supervisory focus at the FDIC. Topics addressed include the potential for increased interest rate risk in a rising rate environment given shifts in bank balance sheet composition, fair lending implications of credit scoring systems, effects of increasing competition in automobile financing on underwriting practices, a review of the enforcement action process as it relates to individuals, a discussion of how the use of publicly available information can strengthen examiner review of technology service providers, and accounting guidance for recognizing other-than-temporary impairments of investment securities.

The lead article in this issue discusses how rising interest rates and a flattening yield curve could pressure net interest margins, particularly for liability-sensitive banks with increased exposure to long-term assets. The article “A Changing Rate Environment Challenges Bank Interest Rate Risk Management” notes that aggregate industry trends – specifically higher levels of exposure to long-term assets, concentrations in mortgage-related assets, and a greater reliance on non-core funding sources that exhibit optionality – raise concern during a period of rising rates about the potential for heightened levels of interest rate risk. It is difficult to draw conclusions about the level of interest rate risk based solely on off-site information. Therefore, the article emphasizes off-site and industry-wide analysis must be joined with on-site examination findings to assess accurately a bank’s interest rate risk exposure and the effectiveness of its risk management processes. The results of on-site examinations identify certain areas where banks can improve risk measurement and management processes. Overall, however, few banks are exhibiting material concerns related to sensitivity to interest rate risk.

The FDIC believes the articles appearing in the current issue will provide valuable and useful information to insured financial institution management and staff. *Supervisory Insights* is available on the FDIC’s Web site at www.fdic.gov.

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