### Core Analysis Decision Factors

Examiners should evaluate the Core Analysis in this section to determine whether an Expanded Analysis is necessary. This module is intended to incorporate and summarize the findings from all of the completed ED Modules for a given examination. Click on the hyperlinks found within each of the Core Analysis Decision Factors to reference the applicable Core Analysis Procedures.

Do Core Analysis and Decision Factors indicate that risks are appropriately identified, measured, monitored, and controlled?

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>C.1.</td>
<td>Does the board adequately supervise the affairs of the bank and provide for management depth and succession? Refer to Core Analysis Procedures #1-19, Procedure #22, Procedures #27-29, Procedure #43.</td>
</tr>
<tr>
<td>C.2.</td>
<td>Has management established an adequate control environment throughout the organization? Refer to Core Analysis Procedures #23-25, Procedure #29, Procedures #40-42, Procedures #44-47.</td>
</tr>
<tr>
<td>C.3.</td>
<td>Is management responsive to recommendations from auditors and supervisory authorities? Refer to Core Analysis Procedure #26.</td>
</tr>
<tr>
<td>C.5.</td>
<td>Are management capabilities sufficient for the size, activities, and condition of the bank? Refer to Core Analysis Procedures #20-21.</td>
</tr>
<tr>
<td>C.6.</td>
<td>Does management identify and assess the major risks confronting the bank? Refer to Core Analysis Procedures #33-42.</td>
</tr>
<tr>
<td>C.7.</td>
<td>Are policies and procedures generally adequate given the size and complexity of the bank? Refer to Core Analysis Procedure #24 &amp; Procedure #27-28.</td>
</tr>
<tr>
<td>C.8.</td>
<td>Do management information systems provide effective internal communication of the bank’s risks? Refer to Core Analysis Procedures #48-49.</td>
</tr>
<tr>
<td>C.9.</td>
<td>Are appropriate governance systems in place to monitor the activities of the bank? Refer to Core Analysis Procedure #32 &amp; Procedure #50.</td>
</tr>
</tbody>
</table>
Examiners are to consider the following procedures but are not expected to perform every procedure at every bank. Examiners should complete only the procedures relevant for the bank’s activities, business model, risk profile, and complexity. If needed, based on other identified risks, examiners can complete additional procedures. References to laws, regulations, supervisory guidance, and other resources are not all-inclusive.

### Preliminary Review

1. Review board, committee, and shareholder meeting minutes since the last examination and the most recent and year-end board packages to assess the extent and adequacy of board supervision. Document important details and consider the following items:
   - Director attendance;
   - Changes in control since the prior examination;
   - Board independence from executive management;
   - Dominant control by a board member, shareholder, or executive management;
   - Significant changes in the direction or activities of the bank;
   - Adequacy of management information systems;
   - Implementation and maintenance of adequate policies; and
   - The bank’s strategic plan.

2. Review changes in management or the directorate since the last examination. Assess compliance with rules concerning notification of changes in executive management. (FRB: Section 914 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. FDIC: Section 32 of the Federal Deposit Insurance Act (FDI Act).)
   - Consider why changes were made or are planned.
   - Assess the effect of any changes on bank operations or risk profile.
   - Review biographical information for new executive officers and directors.

3. Review prior examination reports, workpapers, and correspondence for comments regarding board supervision, management, and internal controls.

### Board and Management Supervision

4. Review the bank’s charter, by-laws, and other related documents to understand the governance framework for the board of directors. Consider the following:
   - The number of directors;
   - Qualifications or restrictions for directors, including the chairman of the board;
Mandatory retirement age, if any, for board members;
Advisory Directors or Advisory Board
Directorate nomination and election process;
Required committee structure; and
Required frequency of board and committee meetings.

5. Assess the composition of the organization’s board of directors. Consider the following:
   • The number of independent directors,
   • Involvement of the chairman in day-to-day operations,
   • The number of years each member has served on the board, and
   • The presence of any financial and other experts on the board.

6. Determine whether the board has an effective process to identify, nominate, and select qualified individuals. (Note: Effective processes generally include recruiting board members whose relevant business, industry, or financial expertise corresponds with the institution’s risk profile and strategic plans.)

7. Determine whether the organization provides new board members with an overview of their fiduciary responsibilities and opportunities for ongoing training.

8. Determine whether the board has adopted a code of ethics that applies to all board members, officers, and employees, and assess adherence to that code.

9. Determine whether the board adopted and management has implemented a strategic plan for the organization’s operation over the next three to five years.

10. Determine whether the board is actively involved in the selection and retention of the chief executive officer (CEO) and other executive officers, and consider whether the board regularly assesses executive officers’ performance.

11. Determine whether the board and management have talent development and succession plans for all key personnel and periodically reviews and updates such plans. (Note: Succession plans may be formal...
12. Determine whether the board, either directly or through a compensation committee:
   - Approves the compensation of senior executives;
   - Ensures that incentive compensation arrangements for covered employees are appropriately balanced and do not jeopardize the safety and soundness of the institution; and
   - Established a process for re-evaluating compensation in the event that employee decisions lead to adverse financial outcomes.

13. Determine the extent and appropriateness of board and management reliance on external advisors or consultants.

14. Assess the appropriateness and effectiveness of board and management committee structures. Consider the following:
   - Charters delineating a committee’s size, responsibilities, and membership qualifications;
   - Selection process for committee members;
   - Rotation requirements;
   - Selection of committee chair;
   - Meeting frequency and attendance;
   - Meeting agendas and minutes;
   - Quality and timing of information flows from committees to the full board; and
   - Need for additional committees.

15. Determine whether committee charters adequately address financial and non-financial risk governance. Consider if charter elements:
   - Define the responsibilities for oversight of risk management policies and practices;
   - Outline board responsibilities to sanction, review, and amend committee practices;
   - Articulate the board’s role and responsibility in establishing and reviewing risk levels;
   - Identify metrics for assessing and reporting risk levels relative to defined risk thresholds and limits; and
   - Provide for ongoing dialogue between board and management regarding risk management practices.

16. Assess the process for setting board and committee meeting agendas, and evaluate the appropriateness,
<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Core Analysis</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>accuracy, completeness, and timing of information received prior to meetings.</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>17. Determine whether the board established and communicated a whistleblower process that allows employees, vendors, and customers to anonymously report their concerns.</strong> (FDIC: consider FIL 80-2005, <em>Guidance on Implementing a Fraud Hotline.</em>)</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>18. Determine whether the board of directors, its committees, and executive management periodically conduct self-assessments of their performance.</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>19. Evaluate the reasonableness and appropriateness of compensation paid to the directorate. Consider the following:</strong></td>
<td></td>
</tr>
<tr>
<td>- Compensation or fees paid on a per meeting attended, annual, or other basis;</td>
<td></td>
</tr>
<tr>
<td>- Additional compensation for committee meetings;</td>
<td></td>
</tr>
<tr>
<td>- Compensation basis (cash, stock, stock option, or other basis);</td>
<td></td>
</tr>
<tr>
<td>- Deferred or other benefits; and</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>20. Determine whether key executives have the appropriate knowledge, skills, and experience relative to the nature and scope of their responsibilities.</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>21. Identify and assess the influence exerted by any dominant official or policymaker.</strong></td>
<td></td>
</tr>
<tr>
<td><em>Note:</em> The presence of a dominant official should not be viewed negatively or as a supervisory concern in and of itself. Rather, the presence of a dominant official coupled with other risk factors such as ineffective internal controls, lack of board independence or oversight, or engaging in risky business strategies may create regulatory concerns or require enhanced supervision.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>22. Determine whether the organizational structure is appropriate given:</strong></td>
<td></td>
</tr>
<tr>
<td>- The size, complexity, and overall risk profile of the bank; and</td>
<td></td>
</tr>
<tr>
<td>- The organization’s strategic plan.</td>
<td></td>
</tr>
</tbody>
</table>
23. Determine whether the board implemented an effective internal control system and ensures all personnel understand the importance of internal controls. Control systems should be designed to provide reasonable assurance that internal controls will prevent or detect:
   - Materially inaccurate, incomplete, or unauthorized transactions;
   - Deficiencies in the safeguarding of assets;
   - Unreliable financial or regulatory reporting; and
   - Deviations from laws, regulations, and internal policies.

24. Determine whether the bank has a policy that requires all officers and employees to be absent from their duties for an uninterrupted period of not less than two consecutive weeks. Assess its adequacy.
   *Note: Absence may involve vacations, rotations of duty, or a combination of both activities. Such policies are highly effective in preventing embezzlements, which usually require a perpetrator’s ongoing presence to manipulate records, respond to inquiries, and otherwise prevent detection. The benefits of such policies are substantially, if not totally, eroded if the duties normally performed by an individual are not assumed by someone else.*

25. Determine whether management addresses integrity in its code of conduct, ethics policy, and actions. (FDIC: refer to FIL 105-2005, *Corporate Codes of Conduct: Guidance on Implementing an Effective Ethics Program*, and Statement of Policy: *Guidelines for Compliance with Federal Bank Bribery Law*). Consider the following:
   - Internal guidelines regarding conflicts of interest, periodic training, and acceptable/unacceptable practices;
   - Remedial action concerning policy exceptions; and
   - Documentation concerning deviations from policy and associated remedial action.

26. Determine whether management takes appropriate and timely action to address recommendations by auditors and regulatory authorities. *(Refer to the Internal and External Audit Evaluation module.)*

27. Determine whether the board, through effective monitoring and enforcement, restricts management’s ability to override established policies and procedures.

28. Determine whether the organization has written policies governing compensation programs. Policies should address base pay and/or performance-based compensation arrangements. Areas of consideration include:

- Evaluate the appropriateness of incentive compensation arrangements for executive management and other employees (individually or as a group) that initiate material risk positions for the bank. When reviewing incentive compensation arrangements, consider:
  - The type, level, and significance of incentive compensation as part of the overall compensation model and its influence on the institution’s risk profile;
  - Board approval of executive compensation incentives;
  - The use of golden parachute agreements (FRB: SR-96-21; FDIC: FIL-8-96, FIL-66-2010, and Part 359); and
  - Any incentive compensation issues identified during compliance examinations (e.g., mortgage loan origination compensation).

- Determine whether any compensation arrangements could be considered unsafe and unsound. When assessing compensation arrangements, review the combined value of all cash and noncash benefits provided to the individual and consider the following:
  - The compensation history of the individual and others with comparable expertise and responsibilities;
  - The financial condition of the institution;
  - Documentation of the board’s review of compensation practices at comparable institutions (Note: Such reviews typically consider factors such as asset size, geographical location, and complexity of activities);
  - For post-employment benefits, the projected total cost and benefit to the institution;
  - Connection between the individual and any fraudulent act or omission, breach of trust or fiduciary duty, or insider abuse;
  - Bank purchases of life insurance for compensation purposes; and
  - Any other relevant factors.

*Note: Appropriate incentive compensation arrangements generally balance risks and rewards; reflect effective controls and risk management practices; and are supported by strong corporate governance. Examiners should refer to the Interagency Guidance on Sound Incentive Compensation Policies, issued June 21, 2010, for further discussion.*

30. Determine whether adequate systems are in place to identify and mitigate self-serving practices or conflicts of interest. Consider compliance with applicable laws, and determine whether:

- Insiders have undue influence over customer activities;
- Insiders are lending personal funds to customers or borrowers;
- Privileges or benefits given to insiders are commensurate with the services rendered;
- Insiders are conducting excessive non-bank related business at the bank or are spending inordinate...
amounts of time away from the bank; and

- Transactions related to insiders’ purchase or use of bank assets (such as other real estate, repossessed vehicles, equipment, or bank facilities) are appropriate.

### 31. Determine whether the board appropriately monitors and manages potential conflicts of interest between the institution and its directors, management, principal shareholders, and affiliates (collectively, affiliated parties). The board should ensure the institution has policies and standards designed to ensure that:

- All transactions between the institution and an affiliated party are sound, in the best interest of the institution, and appropriately documented; and
- Any exceptions to established policies and standards governing transactions with affiliated parties are legally permissible and appropriately approved and documented.

### 32. Determine whether (and if so, why) the external auditor or legal counsel changed since the last examination.

### Risk Assessment

#### 33. Review the adequacy of internal risk assessments for all significant business activities. Determine whether the assessments identify all material risks and consider the adequacy of compensating controls. Consider whether the results of assessments are appropriately reported and that internal controls and risk-assessment methodologies are updated as needed to reflect changes in business activities and work processes.

#### 34. Determine whether management’s risk-taking practices are conservative, moderate, or aggressive by assessing practices relating to loans; investments; asset/liability management; growth; nontraditional banking services; deposit structures, rates, and products; and other pertinent areas.

- Determine whether internal controls sufficiently mitigate higher-risk activities.
- Determine whether there are any material changes in management’s risk-taking practices. For example, changes in deposit products or funding sources; loan products, underwriting, or portfolio mix; security investments, due diligence, or maturity distributions; or asset growth.

#### 35. Assess the effectiveness of the board and management’s planning processes. Consider the following:

- Strategic plans, budget processes, profit plans, and growth projections;
- Experience of individuals involved with the planning process;
- Reasonableness of assumptions;
36. Determine whether management adequately considers risks that influence the success or failure of established objectives. Generally, risk assessments should address:

- External sources of risk, such as:
  - Technology changes,
  - Cyber-security risks,
  - Competition,
  - Economic conditions,
  - Legislative and regulatory environment, and
  - Accounting pronouncements.

- Internal sources of risk, such as:
  - Retention of key management and staff,
  - Availability of funds,
  - Information systems and related conversions,
  - Adequacy of capital funds,
  - Corporate restructuring,
  - Concentrations of credit and funding sources,
  - Rapid growth, and
  - New products or business lines.

- The significance and likely impact of identified risks, compensating controls, and any mitigating factors.

37. Determine whether management monitors reputational risk arising from sources such as:

- Media, internet, and social networks;
- Press releases and annual reports;
- Participation in or sponsorship of community events; and
- Public perception.

38. Consider whether the bank has an appropriate marketing and public relations strategy to manage its reputational risk.
39. Consider whether risks identified by examiners and external auditors often differ from those identified by management.

**Control Activities**

40. Assess the appropriateness of blanket bond insurance levels. Consider:
   - Financial condition of bank, including capital levels and asset quality;
   - Asset/deposit size and trends;
   - Size of transactions, such as loans (in relation to legal lending limit) and wire transfers;
   - Single-loss and aggregate liability levels;
   - Effectiveness of internal controls;
   - Whether areas of operations are rapidly expanding;
   - Amount of cash, securities, and negotiable items normally held;
   - Number, experience, and turn-over rate of personnel;
   - Extent of trust and merchant-credit-card activities;
   - Data processing activities and internet presence;
   - Presence of a dominant official or policymaker; and
   - Previous fraudulent activities or claims and suspicious activity reports.

41. Consider the adequacy of other insurance policies including Director and Officer and any excess employee fidelity policy.

42. Determine the reasons for any significant fidelity insurance claims.

43. Determine whether employment practices for prospective directors, officers, employees, and significant third-party contractors address potential employment impediments. For example, criminal convictions subject to Section 19 of the FDI Act (crimes related to dishonesty, fraud, and money laundering) and banking prohibition orders. *(Note: all FDIC-insured depositories are subject to Section 19 of the FDI Act.)*

44. Determine whether policies, procedures, and practices are adequate for the size, complexity, and risk profile of the bank by reviewing findings from other modules completed during the examination.
45. Determine whether existing controls help ensure adherence to established internal policies and appear reasonable in relation to risk exposures. Review the results of other reviews completed during the examination to determine the overall adequacy of internal controls.

<table>
<thead>
<tr>
<th>46. Determine whether management maintains an effective system of controls and safeguards for activities that expose the bank to risk. Consider the following:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Authorization and reporting requirements;</td>
</tr>
<tr>
<td>• Data access controls; and</td>
</tr>
<tr>
<td>• Joint custody, dual control, and separation-of-duty arrangements.</td>
</tr>
</tbody>
</table>

| 47. Determine whether management takes appropriate steps to comply with laws and regulations. |

### Information and Communication

<table>
<thead>
<tr>
<th>48. Determine the adequacy of information systems to identify, capture, and report relevant internal and external information.</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Determine whether the systems are commensurate with risks.</td>
</tr>
<tr>
<td>• Determine whether the board or management periodically evaluates the adequacy and accuracy of management information systems.</td>
</tr>
<tr>
<td>• Consider the accuracy of the Consolidated Reports of Condition and Income.</td>
</tr>
</tbody>
</table>

| 49. Evaluate whether communication of information is sufficient for personnel to carry out their responsibilities. |

### Monitoring

<table>
<thead>
<tr>
<th>50. Determine whether systems are in place to monitor material risks arising from all major activities in which the institution is engaged. Assess risk monitoring with respect to the following:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Credit risk,</td>
</tr>
<tr>
<td>• Market risk,</td>
</tr>
<tr>
<td>• Liquidity risk,</td>
</tr>
<tr>
<td>• Operational risk,</td>
</tr>
<tr>
<td>• Legal risk,</td>
</tr>
<tr>
<td>• Reputation, and</td>
</tr>
</tbody>
</table>
Core Analysis

- Compliance risk. (FRB: See SR 16-11)

End of Core Analysis. If needed, Continue to the Expanded and Impact Analyses.