CAPITAL ADEQUACY

Expanded Analysis Decision Factors

This section evaluates the significance of deficiencies or other specific concerns identified in the Core and Expanded Analyses. Click on the hyperlinks found within each of the Expanded Analysis Decision Factors to reference the applicable Expanded Analysis Procedures. If needed, proceed to the accompanying Impact Analysis.

Do Expanded Analysis and Decision Factors indicate that risks are adequately identified, measured, monitored, and controlled?

E.1. Has management taken sufficient action to address capital deficiencies? *Refer to Expanded Analysis Procedures #1-18*.

E.2. Are capital deficiencies immaterial to the bank's condition? *Refer to Expanded Analysis Procedures #1-18*. If capital ratios are below regulatory minimums, proceed to *Impact Analysis*.

CAPITAL ADEQUACY

Expanded Analysis Procedures

Generally, procedures used in the Expanded Analysis should target concerns identified in the Core Analysis and Decision Factors. The flexible procedures specified for the Core Analysis also apply to the Expanded Analysis.

Policies and Procedures

1. Determine why exceptions to internal policies or regulatory capital requirements exist. Consider whether management:

- **Overlooked issues,**
- **Is unfamiliar with or disregarded regulatory requirements, or**
- **Is unfamiliar with or disregarded established internal policies.**

2. Determine whether management commits to and supports the adoption of appropriate controls and monitoring practices that will ensure that internal policy and procedure guidelines will be followed in the future. Determine whether proposed controls, if any, are reasonable.

3. Evaluate management's response to examiner and auditor recommendations.

Internal Controls

4. Review general ledger transactions since the prior examination. Obtain or prepare a detailed capital reconciliation and scrutinize entries for appropriateness.

5. Review procedures regarding stock certificates to assess the following controls:

- **Unissued stock certificates are under dual control, and**
- **Redeemed stock certificates are properly controlled and canceled.**

Audit or Independent Review

6. Research all inadequacies cited in audit or independent reviews to determine the underlying cause(s).

7. Evaluate the materiality of any deficiencies disclosed in the audit or independent reviews.

Information and Communication Systems

8. Research the inaccuracies or inadequacies in reporting systems to determine underlying cause.

9. Evaluate the appropriateness of reports distributed to management and the board.

10. Determine whether any of the inaccuracies cited above compromise management's planning efforts or negatively affect the overall effectiveness of implementing strategic initiatives.

11. Consider the implications of employee stock ownership plans (ESOPs) and associated accounting procedures. Refer to the Consolidated Reports of Condition Instructions. (FDIC: Refer to Advisory Opinions 81-15, 84-22, 90-18, 91-33, and 93-75.)

Earnings Considerations

12. If there is significant uncertainty whether the bank's future performance will be satisfactory, estimate future capital levels under applicable and to-be-phased-in regulatory capital rules using information collected during the examination and discussions with management (such as, additional provision expenses, estimated impairment losses related to goodwill or core deposit intangibles, fees paid to the parent company, and non-recurring items).

13. Determine whether there is undue pressure to pay dividends. Items to consider include:

- **The holding company’s financial condition and contractual obligations,**
- **The financial condition of affiliates,**
- **Stockholder or market pressure, and**
- **Capital distribution and bonus limitations under the capital conservation buffer (effective phase-in starting January 1, 2016).**

Risk Profile Considerations

14. Validate the following calculations if reported compliance with risk-based capital minimums is marginal: • **Risk-weighted assets, and** • **Capital ratios.**
15. If high levels of off-balance sheet activities exist, review supporting documentation and determine whether management properly monitors these exposures. (Note: Monitoring of concentrations should include contingent liabilities.)
16. Assess the adequacy of blanket bond insurance.
17. Review lawsuits (legal opinions or other documentation) that involve the bank or management (focus primarily on cases involving insiders or significant dollar amounts).
18. If capital exposure is significant, assess the board and management's capacity to mitigate or remediate the exposure in the near term (such as raising additional capital, selling assets, restructuring the balance sheet, etc.). Prospective capital raises should conform to the criteria mandated in the capital rules. ***Note: The rules are codified at Title 12 of the Code of Federal Regulations (CFR) for the FRB in Part 217 and codified at Title 12 of the CFR for the FDIC in Part 324.***
End of Expanded Analysis. If needed, Continue to Impact Analysis.

CAPITAL ADEQUACY
Impact Analysis Procedures

Impact Analysis reviews the impact that deficiencies identified in the Core and Expanded Analysis and Decision Factors have on the bank's overall condition, and directs the examiner to consider possible supervisory options.

Impact Analysis Procedures
1. Assess the impact current capital levels may have on the future viability of the bank. • **Assess management's ability to reverse deteriorating trends and augment capital through earnings.** • **Assess the bank's ability to raise capital from existing shareholders, by issuing new capital instruments, or accessing alternative sources of capital.** • **If the capital level and trend raise going-concern issues, estimate time to reach insolvency as well as time to reach the 2 percent of Tangible Equity to Total Assets.**
2. Determine the need for administrative or enforcement actions, formulate specific recommendations, and discuss concerns with appropriate regulatory supervisors.
3. After discussing concerns with appropriate regulatory supervisors, discuss potential regulatory responses with management and the board. Topics of discussion may include: • **Formal or informal enforcement actions or capital directives;** • **The submission of a capital restoration plan (for banks with less than the minimum leverage capital requirement);** • **Written agreements to increase capital to acceptable levels (for banks with less than a 2 percent of Tier 1 Tangible Equity to Total Assets ratio as of January 1, 2015; and** • **Other requirements or restrictions under PCA guidelines (for banks that are undercapitalized, significantly undercapitalized, or critically undercapitalized).**
End of Impact Analysis.