# LOAN PORTFOLIO REVIEW

## 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?**

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| **E.1.** | **Are deficiencies immaterial to the supervision of the lending function? *Refer to Expanded Analysis Procedures #1-20.*** |
| **E.2.** | **Are deficiencies immaterial to the bank's condition? *Refer to Expanded Analysis Procedures #1-20.*** |

# LOAN PORTFOLIO REVIEW
## 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.*

### Identifying, Monitoring, and Reserving for Credit Risk

**LOAN REVIEW**

**1. Evaluate the inadequacies in the loan review process to determine the underlying cause.**

**2. Expand loan sampling in order to gain a better understanding of the credit risk within the loan portfolio.**

**ALLOWANCE FOR LOAN AND LEASE LOSSES (ALLL) (or allowance for credit losses (ACL),[1] when applicable**

***When the overall ALLL (or ACL, when applicable) appears deficient, bank management should be directed to address the appropriateness of its ALLL (or ACL, when applicable) estimate and to provide additional allowances as necessary for estimated credit losses identified in the examination process that have not been included, or have not been fully included, in management's original ALLL (or ACL, when applicable) estimate.***

***Examiners should determine whether the bank's methodology could be utilized with adjustments to arrive at a reasonable and reliable estimate for additional needed provisions. If the bank's methodology can be utilized, examiners should direct bank management to make appropriate adjustments and use the most relevant information sources available to develop a reasonable estimate of the deficiency in the bank's ALLL (or ACL, when applicable). The information sources used should include examination loan review findings and publicly available data on real estate or other collateral values in the bank's lending area.***

***In the rare event, that the bank's methodology cannot be utilized even with adjustments (substantially inadequate loan review, material weakness in credit administration etc.) examiners should estimate the ALLL (or ACL, when applicable) deficiency in the absence of more relevant data. The selection and use of financial ratios or statistical models (utilizing bank-specific historical loss data) should be supported by sufficient analysis to demonstrate objective support for a short-term range of proxy estimates. However, such estimates based on industry or peer group information should only be used as a short-term proxy and cannot be accepted as a substitute for an effective ALLL (or ACL, when applicable) methodology. Bank management should be directed to correct deficiencies in their methodology as soon as possible.***

***Consider the following items in this section to determine an appropriate ALLL (or ACL, when applicable) level.***

[1] **ACL replaces the term ALLL for those banks that adopted ASU 2016-13.**

**3. Determine if the ALLL (or ACL, when applicable) is sufficient to cover estimated credit losses on:**

- **Loans classified Loss (in whole or in part) that have not yet been charged-off;**
- **Loans classified Doubtful (without partial Loss classification);**
- **All remaining adversely classified loans (without partial Loss or Doubtful classifications, either individually, if impaired under ASC Topic 310, or in groups);**
- **Other problem loans (either individually, if impaired under ASC Topic 310, or in groups); and**
- **Remaining categories of loans segmented into groups with similar risk characteristics.**

**4. Consider the bank's loan loss history in aggregate and by loan type.**

- **Calculate the average loan loss history, generally for the past five years, using net loan chargeoffs to average total loans. Such data should available in year-end UBPRs.**
- **Evaluate any aberrations in a specific year, and make adjustments as needed for current conditions to arrive at a realistic average that reflects loss expectations similar to current conditions.**
- **Consider migration analysis.**

**5. Consider the most recent, average reserve coverage of nonperforming loans by state, rating, and charter.**

***Note: Care should be exercised when considering reserve coverage because these ratios compare banks' ALLLs (or ACL, when applicable) to the amount of these loans, but the ALLL (or ACL, when applicable) should cover the estimated credit losses on the nonperforming loans, which is an estimate of the net chargeoffs likely to be realized on the loans. Particularly for nonperforming loans that are collateralized, net chargeoffs are not likely to equal the entire amount of these loans.***

**6. Consider the historical average of loan loss reserves to nonperforming loans for all banks within the region and the nation. (Reminder: Reserve coverage of nonperforming loans is typically higher at banks with sound loan portfolios. FDIC: Refer to the FDIC Quarterly Banking Profile.)**

**7. Consider the following factors to determine appropriate adjustments to the bank's average loss experience by loan type for nonclassified loans:**

- **Degree of board or committee involvement, oversight, and control;**
- **Expertise, training, and adequacy of loan staff;**
- **Adequacy of and adherence to the bank's loan policy;**
- **Effectiveness of collection procedures;**
- **Adequacy of renewal and extension policies;**
- **Adequacy of charge-off policies;**
- **Effectiveness of internal loan review function;**
- **Adequacy of appraisal procedures;**

- **Maintenance and analysis of financial information;**
- **Adequacy of documentation (other than financial information);**
- **Capitalization of interest;**
- **Over reliance on collateral values;**
- **Composition of the loan portfolio; *(Note: It may be appropriate to use different percentages for consumer, residential and commercial real estate, and commercial loans.)***
- **Existence of self-dealing and insider transactions;**
- **Level of classified loans and trend over past few examinations;**
- **Level and trend of internally identified loan problems;**
- **Level and trend of overdue and nonaccrual loans;**
- **General economic considerations (local, state, regional, national);**
- **Growth trends;**
- **Entry into new areas of lending;**
- **Extent of out-of-territory lending; and**
- **Adequacy of follow-up systems.**

***(Note: If the bank uses a formula approach that includes both historical loss experience and adjustments for qualitative or environmental factors to determine an appropriate level for the ALLL (or ACL, when applicable), it may be feasible to use the internal formula in arriving at the estimated credit losses for these loans even though the overall system may be considered inadequate.)***

## Portfolio Quality

**8. Determine the reasons for the current level of asset quality problems.**

- **Evaluate the impact of local economic conditions on the loan portfolio.**
- **Determine if there are sectors of risk within the portfolio by either type of or concentrations of risk.**
- **Evaluate the impact of ineffective underwriting in new product areas on the level and severity of classifications or delinquencies.**
- **Determine that individual account officers as well as lending committees have appropriate lending authorities.**
- **Evaluate delinquency levels by individual account officers.**
- **Evaluate individual loan officers' experience levels and expertise.**

**9. Based on the results of the above analysis, consider expanding the sample of loans (including off-balance sheet activities).**

## Managerial Effectiveness

**APPLICABLE LAWS AND REGULATIONS**

**10. Determine the cause of any violations and identify responsible parties. Consider the following items:**

- **Lack of familiarity with laws or regulations,**
- **Negligence,**
- **Misinterpretation, and**
- **Willful disregard or noncompliance.**

**CREDIT ADMINISTRATION**

**11. Determine why collateral appraisals are not sufficient to support current loan advances.**

**12. Determine why management did not correct identified deficiencies. Consider whether:**

- **Management overlooked issues,**
- **Management is unfamiliar with prudent loan portfolio practices and procedures, and**
- **Management is unwilling or unable to react to changing conditions.**

**13. Determine why loan losses are not recognized in a timely manner. Reasons for not recognizing losses in a timely manner may include the following:**

- **Inadequate identification or reporting of problem loans,**
- **Loss deferral motivated by earnings performance and bonus compensation, and**
- **Loss deferral motivated by poor financial condition.**

## Other Loan Related Topics

**OTHER REAL ESTATE (ORE)**

**14. Determine if management's non-compliance with regulations or accounting pronouncements are due to oversight, lack of requisite knowledge or experience, or a general disregard.**

**15. Compare expenses and income information contained in appraisals with the actual income and expenses of related income producing properties. Recalculate appraisal results using realistic assumptions, if necessary.**

**16. Investigate the deficiencies identified in managing foreclosed real estate.**

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| **17. Expand file sampling as necessary to accurately determine the quality of ORE. Where appropriate, consider conducting on-site inspections to assist in valuation and classification.** |
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| **REPOSSESSION** |
| **18. Investigate the deficiencies identified in managing repossessed assets.** |
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| **19. Expand file sampling as necessary to accurately determine the quality of repossessed assets. Where appropriate, consider physical inspections of the repossessed assets to assist in valuation and classification.** |
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| **NON-LEDGER ASSETS** |
| **20. Determine the underlying reasons for asset write-offs.** |
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| **End of Expanded Analysis. If needed, Continue to Impact Analysis.** |

# LOAN PORTFOLIO MANAGEMENT AND REVIEW: GENERAL

## 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** |
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| **1. Determine the impact of noted deficiencies on the institution's capital, earnings, and liquidity, and assess the future impact on the institution if these deficiencies continue.** |
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| **2. Assess the overall effectiveness of risk management practices in light of the identified deficiencies.** |
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| **3. Determine the impact of an inadequate ALLL (or ACL, when applicable) on the bank's earnings and capital.** |
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| **4. Determine the need for direct confirmation of loan accounts.** |
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| **5. If administrative or enforcement actions appear necessary, form specific recommendations and discuss concerns with appropriate supervisors. (FDIC: field office supervisor, regional office.)** |
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| **6. If approved by appropriate supervisors, discuss the possibility of administrative and enforcement actions with executive management and the board of directors.** |
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| **7. Investigate the circumstances and facts surrounding apparent violations. When necessary, prepare recommendations for appropriate actions** |
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| **End of Impact Analysis.** |