

Any attachments to this document are rescinded only as they relate to national banks and federal savings associations.

## Introduction

This section defines the types of trust and asset management examinations and discusses the considerations and techniques involved in proper planning and control of these examinations.

## Types of Examinations

Consistent with examinations in other areas, there are three principal types of trust and asset management examinations: regular, targeted and special.

A *regular examination* is an examination of an institution's trust department in which all necessary and applicable regulatory procedures are performed by the examiner. The regular examination is triggered by the rating assigned at the previous examination under the Uniform Interagency Trust Rating System (see Section 060). The trust department will always be assigned a rating at the completion of a regular examination.

A *targeted examination* is one that focuses on either outstanding items from the previous examination (i.e., areas identified as needing improvement or correction) or a review of selected areas (i.e., one or two specific types of accounts, new fiduciary services or compliance with a new regulation). A trust department can be assigned a new rating as a result of a targeted examination. If a targeted examination uncovers serious deficiencies in the trust department, it should be discontinued and a regular examination should be commenced.

A *special examination* is conducted for the initial six month review of denovos and in response to special or dictated circumstances. For example, if a regional office receives a complaint alleging mismanagement of a fiduciary account, an on-site investigation may be necessary to properly respond to the complaint. A trust department can be assigned a new rating as a result of a special examination.

## Examination Planning Objectives

Planning an examination provides direction and is essential in order to effectively and efficiently conduct the examination. It is during the planning process that decisions can be made regarding the overall objectives of the particular examination, the scope of the particular examination, the examination procedures to be used and the probable extent of testing and personnel requirements. The overall objectives of this phase of the examination process are to:

- collect and review as much information as possible prior to the on-site examination (or arrange for it to be available on-site at the start of an examination or at a preexamination scoping visit), so that the examination team can perform its work more efficiently on-site;
- minimize the amount of time spent during an examination waiting for essential data from the institution;
- develop a clearer understanding of the volume of trust and asset management activity, types of trust and asset management services and other information necessary to determine the examination scope, including activities that have transpired since the last examination;

- assist in determining personnel requirements and assigning areas of responsibility; and
- assist in estimating on-site examination time.

Prior to the commencement of a trust and asset management examination, the examiner should obtain and review all sources of information regarding the institution and its trust department, including (to the extent that each exists):

- the most recent trust and asset management examination report and workpapers;
- the most recent thrift, operating subsidiary, service corporation and/or state examination report;
- the most recent Annual Report of Trust Assets (ART) filed;
- business plan;
- conditions of approval of any applications;
- the most recent audit report; and
- any correspondence or other materials relating to activity that has transpired since the previous examination (e.g., directors' response letter, consumer complaints, request for rulings, outstanding enforcement actions, etc.).

The examiner should, if possible, discuss the institution and its trust department with the previous examiner-in-charge.

### Trust PERK

Keeping in mind that examination efficiency leads to a better overall work product, the institution should be asked to submit all or part of a completed Preliminary Examination Response Kit (PERK) prior to the on-site portion of the examination. The information not submitted in advance should be available on-site at the start of the examination. The collection and review of the information in the PERK should help minimize the examination time spent on-site. A copy of the trust and asset management PERK is contained in Section 041. The PERK is designed to be comprehensive and applicable to all savings associations, however, information requests may be added to or deleted from the PERK to accommodate the type and complexity of the institution or the examination. PERK information may be requested from management in three ways:

- Information marked with an "A" should be mailed to the EIC at least 10 business days prior to the start of the examination
- Information marked with an "X" should be provided to the EIC at examination commencement
- Information marked with an "R" should be made available for on-site review

If you elect to have information mailed prior to the on-site portion of the examination, the PERK should go out a few days earlier than recommended in the normal customer service standards. Examiners should not require savings associations to photocopy and ship materials if it creates rather than reduces regulatory burden. Regulatory staff should gauge the resources and attitudes of each institution when requesting off-site delivery.

## Examination Scope

Setting the scope of an examination is a critical component of the examination process, yet it is a process under which definitive and precise guidelines, equally applicable to all departments in all instances, cannot and should not be provided. Nevertheless, the following paragraphs discuss some broad parameters that should be considered when setting the examination scope. As noted throughout this handbook, the scope of an examination relates to a particular subject area and a number of specific factors should be considered, not all of which may be evident prior to the on-site portion of the examination. Most importantly, the scope must be tailored to fit the individual circumstances that exist in a department.

- \* Examination scope must be established in stages. Throughout this entire process, setting the examination scope is closely related to the examination approach. The first stage consists of reviewing comments contained in past examination and audit reports, workpapers and other preexamination materials. This will aide examiners to develop a feel for the trust department's previous condition. If any adverse matters were contained in those materials, they should be specially reviewed at the subsequent examination in order to ensure that appropriate corrective action was taken. This follow-up review would include verifying any assurances given by management in its written response to the previous report of examination that any adverse matters had received appropriate attention. Similarly, any significant matters that have transpired between examinations should be incorporated into the examination scope.
- \* The extent of internal or external audit coverage should be determined and any audit reports issued since the last examination should be reviewed. This review may allow the examiner to formulate initial conclusions concerning audit coverage, indicate additional areas for examiner review (e.g., follow-up of exceptions noted in the report) and aide in delineating examination procedures to perform or not perform (e.g., if certain procedures were performed by auditors, the examiner would ordinarily not duplicate those procedures unless significant weaknesses were noted).
- \* An assessment should be made to determine whether the institution has implemented a formal risk management and compliance program. Reports issued by these two functions should be reviewed at the start of the examination and, as with the review of the audit coverage, a determination should be made as to the effectiveness of these programs. If it is evident that the management oversight provided by audit, compliance and risk management programs is sound, a reduction in examination scope may be warranted.
- \* The preliminary scope will often be expanded, contracted or otherwise refined once the on-site portion of the examination begins, as a result of additional information obtained from management conferences and initial review of policies, procedures, internal control reports, files and ledgers. For example, the lack of policies or procedures in a given area would generally indicate a need for testing, since an examiner cannot conclude that practices conform to a nonexistent policy or procedure. In addition, development of and compliance with, any new or revised policies or procedures would ordinarily be reviewed in more depth than existing ones.
- \* Finally, the scope may be adjusted once the examination has begun. The depth of review accorded to individual subject areas should be dependent upon the degree to which there has been activity in that area in a particular department. For example, topics such as experience level and adequacy of staffing would be reviewed in greater depth if a department had experienced substantial turnover since the last examination, in contrast to a department in which personnel had remained relatively stable. Similarly, the area affected by the turnover would be reviewed in greater depth. In situations where there are new hires, such as a new account administrator, a sample of his or her accounts may be selected for review.

## Examination Procedures

Examination programs are organized in a top-down fashion and are divided into three groups, each representing a different level of review (Levels I, II and III). The top-down approach begins with a review of policies, procedures and internal controls while focusing on the overall condition of the institution (Level I). With this approach, regulatory personnel can assess the degree of risk in each area of an institution's operations early in the examination and determine the depth of review and the procedures (Levels I, II and III) needed.

The optional topic questions following the program are intended to serve as guides and reminders for the examiners. Less experienced examiners will find the questions especially useful as guides for the effective completion of assigned phases of examinations. More experienced examiners should use the optional topic questions as reminders of what is expected to be reviewed within each phase of an examination.

Not all programs will be applicable to an institution, and furthermore, of those programs used for a particular examination, not all procedures will be needed. The examination scope should help determine the level of review.

When using this risk-based examination approach, the examiner should use sound professional judgment to ensure that the depth of review is adequate but not excessive. The following is a discussion of the three levels of procedures available to the examiner.

### Level I

Level I procedures focus on the review of examination scoping materials; institution and regulatory documents; policies and procedures; relevant PERK documents; ECEF reports; previous examination reports; and committee minutes. In addition, the Level I review is followed-up by interviews with personnel to determine if practices conform to written guidelines and to confirm any other preliminary findings.

If items of concern are uncovered during Level I analysis or if problems were identified during the preexamination monitoring and scoping, the examiner may need to use some or all Level II procedures.

### Level II

Level II procedures focus on further institution materials and management reports, as well as more in depth interviews. These procedures may also include reviewing a small sample of account files and/or transactions to support a conclusion for a specific area.

Level I and selected Level II procedures normally provide a comprehensive analysis from which conclusions can be drawn but do not include any significant auditing procedures. If the examiner cannot rely on the data contained in institution records, Level III procedures may be necessary.

### Level III

Level III procedures include steps that auditors usually perform. Although certain situations may require Level III procedures, it is not standard practice of Office of Thrift Supervision (OTS) examiners to duplicate the testing efforts of auditors.

*Again*, it may not be necessary to complete every program or every procedure within a program. The examiner has the discretion to determine which programs and procedures are necessary to address the scope

and reach a sound conclusion. In some situations it may be even appropriate to customize existing procedures or to perform procedures that are not listed within a program in order to achieve the most efficient and meaningful analysis. The examiner should, however, document any decisions to deviate significantly from the initial scope instructions or to modify existing procedures on the relevant programs.

### Examination Management

Once the examination materials are obtained and reviewed, the “examiner in charge” (EIC) should be in a good position to identify areas of the institution’s operations where examination time can best be focused. For example, if the response to the PERK lists a number of transactions with affiliates or discretionary use of affiliated products or the savings association’s securities, examination resources should emphasize the conflicts of interest area of the compliance section. In addition, review of the information should assist the EIC to determine with greater precision the specific work assignments to be completed and in turn, enable the EIC to assign that work to other members of the examination team. The EIC should also discuss or prepare a memorandum for the examination team addressing the preliminary examination scope and the rationale for that scope with emphasis on any special concerns disclosed as a result of the examination analysis and review process.

Once the examination has begun, the EIC must closely monitor its progress and supervise and coordinate the work of the examination team. Any adjustments in the scope of the examination should be made as early as possible or, if in response to current circumstances, immediately. As assignments are completed, the EIC should review workpapers to ensure that they are factually complete, that they support the conclusions reached and that any deviations from the initial scope are documented and explained.

At the start of the examination, the EIC should meet with the savings association’s executive management (including management of the institution and the trust department). The meeting should discuss the department’s general condition, changes in key personnel, strategic planning and business activity that have occurred since the previous examination. The EIC should introduce any other members of the examination team and convey the anticipated scope of the examination. Executive management should introduce staff responsible for the most important areas of the trust department and provide a contact person if examiners need assistance. Examples of key personnel in a larger department would include the compliance officer and persons responsible for trust operations, trust investments and account administration.

In addition to the above objectives, this initial meeting should strive to establish an effective working relationship between the examiners and management to expedite the examination process and minimize operational intrusions. As is the case with examinations in other areas, examiners must observe the highest standards of professional and personal conduct. Examiners are often the only representatives of OTS that the savings association meets; it is therefore important that a favorable impression be made. The EIC should structure the examination in such a manner as to minimize disruptions and intrusions of department personnel and activity.

The EIC should determine what additional information will be needed during the examination, at least initially. This determination can be based on a number of factors, including the EIC’s overall experience or previous experience with the particular department, the extent of information requested (and received) during the preexamination planning process and the information maintained by and in the department (i.e., computer runs and management reports). Section 042 summaries typical information maintained by a department that may be useful to the examination team.

Throughout the examination, the EIC should continue to meet with senior management to discuss the status of the examination. These meetings should be viewed as a vehicle for improving an understanding of the trust department's processes as well as informing management of any critical areas of concern. When possible, the EIC should identify areas where corrective action will be necessary, obtain management's concurrence and suggest that such action be implemented immediately. If corrective action is implemented during the examination, it should be noted in the report of examination.

### Examination Conclusions

The ability to formulate conclusions, prioritize findings and communicate those findings to trust department management, boards of directors and OTS personnel is critical to the regulatory and supervisory process. As individual examination assignments are completed and workpapers compiled, the EIC should begin to formulate an impression of the department's overall condition. The objectives of developing examination findings and conclusions in preparation for the closing conference with senior management and the report of examination are:

- to review all major findings from the examination (including work performed by assistants if not previously reviewed) and to verify that all assertions of facts and opinions are substantiated in the workpapers;
- to convert the assembled information into a unified assessment of comments and conclusions relative to specific subject areas or practices, the department's present condition, future prospects and its adherence to sound fiduciary practices;
- to formulate recommended corrective action when appropriate, based on those comments and conclusions; and
- to communicate the results of the examination to appropriate personnel in the department, institution and OTS through the closing conference and the report of examination.

Conclusions and recommendations should be based on objective information gathered during the examination. In order to attain their maximum effectiveness, conclusions must be drawn from a comprehensive analysis of patterns and practices. Although individual violations or other significant and substantive deficiencies must be dealt with, emphasis on the pattern or practice, the cause of the violation, will not only bring about better and more effective corrective action but will also enhance future compliance.

This handbook, the trust rating system and the report of examination are all organized in terms of a department's overall exercise of trust powers and the exercise of those powers as it relates to five major subject areas. This format is also a convenient one in which to form conclusions and to organize the agenda of the closing management conference.

### Management Discussions

The objectives of the closing conference are to inform the chief executive officer (and/or other senior management) of the examiner's evaluation of the department's condition and to reach agreement, where possible, on the accuracy of the issues presented and management's commitment to initiate appropriate corrective or other action based upon the examination findings. The closing conference should leave management and the examiner with a clear and mutual understanding of what items will appear in the report of examination and what the overall tone of the report will be. The examiner should present findings and conclusions as well as the potential composite and individual MOECA component ratings and be receptive to

any evidence presented by management that is contrary to those findings and conclusions. No critical items should appear in the report of examination unless they were discussed at this closing conference.

The personnel with whom the examiner should discuss the examination findings depend upon the nature of the findings, the structure of the savings association and past experience in communicating and correcting adverse matters. Isolated, technical or other nonsubstantive findings should be presented to the individual responsible (assuming they should be presented at all), such as the operations officer or the account administrator responsible for the individual account. Overall or significant findings and trends should be presented to senior management of the department and the chief executive officer of the savings association. Adverse findings related to audits should be presented to the internal auditor or audit committee.

The OTS examination approach emphasizes the role that a savings association's board of directors plays in establishing policies and procedures for the safe and sound operation of its trust and asset management activities. Since the OTS believes that board members, particularly trust committee members, should be involved in the regulatory process, it is important that they be given the opportunity to meet with examination personnel following an examination. Therefore, the practice of meeting periodically with the trust committee (or similar committee having board of directors representation) and the full board of directors is encouraged in all instances. Participation in such meetings allows the examiner to communicate examination findings to a broad audience and fosters open communication, which should result in a better understanding of the respective roles of management and examiners. The examiner should also be able to evaluate the knowledge of, and degree of involvement by, those personnel in the operation of the trust department.