Prompt Corrective Action: Guidelines and Rescissions

Summary


Note for Community Banks

This OCC bulletin applies to all FDIC-insured national banks, federal savings associations (FSA), and federal branches of foreign banking organizations (collectively, banks). 1

The Economic Growth, Regulatory Relief, and Consumer Protection Act (Pub. L. 115–174) (Act) was signed into law on May 24, 2018. The Act requires the OCC, the Federal Deposit Insurance Corporation (FDIC), and the Board of Governors of the Federal Reserve System to establish a simplified leverage ratio capital framework for qualifying community banks. The framework would specify a minimum leverage ratio that would deem a qualifying bank to be well-capitalized for prompt corrective action purposes. As of the publication of this OCC bulletin, this framework was not yet established.

Background

The purpose of prompt corrective action (PCA) is to resolve the problems of insured depository institutions at the least possible long-term loss to the Deposit Insurance Fund. 2 Section 38 of the Federal Deposit Insurance Act (FDI Act) (12 USC 1831o), as added by section 131 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), establishes a system of PCA that classifies insured depository institutions into five categories based on their regulatory capital ratios. The OCC's regulations implementing 12 USC 1831o are 12 CFR 6 (national banks and FSAs); 12 CFR 19, Subparts M and N (national banks); and 12 CFR 165.8 and 12 CFR 165.9 (FSAs).

The PCA capital categories should not be considered indications of capital adequacy under 12 CFR 3, the OCC's capital adequacy regulation. For example, a bank that is well capitalized for the purposes of 12 CFR 6 may be found by the OCC to have inadequate capital for the purposes of 12 CFR 3. The OCC assesses capital adequacy based on the bank's risk profile relative to its risk management. Under 12 CFR 3, the OCC may require a bank to maintain a higher individual minimum capital ratio, without regard for the bank's PCA capital category. 3

PCA Capital Categories

12 USC 1831o establishes a framework of supervisory actions based on the capital level of a bank. The statute establishes the following five PCA capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized.

National Banks and Federal Savings Associations

The OCC's regulation defines the PCA capital thresholds for each capital category at 12 CFR 6.4 using the following ratios:

- Total risk-based capital (RBC) ratio
- Tier 1 RBC ratio
- Common equity tier 1 (CET1) ratio
- Leverage ratio
The calculation of these ratios must be in accordance with the definitions in 12 CFR 3. Additionally, management of a bank with any ratio below the minimum capital requirements in 12 CFR 3 should monitor the bank’s tangible equity ratio to determine if the bank is critically undercapitalized.

To be "well capitalized," each of the bank’s capital ratios must meet or exceed the levels set in 12 CFR 6.4. Regardless of a bank’s capital level, no bank is considered well capitalized if it is subject to any written agreement, order, capital directive, or PCA directive that requires the bank to meet and maintain a specific capital level for any capital measure. Banks in compliance with such agreements, orders, or directives will not be "well capitalized" unless and until the agreement, order, or directive is terminated or modified to eliminate the capital requirement.

The following table summarizes the capital thresholds for each PCA capital category applicable to national banks and FSAs.

Table 1: PCA Capital Category Ratios for National Banks and FSAs

<table>
<thead>
<tr>
<th>PCA capital category</th>
<th>Total RBC ratio</th>
<th>Tier 1 RBC ratio</th>
<th>CET1 RBC ratio</th>
<th>Tier 1 leverage ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Well capitalized</td>
<td>10%</td>
<td>8%</td>
<td>6.5%</td>
<td>5%</td>
</tr>
<tr>
<td>Adequately capitalized</td>
<td>8%</td>
<td>6%</td>
<td>4.5%</td>
<td>4%</td>
</tr>
<tr>
<td>Undercapitalized</td>
<td>&lt; 8%</td>
<td>&lt; 6%</td>
<td>&lt; 4.5%</td>
<td>&lt; 4%</td>
</tr>
<tr>
<td>Significantly undercapitalized</td>
<td>&lt; 6%</td>
<td>&lt; 4%</td>
<td>&lt; 3%</td>
<td>&lt; 3%</td>
</tr>
</tbody>
</table>

**Critically undercapitalized**

Tangible equity to total assets ≤ 2%

Tangible equity means the amount of tier 1 capital, as calculated in accordance with 12 CFR 3, plus the amount of outstanding perpetual preferred stock (including related surplus) not included in tier 1 capital. Total assets means quarterly average total assets as reported on the bank's call report. The OCC reserves the right to require a bank to compute and maintain its tangible equity ratio on the basis of actual, rather than average, total assets. Refer to 12 CFR 6.2.

Insured Federal Branches

Insured federal branches of foreign banking organizations are not subject to the minimum capital requirements applicable to insured national banks. Instead, the OCC requires insured federal branches to comply with the FDIC's regulations governing pledge of assets and the level of eligible assets to determine the insured federal branch's PCA capital category. The following table summarizes those ratios and corresponding PCA capital categories:

Table 2: PCA Capital Category Ratios for Insured Federal Branches

<table>
<thead>
<tr>
<th>PCA capital category</th>
<th>Pledged assets ratio (refer to 12 CFR 347.209)</th>
<th>Asset maintenance ratio (refer to 12 CFR 347.210)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Well capitalized</td>
<td>≥ 5.0%</td>
<td>≥ 108%</td>
</tr>
<tr>
<td>Adequately capitalized</td>
<td>≥ 5.0%</td>
<td>≥ 106%</td>
</tr>
<tr>
<td>Undercapitalized</td>
<td>&lt; 5.0%</td>
<td>&lt; 106%</td>
</tr>
<tr>
<td>Significantly undercapitalized</td>
<td>&lt; 104%</td>
<td></td>
</tr>
<tr>
<td>Critically undercapitalized</td>
<td>&lt; 102%</td>
<td></td>
</tr>
</tbody>
</table>

Additionally, for an insured federal branch to be well capitalized, it must not have received written notification.
from the OCC to increase the insured branch's capital equivalency deposit pursuant to 12 CFR 28.15, or to comply with asset maintenance requirements pursuant to 12 CFR 28.20.

from the FDIC to pledge additional assets pursuant to 12 CFR 347.209 or to maintain a higher ratio of eligible assets pursuant to 12 CFR 347.210.

Notification of Capital Category

Bank management should monitor the bank's capital levels to remain aware of the bank's PCA capital category. Management of a bank that operates with capital levels at or near the regulatory minimums in 12 CFR 3 should be attentive to the impact of the bank's operations on capital ratios to avoid becoming subject to restrictions and requirements applicable to undercapitalized, significantly undercapitalized, or critically undercapitalized banks. As such, management of banks operating near the regulatory minimums should generally engage in more frequent monitoring of the bank's capital ratios than a bank that is well-capitalized under PCA.

A bank becomes subject to the mandatory restrictions applicable to a given PCA capital category as of the date it is notified of, or is deemed to have notice of, its PCA capital category. Under 12 CFR 6.3(b), a bank is deemed to be notified of its capital levels and its PCA capital category as of the most recent of the following dates:

- A Consolidated Report of Condition and Income (call report) is required to be filed with the OCC.
- A final report of examination is delivered to the bank.
- The OCC provides written notice to the bank
  - of the bank's PCA capital category, or
  - that the bank's PCA capital category has changed pursuant to 12 CFR 6.3(e) or 12 CFR 6.4(e), 12 CFR 19, subpart M (national banks), or 12 CFR 165.8 (FSAs).

When the OCC determines, through an examination or otherwise, that a bank's PCA capital category has changed, the appropriate OCC supervisory office must notify the bank of that determination in writing.

If a material event occurs between call report periods that would cause the bank to be placed in a lower PCA capital category, the bank must notify the OCC that the bank's PCA capital category may have changed. Examples of a material event include accounting adjustments resulting from an external audit, a large operating loss, or provision to the allowance for loan and lease losses (ALLL). The bank must inform the appropriate OCC supervisory office in writing of the details of the change within 15 calendar days of the material event. The supervisory office must review the bank's submission and determine whether to change the bank's PCA capital category and notify the bank of the OCC's determination.

If a bank's capital ratio(s) improve between call report periods, the bank may request that the OCC reassess the bank's PCA capital category. Movement into a higher PCA capital category is not automatic and occurs only if the OCC concurs.

Moreover, a bank that incorrectly reports its financial condition in its call report by deferring losses or by failing to make sufficient provisions to its ALLL violates 12 USC 161 (national banks) or 12 USC 1464(v) (FSAs). Such violations may subject the bank or its institution-affiliated parties to enforcement actions, including civil money penalties.

Reclassification Based on Unsafe or Unsound Condition or Practice

The OCC may, under certain circumstances, reclassify a well-capitalized bank as adequately capitalized. In addition, the OCC may require an adequately capitalized or undercapitalized bank to comply with the supervisory provisions applicable to banks in the next lower capital category if the bank is in an unsafe or unsound condition or engaged in an unsafe or unsound practice.

A bank may be reclassified if the OCC determines, after notice and opportunity for an informal agency hearing, that the bank is in an unsafe or unsound condition or is engaged in an unsafe or unsound practice. A bank may be deemed to be engaged in an unsafe and unsound practice if the bank has received a less-than-satisfactory rating in its most recent report of examination for asset quality, management, earnings, or liquidity and the bank has not corrected the deficiency.
The supervisory office, together with assigned legal staff, is typically responsible for presenting recommendations regarding PCA reclassifications to the appropriate supervision review committee. The appropriate Senior Deputy Comptroller must approve sending a notice of intent to reclassify, although the notice of intent is sent by the supervisory office.

Notice of Intent to Reclassify

The OCC must provide a bank with prior written notice of intent by the OCC to reclassify. A notice of intent to reclassify must include the following:

- The reasons for the proposed reclassification.
- A statement of the bank’s capital ratios and capital levels and the category to which the bank would be reclassified.
- The date by which the bank may respond and request an informal hearing.

The bank’s response and request for an informal hearing must be made within 14 days of receiving notice of the intent to reclassify, unless the OCC specifies a different time frame. The OCC may shorten the period for response if it determines that a shorter time period is appropriate in light of the financial condition of the bank or other relevant circumstances. Failure to respond within the specified time period constitutes a bank’s waiver its opportunity to respond and constitutes consent to the reclassification.

Informal Hearing

The bank has the right to an informal OCC hearing on the proposed reclassification. The bank has the right to introduce relevant written materials and to present oral argument at the hearing. In its request for a hearing, the bank must include any request to present oral testimony or witnesses at the hearing and must list the names of witnesses and the general nature of their expected testimony. The bank may introduce oral testimony and present witnesses only if authorized by the OCC or the presiding officer.

After receiving a timely written request for an informal hearing the OCC must issue an order directing that the hearing commence within 30 days of the request. The OCC may allow additional time if requested by the bank.

An OCC official not involved in the initial recommendation to reclassify the bank must serve as the presiding officer conducting the hearing. Within 20 days after the informal hearing, the presiding official must make a reclassification recommendation to the appropriate Senior Deputy Comptroller. The OCC’s final decision on whether to reclassify the bank must be issued within 60 calendar days after the hearing record is closed, or the date of the response in a case where no hearing was requested.

Restrictions Applicable to Reclassified Banks

A well-capitalized bank that is reclassified as adequately capitalized is not subject to any additional restrictions under 12 USC 1831o. Other restrictions or requirements, however, may apply to such reclassified banks.

The OCC may require an adequately capitalized or undercapitalized bank to comply with one or more of the provisions applicable to banks in the next lower capital category (except the requirement to file a capital restoration plan (CRP)). The mandatory restrictions that apply without any action by the OCC to undercapitalized and significantly undercapitalized banks, however, do not automatically apply to reclassified banks. Such restrictions only apply if ordered by the OCC. For example, an adequately capitalized bank that is reclassified as undercapitalized may be prohibited from making capital distributions or subjected to asset growth restrictions, but only if the OCC expressly orders it. Other restrictions or requirements may also apply to some reclassified banks.

Prohibition on Disclosure of Capital Category

Banks are prohibited from disclosing their PCA capital categories in advertisements or promotional materials, unless such disclosure is required by law or authorized by the OCC.
The OCC recognizes that disclosure of a bank’s capital category may be appropriate in certain circumstances and under certain conditions. For example, disclosure of the bank’s PCA capital category, and related material regulatory restrictions, may be required under federal securities and banking laws in a bank’s securities filings or in annual or quarterly reports. Moreover, the restriction on disclosure in advertising is not intended to prohibit a bank from disclosing its PCA capital category in response to inquiries from investors, customers, or other third parties as long as the bank also provides appropriate caveats regarding the PCA capital category. A bank that discloses its PCA capital category to the public (e.g., in a securities filing, in an annual report, or in response to an inquiry) should also disclose that the bank’s capital category is determined solely for the purposes of applying PCA and that the PCA capital category may not constitute an accurate representation of the bank’s overall financial condition or prospects.

If a bank discloses its PCA capital category, and the capital category subsequently changes, the bank may have an obligation to disclose the change. In addition, management or the board of directors of a bank that believes materially false or misleading information relating to the bank’s PCA capital category exists in the marketplace should also consider whether the bank has an obligation to correct the information under applicable federal securities and banking law.

### PCA Restrictions

Banks in each PCA capital category are subject to certain statutorily prescribed restrictions. The restrictions become increasingly severe as the bank moves downward through each successive PCA capital category. Some of the restrictions are mandatory and apply without any action by the OCC when a bank is notified of its capital category. Other restrictions may be imposed by the OCC by issuance of a PCA directive.

A bank may be subject to other restrictions or requirements based on the bank’s PCA capital category, for example, restrictions on brokered deposits, prohibition from accepting employee benefit plan deposits, limits on exposure to interbank liabilities, and risk-based deposit assessment. Some of these statutes and regulations use definitions of the capital categories that are different from the definitions in 12 USC 1831o.

Banks and OCC supervisory offices should refer to the relevant statute and regulation to determine the appropriate capital category for each restriction.

The following table summarizes PCA restrictions for each PCA capital category. More details are provided in the sections following the table.

**Table 3: Summary of Applicable PCA Provisions by PCA Capital Category**

<table>
<thead>
<tr>
<th>PCA category</th>
<th>Applicable PCA provisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Well capitalized or adequately capitalized</td>
<td>The bank must not make a capital distribution or pay management fees if the bank would be undercapitalized after making such distributions or paying such fees.</td>
</tr>
<tr>
<td>Undercapitalized</td>
<td>Same as adequately capitalized banks, plus restrictions on asset growth, acquisitions, new branches, and new lines of business. Bank must submit an acceptable CRP to the OCC within 45 days of the date the bank was notified of its undercapitalized status, unless the OCC specifies a different time frame. Discretionary application of certain restrictions otherwise applicable only to significantly undercapitalized banks.</td>
</tr>
</tbody>
</table>
Significantly undercapitalized banks and undercapitalized banks that have failed to submit an acceptable CRP

- restrictions on senior executive officer compensation.

The OCC must also take one or more of the following actions:

- Require recapitalization.
- Restrict affiliate transactions.
- Restrict interest rates on deposits.
- Further restrict asset growth or require the bank to reduce assets.
- Require the bank to alter, reduce, or terminate activities.
- Require the bank to improve management by electing new directors, dismissing directors or senior executive officers, or requiring qualified senior executive officers.
- Prohibit the bank’s acceptance of deposits from correspondent banks.
- Require certain divestitures of subsidiaries.
- Require the bank to take any other action the OCC determines will resolve the bank’s problems at the least possible long-term cost to the Deposit Insurance Fund more effectively than any of the actions described here.

Critically undercapitalized

Same as significantly undercapitalized banks and undercapitalized banks that have failed to submit and implement an acceptable CRP, plus

- receivership or conservatorship within 90 days, or such other action the OCC determines, with the concurrence of the FDIC, would better achieve the purposes of PCA.
- restrictions on payments of principal or interest on the bank’s subordinated debt.

The FDIC must also prescribe certain further restrictions on the activities of the bank.

All Banks

Pursuant to 12 USC 1831o(d), banks of any PCA capital category are prohibited from making any capital distribution\textsuperscript{20} to shareholders or paying any management fee\textsuperscript{21} to any person with control\textsuperscript{22} over the bank if after making the distribution or paying the fee, the bank would be undercapitalized. This prohibition means that no undercapitalized, significantly undercapitalized, or critically undercapitalized bank may make any capital distribution to shareholders or pay any management fee to a controlling person.
A limited exception to the prohibition on capital distributions is provided for stock redemptions. Under 12 USC 1831o(d)(1)(B), the OCC may permit, after consultation with the FDIC, a bank to repurchase, redeem, retire, or otherwise acquire shares or ownership interests if the repurchase, redemption, retirement, or other acquisition

- is made in connection with the issuance of additional shares or obligations of the institution in at least an equivalent amount; and
- will reduce the institution’s financial obligations or otherwise improve the institution’s financial condition.

**Undercapitalized Banks**

Undercapitalized banks are subject to mandatory requirements, and may be subject to discretionary requirements. Mandatory requirements apply by operation of law, without any action by the OCC. The following are the mandatory requirements:

- Restrictions on asset growth, acquisitions, new branches, and new lines of business.
- The bank must submit an acceptable CRP to the OCC within 45 days of the date the bank was notified of its undercapitalized status, unless the OCC specifies a different time frame.

The OCC may impose any of the discretionary restrictions applicable to significantly undercapitalized banks by issuance of a PCA directive, if the OCC determines that such actions are necessary to help resolve the problems of the bank at the least possible long-term cost to the Deposit Insurance Fund. Refer to the "PCA Restrictions for Significantly Undercapitalized Banks and Certain Undercapitalized Banks" section of this bulletin for more information.

**Restrictions on Asset Growth and Expansion of Activities**

An undercapitalized bank's average total assets during any calendar quarter must not exceed its average total assets during the preceding quarter unless

- the OCC has approved its CRP;
- the increase in total assets is consistent with the approved CRP; and
- the bank's ratio of tangible equity to assets increases during the calendar quarter at a rate sufficient to enable it to become adequately capitalized within a reasonable time.

Each undercapitalized bank must secure the prior written approval of the OCC to acquire an interest in any company or insured depository institution, establish or acquire any additional branch office, or engage in any new line of business (collectively, expansion of activities). The OCC cannot approve expansion of activities unless the bank is operating under an approved CRP.

**Monitoring Undercapitalized Banks**

The OCC must

- closely monitor the condition of the bank.
- closely monitor compliance with restrictions and requirements imposed under PCA.
- closely monitor compliance with the CRP.
- periodically determine whether the restrictions, requirements, and CRP are achieving the purpose of PCA.

The OCC should conduct these activities at least quarterly, unless the supervisory office determines that another review schedule will provide sufficiently close monitoring. The bank's portfolio manager or examiner-in-charge is generally responsible for monitoring the bank's financial condition each quarter using call reports and other relevant information provided by the bank. The examiner should document the results of each quarter's review and discuss the need for any additional action with the supervisory office.

**Significantly Undercapitalized Banks and Certain Undercapitalized Banks**

Significantly undercapitalized banks are subject to the mandatory restrictions applicable to undercapitalized banks, plus restrictions on senior executive officer compensation. These
restrictions also apply to undercapitalized banks that have failed to submit or implement, in any material respect, an acceptable CRP.

If a significantly undercapitalized bank has already submitted an acceptable CRP, the supervisory office should review the CRP and determine whether to require a new or revised CRP. Table 3 summarizes the mandatory and discretionary requirements.

Additionally, the OCC generally must take one or more discretionary actions, as indicated in the "Discretionary Actions" sub-section.

Restrictions on Senior Executive Officer Compensation

Significantly undercapitalized banks, and undercapitalized banks that have failed to submit or implement, in any material respect, an acceptable CRP, are required to obtain the prior written approval of the OCC before paying any bonus or increasing the compensation to any senior executive officer. If the bank has not submitted an acceptable CRP, the OCC cannot approve such a request.

Discretionary Actions

12 USC 1831o directs the OCC to take at least one of the following actions against each significantly undercapitalized bank, and against each undercapitalized bank that fails to submit or implement an acceptable CRP. While these actions are generally discretionary, 12 USC 1831o presumes that the OCC will take the first three actions listed below unless the OCC determines the actions would not further the purposes of PCA.

- Require recapitalization through one or more of the following:
  - Requiring the sale of enough shares or obligations of the bank so that the bank will be adequately capitalized after the sale. The OCC may further require that instruments sold be voting shares.
  - Requiring the bank to be acquired by a depository institution holding company, or to combine with another insured depository institution, if one or more grounds exist for appointing a conservator or receiver for the institution.

- Restrict transactions with affiliates by requiring the bank to comply with 12 USC 371c as if the exemption in 12 USC 371c(d)(1) did not apply (commonly referred to as the "sister bank exemption"). The OCC may also further restrict the bank's transactions with affiliates.

- Restrict interest rates paid on the bank's deposits to the prevailing rates in the region where the bank is located, as determined by the OCC. The OCC cannot retroactively restrict interest rates paid on time deposits made before the OCC imposed the interest rate restriction under 12 USC 1831o(f)(2)(C)(i).

- Further restrict the bank's asset growth or require the bank to reduce its total assets.

- Restrict activities by requiring the bank or its subsidiaries to alter, reduce, or terminate any activity that the OCC determines poses excessive risk to the bank.

- Improve management through one or more of the following:
  - Ordering a new election for the bank's board of directors.
  - Requiring the bank to dismiss directors or senior executive officers who held office for more than 180 days immediately before the institution became undercapitalized. Dismissal under PCA does not constitute a removal action under 12 USC 1818.
  - Requiring the bank to employ qualified senior executive officers, who, if the agency so specifies, are subject to OCC approval.

- Prohibit the bank from accepting deposits from correspondent banks, including renewals and rollovers of prior deposits.

- Require the bank to divest itself of or liquidate any subsidiary if the OCC determines that the subsidiary is in danger of becoming insolvent and poses a significant risk to the bank, or is likely to cause significant dissipation of the bank's assets or earnings. The OCC must consult with other regulators when such an affiliate is a broker, dealer, government securities broker, investment company, or investment adviser, or if the affiliate is subject to any financial responsibility or capital requirement of another regulator.
• Require the bank to take other action(s) that the OCC determines will better carry out the purpose of PCA.

There are additional discretionary actions that can be taken against parent companies and affiliates by the appropriate federal banking agency, generally the Board of Governors of the Federal Reserve System. If the OCC determines that such actions would improve the bank's condition, the supervisory office should contact the Board of Governors of the Federal Reserve System or appropriate Federal Reserve Bank.

PCA Restrictions for Critically Undercapitalized Banks

Critically undercapitalized banks are subject to all the mandatory and discretionary restrictions applicable to significantly undercapitalized banks. Critically undercapitalized banks are also subject to several additional actions, including

• receivership or conservatorship within 90 days, or such other action that the OCC determines, with the concurrence of the FDIC, would better achieve the purposes of PCA.
• restrictions on payments of principal or interest on the bank's subordinated debt.

In addition to these actions, the FDIC may, by regulation or order, restrict the activities of a critically undercapitalized bank. Refer to the "FDIC Restrictions on Activities" section of this bulletin for more information.

Appointment of Receiver or Conservator

Critically undercapitalized banks are required to be placed in receivership or conservatorship within 90 days of becoming critically undercapitalized unless the OCC and FDIC agree that another action would better achieve the purposes of PCA. Except in rare circumstances, the OCC appoints the FDIC as receiver within 90 days of a bank becoming critically undercapitalized. In rare cases, the OCC may consider appointing a conservator instead of a receiver. The FDIC must agree in writing before a conservator, rather than a receiver, can be appointed.

If the OCC determines that a bank should not be placed into receivership or conservatorship, the OCC must document the reasons an alternate action would better serve the purpose of PCA and receive the FDIC's concurrence to take the alternate action. If the FDIC concurs, no receiver or conservator need be appointed within 90 days of the bank becoming critically undercapitalized. The determination to defer placing a bank in receivership or conservatorship must be reviewed every 90 days. If the alternative action fails to restore capital, the OCC is required to appoint a receiver if the institution is critically undercapitalized on average during the calendar quarter beginning 270 days after the date on which the bank became critically undercapitalized. A limited exception to this requirement is possible when all of the following conditions are met:

• The OCC determines and the FDIC concurs that
  • the bank has positive net worth;
  • the bank has been in substantial compliance with an approved CRP that has required consistent improvement in the bank's capital since the approval date;
  • the bank is profitable or has an upward trend in earnings that the OCC projects as sustainable; and
  • the bank is reducing its ratio of nonperforming loans to total loans.
• The Comptroller of the Currency and the Chairperson of the FDIC certify, in writing, that the bank is viable and is not expected to fail.

Restriction on Payment of Subordinated Debt

Critically undercapitalized banks are also prohibited from making any payments of principal or interest on the bank's subordinated debt (without the prior approval of the FDIC) beginning 60 days after becoming critically undercapitalized.

FDIC Restrictions on Activities
Unless given prior written approval by the FDIC, critically undercapitalized banks are prohibited
from the following:

- Entering into any material transaction, other than in the usual course of business, that
  would normally require prior notice to the OCC.
- Extending credit for any highly leveraged transaction.
- Amending the bank’s charter or bylaws, except to the extent necessary to carry out any
  other requirements of law, regulation, or order.
- Making any material change in accounting methods.
- Engaging in any covered transaction, as that term is defined in 12 USC 371c(b)(7).
- Paying excessive compensation or bonuses.
- Paying rates of interest on new or renewed liabilities at a rate that would increase the
  bank’s weighted average cost of funds to a level significantly above the prevailing rates of
  interest on insured deposits in the bank’s normal market areas.

Capital Restoration Plans

A bank must submit a CRP to the OCC supervisory office within 45 days after the bank has
notice, or is deemed to have notice, that it is undercapitalized, significantly undercapitalized, or
critically undercapitalized, unless the OCC specifies a different time frame.

If a bank is operating under an approved CRP and its capital category changes, it must file a
new or revised CRP only when required by the OCC in writing.

Content of Capital Restoration Plan

To prepare an acceptable CRP, a bank’s board of directors and management should analyze the
current condition and future prospects of the bank to determine the most efficient and expedient
way to return the bank to the adequately capitalized PCA capital category. The bank’s CRP
should fully document the results of that analysis. Elements of this analysis should include
current and pro forma balance sheets, current and long-term budgets, a strategic plan for the
bank, the market analysis used to derive the appropriate means to raise capital, and any other
relevant information. The CRP should clearly detail the assumptions used in the analysis.

The CRP must address the following:

- The steps the bank will take to become adequately capitalized.
- The levels of capital to be attained during each year of the plan.
- The types and levels of activities in which the bank will engage.
- How the bank will comply with the restrictions against asset growth (see 12 USC 1831o(e)
  (3)) and acquisitions, branching, and new lines of business (see 12 USC 1831o(e)(4)); and
- Any other information required by the OCC.

Capital plans required under 12 CFR 3, subpart J and subpart H do not automatically constitute
CRPs required under PCA. A capital plan submitted under 12 CFR 3 is not acceptable as a CRP
unless it addresses statutory requirements in 12 USC 1831o(e).

Guarantee of CRP by Controlling Company

The OCC cannot approve any CRP unless each company that controls the bank guarantees that
the bank will comply with the CRP. The purpose of the guarantee is for the controlling company
to provide a financial commitment; the controlling company must also provide appropriate
assurances of performance to the OCC that the company’s subsidiary bank will comply with the
CRP.

The company’s aggregate liability under the guarantee is limited to the lesser of the following:

- Five percent of the bank’s total assets at the time the bank became undercapitalized.
- The amount necessary to restore the capital of the bank to the applicable minimum capital
  levels as those levels were defined at the time the bank initially failed to comply with its
  CRP.

The guarantee and limit of liability expire after the OCC notifies the bank in writing that the bank
has remained adequately capitalized for four consecutive calendar quarters.
a guarantee given by a company or fulfillment of a guarantee given by a company in connection with one CRP does not relieve the company from an obligation to guarantee another CRP at a future date for the same bank if the bank again becomes undercapitalized. Fulfillment of one guarantee up to the statutory limit would not reduce the amount of any guarantee of a future CRP for the same bank. In addition, a new or revised guarantee is required if the bank is required to submit a new or revised CRP.

Each company controlling a given bank is jointly and severally liable for the amounts needed to recapitalize the bank. The OCC may direct the bank to seek payment of the full amount of the guarantee from any or all of the companies issuing the guarantee.

Content of Guarantee

In general, the guarantee should provide the controlling company’s financial commitment guaranteeing the bank’s compliance with the CRP. In addition, the guarantee may include assurances that the company will take actions required by the CRP, for example, (1) ensuring that competent management will be selected, (2) restricting transactions between the bank and the company, and (3) discontinuing certain risky or inappropriate bank or affiliate activities.

Depending on the company involved, other assurances of performance may be appropriate, such as a promissory note, a pledge of controlling company assets, legal opinions from controlling company counsel, or a controlling company board of director’s resolution.

Attached to this bulletin is a sample guarantee companies may use when guaranteeing CRPs to assure performance. The sample guarantee

- references the parties to the guarantee (the bank and the guarantor holding company(s)).
- incorporates by reference the CRP submitted for approval by the bank.
- provides that the holding company unconditionally guarantees and provides a financial commitment that the bank will comply with its CRP.
- provides that the holding company will (1) take any action directly required under the CRP; (2) take any corporate actions necessary to enable the bank to take actions required of the bank under the CRP; (3) not take any action that would impede the bank’s ability to implement its CRP; (4) ensure that the bank is staffed by competent management; and (5) restrict transactions between the holding company and the bank.
- states the limit of liability and the promise to pay the amount described.
- incorporates by reference a certified resolution of the board of directors of the holding company regarding the guarantee.
- describes the consideration provided, and certain rights of the parties.
- provides for the pledge of holding company assets, or other appropriate collateral, to secure the guarantee, when deemed appropriate.
- includes certain other provisions such as a statement on governing law.

The guarantee is patterned after a standard commercial guarantee. It requires the controlling company to perform on its guarantee when the bank notifies the company that the bank has failed to comply with its CRP. If the bank declines or delays in enforcing the guarantee, the OCC may take action directing the bank to enforce the guarantee or take any other action under 12 USC 1831o or 12 USC 1818 as may be appropriate. In the event the bank is placed in receivership, the FDIC as receiver would be entitled to the proceeds of any contribution by the controlling company.

Pledge of Controlling Company Assets

12 USC 1831o(e)(2)(C)(ii)(II) states each company having control over the bank must provide “appropriate assurances of performance” to satisfy the guarantee requirement. These assurances vary on a case-by-case basis depending on the bank’s condition and willingness to implement changes, the strength of the controlling company, and other relevant factors.

In the case of a cooperative, strong company controlling an undercapitalized bank, the OCC generally requires only a written guarantee from the company along with a copy of its audited financial statements.
In other cases, a pledge of certain non-banking assets may be required. For example, the OCC typically requires a financially weak company that controls an undercapitalized bank to pledge assets to secure its guarantee. Similarly, the OCC typically requires a company that controls a significantly or critically undercapitalized bank to pledge assets regardless of its financial strength. The OCC may also require a security agreement and a UCC-1 financing statement if a controlling company pledges assets to secure the guarantee.

In addition, if the pledged assets are not of a type that a bank can legally hold, to the extent permissible under applicable law, the pledge agreement and other relevant documents will not prevent or inhibit the bank from liquidating such assets following contribution of those assets to the bank.

The need for a pledge also depends on the organizational structure of the controlling company. In a multi-tiered company structure, each controlling company is jointly and severally liable for implementation of the bank’s CRP. So, for the bank’s CRP to be acceptable, each company must guarantee the CRP and provide adequate assurances of performance. Intermediate shell holding companies may, however, rely on the financial resources of the parent company or of a third party as adequate assurance of performance on the guarantee.

In the case of a controlling shell company or a company that has limited resources, a guarantee is required for the bank’s CRP to be acceptable. Given the company’s lack of resources, however, a pledge of assets is not generally required. Instead, the OCC evaluates the CRP on the same basis that it evaluates plans submitted by banks owned by individuals. If the OCC would approve a CRP submitted by a bank owned by an individual, it will approve a similar CRP submitted by a bank owned by a shell company.

OCC Review of CRP and Controlling Company Guarantees

The OCC does not accept a CRP unless the plan contains the information required by statute, is based on realistic assumptions, is likely to succeed in restoring the bank’s capital, and will not increase the risk to the bank. In addition, the OCC does not accept a CRP that is not guaranteed by the company or companies that control the bank.

The OCC determines, on a case by case basis, the adequacy of guarantees and assurances of performance by the bank’s controlling company. The OCC supervisory office may consult with the Board of Governors of the Federal Reserve System or appropriate Federal Reserve Bank to discuss provisions of the guarantee. The OCC may also consult with the FDIC on the terms of the guarantee to ensure that the FDIC’s interest as receiver would be protected if the bank is later placed in receivership. The OCC may also request that the bank and the controlling company obtain a legal opinion from the bank’s or company’s counsel that the guarantee and any pledge of assets securing such guarantee, if applicable, constitute a legally binding commitment against the company that is given in the ordinary course of business for adequate consideration.

The OCC generally must notify the bank in writing of the CRP’s approval within 60 days of receipt or must notify the bank in writing of the delay and the reason for the delay. The OCC supervisory office must submit a copy of each approved CRP to the FDIC’s regional office within 45 days of approval.

Assessment of Grounds for Appointment of Receiver or Conservator

In reviewing the bank’s CRP, the OCC also assesses the bank’s viability, including an assessment of whether grounds exist for the appointment of a receiver. The OCC may appoint the FDIC receiver if one or more of these grounds exists:

- The bank’s assets are less than its obligations to its creditors and others, including members of the bank.
- There is substantial dissipation of assets or earnings due to
  - any violation of any statute or regulation, or
  - any unsafe or unsound practice.
- The bank is in an unsafe or unsound condition to conduct business.
- There is willful violation of a final order to cease and desist.
• There is any concealment of the bank's books, papers, records, or assets, or any refusal to submit the bank's books, papers, records, or affairs for inspection to any examiner or to any lawful agent of the OCC.

• The bank is likely to be unable to pay its obligations or meet its depositors' demands in the normal course of business.

• The bank has incurred or is likely to incur losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the bank to become adequately capitalized without federal assistance.

• There is any violation of law or regulation, or any unsafe or unsound practice or condition that is likely to
  • cause insolvency or substantial dissipation of assets or earnings;
  • weaken the bank's condition; or
  • otherwise seriously prejudice the interests of the bank's depositors or the Deposit Insurance Fund.

• The bank, by resolution of its board of directors or its shareholders or members, consents to the appointment.

• The bank has ceased being an insured institution.

• The bank is undercapitalized and
  • has no reasonable prospects of becoming adequately capitalized;
  • has failed to become adequately capitalized when required to do so;
  • has failed to submit an acceptable CRP within the time prescribed; or
  • has materially failed to implement an accepted CRP.

• The bank is critically undercapitalized or otherwise has substantially insufficient capital.

• The Attorney General notifies the OCC or FDIC in writing that the bank has been found guilty of a criminal offense under 18 USC 1956, 18 USC 1957, 31 USC 5322, or 31 USC 5324.

• A national bank's board of directors has fewer than five members.

A bank that meets one or more of these grounds may not be viable.

PCA Directives

The OCC imposes the discretionary actions applicable to undercapitalized, significantly undercapitalized, and critically undercapitalized banks by issuing a PCA directive. Refer also to PPM 5310-3, "Bank Enforcement Actions and Related Matters," for the OCC's enforcement action procedures, including procedures applicable to issuing a PCA directive.

A PCA directive is enforceable as a final order in federal district court in the same manner and to the same extent as a final cease-and-desist order. Also, civil money penalties may be assessed for violation of a PCA directive.

Further Information

Please contact Michael Brickman, Deputy Comptroller for Special Supervision, at (202) 649-6450.

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Related Links

• PPM 5310-3, "Bank Enforcement Actions and Related Matters" (PDF)
Although this issuance uses the term "bank" to include insured federal branches, the OCC recognizes that some of the prescribed measures and applicable restrictions may not be practical or appropriate in dealing with insured federal branches. The OCC intends to apply to insured federal branches as many of the PCA measures and restrictions as practical and appropriate, given the unique characteristics of federal branches and the individual circumstances in any given case. When appropriate, PCA directives taken against insured federal branches will be comparable to those taken against insured national banks or FSAs.

Refer to 12 USC 1831o(a)(1).

Refer to the "Capital and Dividends" booklet of the Comptroller's Handbook for more information.

The minimum requirements in 12 CFR 3 align with the definition of "adequately capitalized" in 12 CFR 6.4.

"Written agreement" means those agreements that are considered formal enforcement actions. Refer to PPM 5310-3, "Bank Enforcement Actions and Related Matters," for more information.

This includes agreements, orders, or directives issued by the OCC or the former Office of Thrift Supervision pursuant to section 8 of the FDI Act, the International Lending Supervision Act of 1983 (12 USC 3907), the Home Owners' Loan Act (12 USC 1464(l)(6)(A) (ii)), or section 38 of the FDI Act, or any regulation thereunder.

Refer to 12 CFR 6.6.

"ALLL" as used in this bulletin should also be interpreted to mean the allowance for credit losses upon implementation of the current expected credit losses (CECL) model.

Refer to 12 CFR 6.3(c).

Refer to 12 CFR 19.221 (national banks) and 12 CFR 165.8 (FSAs).

Refer to 12 USC 1818(b)(8).

Refer to the "Supervision Review Committees" section of PPM 5310-3, "Bank Enforcement Actions and Related Matters," for more information.

Refer to 12 CFR 19.221(b) (national banks) and 12 CFR 165.8(a)(2) (FSAs).

Refer to 12 CFR 19.221(f) (national banks) and 12 CFR 165.8(a)(6) (FSAs).

Refer to 12 CFR 6.1(e).

Refer to 12 USC 1831f, 12 CFR 303.243 and 337.8. Deposit rate restrictions prevent a bank that is not well capitalized from circumventing the prohibition on brokered deposits by offering rates significantly above market in order to attract a large volume of deposits quickly. As a general rule, a bank that is not well capitalized may not offer deposit rates more than 75 basis points above average national rates for deposits of similar size and maturity. Refer to FDIC FIL-42-2016, "Frequently Asked Questions on Identifying, Accepting and Reporting Brokered Deposits," for more information.

Refer to 12 USC 1821(a)(1)(D).

Refer to 12 USC 371b-2 and 12 CFR 206.

Refer to 12 USC 1817(b)(1)(C) and 12 CFR 327.

Refer to 12 USC 1831o(b)(2)(B).

Refer to 12 CFR 6.2. The definition of "management fee" does not include payments such as those for electronic data processing, trust activities, mortgage servicing, audit or accounting services, property management, or similar service fees.

Refer to 12 USC 1841.

Refer to 12 USC 1831o(e)(4)(B).

Refer to 12 USC 1831o(e)(4)(A).

Banks may have additional obligations under 12 CFR 359, "Golden Parachute and Indemnification Payments." Requesting approval for paying a bonus or increasing compensation of a senior executive officer for PCA purposes does not fulfill the bank's obligations under 12 CFR 359.

Refer to 12 USC 1831o(f)(2).

For more information regarding receivership or conservatorship grounds, refer to 12 USC 1821(c)(5) (national banks and FSAs), 12 USC 191 and 203 (national banks) and 12 USC 1464(d)(2) (FSAs).
29 Separate notice and OCC review may be required under 12 CFR 5.51. Refer to the “Changes in Directors and Senior Executive Officers” booklet of the Comptroller's Licensing Manual for more information.

30 Refer to 12 USC 1831o(f)(6).

31 Refer to 12 USC 1831o(f)(2)(H) and (I)(ii)-(iii).

32 Refer to 12 USC 1831o(i)(2).

33 Refer to 12 USC 1831o(e)(2).

34 Refer to 12 CFR 6.5(i)(1)(ii).

35 Refer to 12 USC 1821(c)(5) (national banks and FSAs), 12 USC 191 (national banks), and 12 USC 1464(d)(2) (FSAs).

36 Refer to 12 USC 71a (national banks). There is no equivalent statutory provision for FSAs.