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DEPARTMENT OF TREASURY
Office of the Comptroller of the Currency
12 CFR Part 4
[Docket ID OCC-2016-0001]
RIN 1557-AE01

FEDERAL RESERVE SYSTEM
12 CFR Parts 208 and 211
[Docket No. R-1531]
RIN 7100-AE45

FEDERAL DEPOSIT INSURANCE CORPORATION
12 CFR Parts 337, 347, and 390
RIN 3064-AE42

Expanded Examination Cycle for Certain Small Insured Depository Institutions and U.S. Branches and Agencies of Foreign Banks

AGENCY: Office of the Comptroller of the Currency (OCC), Treasury; Board of Governors of the Federal Reserve System (Board); and Federal Deposit Insurance Corporation (FDIC).

ACTION: Joint final rules.

SUMMARY: The OCC, Board, and FDIC (collectively, the agencies) are jointly adopting as final and without change the agencies' interim final rules published in the *Federal Register* on February 29, 2016, that implemented section 83001 of the Fixing America's Surface Transportation Act (FAST Act). Section 83001 of the FAST Act permits the agencies to conduct a full-scope, on-site examination of qualifying insured depository institutions with less than \$1 billion in total assets no less than once during each 18-month period. Prior to enactment of the FAST Act, only qualifying insured depository institutions with less than \$500 million in total assets were eligible for an 18-month on-site examination cycle. The final rules, like the interim final rules, generally allow well capitalized and well managed institutions with less than \$1 billion in total assets to benefit from the extended 18-month examination schedule. In addition, the final rules adopt as final parallel changes to the agencies' regulations governing the on-site

examination cycle for U.S. branches and agencies of foreign banks, consistent with the International Banking Act of 1978. Finally, through this rulemaking, the FDIC has integrated its regulations regarding the frequency of safety and soundness examinations for State nonmember banks and State savings associations.

DATES: Effective on [INSERT DATE 30 DAYS FROM DATE OF PUBLICATION IN FEDERAL REGISTER].

FOR FURTHER INFORMATION CONTACT:

OCC: Deborah Katz, Assistant Director, or Melissa J. Lisenbee, Attorney, Legislative and Regulatory Activities Division, (202) 649-5490; Scott Schainost, Midsize and Community Bank Supervision Liaison, Midsize and Community Bank Supervision, (202) 649-8173.

Board: Division of Banking Supervision and Regulation—Richard Naylor, Associate Director, (202) 728-5854; Richard Watkins, Deputy Associate Director, (202) 452-3421; Virginia Gibbs, Manager, (202) 452-2521; or Alexander Kobulsky, Supervisory Financial Analyst, (202) 452-2031; and Legal Division—Laurie Schaffer, Associate General Counsel, (202) 452-2277; Brian Chernoff, Senior Attorney, (202) 452-2952; or Mary Watkins, Attorney, (202) 452-3722.

FDIC: Thomas F. Lyons, Chief, Policy and Program Development, (202) 898-6850, Karen Jones Currie, Senior Examination Specialist, (202) 898-3981 for the Division of Risk Management Supervision; Mark A. Mellon, Counsel, (202) 898-3884 for revisions to 12 CFR part 337; Rodney D. Ray, Counsel, (202) 898-3556 for revisions to 12 CFR part 347; Suzanne J. Dawley, Senior Attorney, (202) 898-6509 for revisions to 12 CFR part 390 for the Legal Division.

SUPPLEMENTARY INFORMATION:

I. Background

Section 10(d) of the Federal Deposit Insurance Act (FDI Act)¹ generally requires the appropriate Federal banking agency for an insured depository institution (IDI) to conduct a full-scope, on-site examination of the institution at least once during each 12-month period. Prior to enactment of section 83001 of the FAST Act,² section 10(d)(4) of the FDI Act authorized the appropriate Federal banking agency to extend the on-site examination cycle for an IDI to at least once during an 18-month period if the IDI (1) had total assets of less than \$500 million; (2) was well capitalized (as defined in 12 U.S.C.1831o); (3) was found, at its most recent examination, to be well managed³ and to have a composite condition of “outstanding” or, in the case of an institution that has total assets of not more than \$100 million, “outstanding” or “good;” (4) was not subject to a formal enforcement proceeding or order by the FDIC or its appropriate Federal banking agency; and (5) had not undergone a change in control during the previous 12-month period in which a full-scope, on-site examination otherwise would have been required. Section 10(d)(10) of the FDI Act, prior to the enactment of section 83001 of the FAST Act, also gave the agencies discretionary authority to raise the eligibility size limit for the 18-month examination cycle for otherwise qualifying IDIs with an “outstanding” or “good” composite rating from \$100 million to an amount not to exceed \$500 million in total assets if the agencies determined that the

¹ 12 U.S.C. 1820(d). Section 10(d) of the FDI Act was added by section 111 of the Federal Deposit Insurance Corporation Improvement Act of 1991.

² Pub. L. 114-94, 129 Stat. 1312 (2015).

³ Depository institutions are evaluated under the Uniform Financial Institutions Rating System (commonly referred to as “CAMELS”). CAMELS is an acronym that is drawn from the first letters of the individual components of the rating system: Capital adequacy, Asset quality, Management, Earnings, Liquidity, and Sensitivity to market risk. CAMELS ratings of “1” and “2” correspond with ratings of “outstanding” and “good.” In addition to having a CAMELS composite rating of “1” or “2,” an IDI is considered to be “well managed” for the purposes of section 10(d) of the FDI Act only if the IDI also received a rating of “1” or “2” for the management component of the CAMELS rating at its most recent examination. See 72 FR 17798 (Apr. 10, 2007).

higher limit would be consistent with the principles of safety and soundness.⁴ Under section 10(d)(3), the Board and the FDIC, as the appropriate Federal banking agencies for State-chartered insured banks and savings associations, are permitted to conduct on-site examinations of such IDIs on alternating 12-month or 18-month periods with the institution's State supervisor, if the Board or FDIC, as appropriate, determines that the alternating examination conducted by the State carries out the purposes of section 10(d) of the FDI Act.⁵

Section 7(c)(1)(C) of the International Banking Act (IBA) provides that a Federal or a State branch or agency of a foreign bank shall be subject to on-site examination by its appropriate Federal banking agency or State bank supervisor as frequently as a national or State bank would be subject to such an examination by the agency.⁶ The agencies previously adopted regulations to implement the examination cycle requirements of section 10(d) of the FDI Act and section 7(c)(1)(C) of the IBA, including the extended 18-month examination cycle available to qualifying small institutions and U.S. branches and agencies of foreign banks.⁷ The agencies have also exercised their discretion, under section 10(d)(10) of the FDI Act, to extend the 18-month examination cycle for otherwise qualifying institutions with "good" composite ratings,⁸ first, in 1997, for such institutions with total assets of \$250 million or less, and, again, in 2007, for such institutions with total assets of \$500 million or less.⁹

Section 83001 of the FAST Act, effective on December 4, 2015, amended section 10(d) of the FDI Act to raise, from \$500 million to \$1 billion, the total asset threshold below which an

⁴ 12 U.S.C. 1820(d)(10).

⁵ 12 U.S.C. 1820(d)(3).

⁶ 12 U.S.C. 3105(c)(1)(C).

⁷ See 12 CFR 4.6 and 4.7 (OCC), 12 CFR 208.64 and 211.26 (Board), 12 CFR 337.12, 347.211, and 390.351 (FDIC).

⁸ Corresponding to a CAMELS or Risk management, Operational controls, Compliance, and Asset quality (ROCA) rating of "2."

⁹ See 62 FR 6449 (Feb. 12, 1997) (interim final rule); see also 63 FR 16377 (Apr. 2, 1998) (final rule); see also 72 FR 17798 (Apr. 10, 2007) (interim final rule); see also 72 FR 54347 (Sept. 25, 2007) (final rule).

agency may apply an 18-month (rather than a 12-month) on-site examination cycle for IDIs with “outstanding” composite ratings, and to raise, from not more than \$100 million to not more than \$200 million, the total asset threshold below which an agency may apply an 18-month examination cycle to an institution with an “outstanding” or “good” composite rating.¹⁰ Section 83001 also amended section 10(d)(10) of the FDI Act to authorize the appropriate Federal banking agency to increase, by regulation, the maximum amount limitation for IDIs with “outstanding” or “good” composite ratings from not more than \$200 million to not more than \$1 billion if the appropriate Federal banking agency determines that the higher amount would be consistent with the principles of safety and soundness for IDIs.¹¹

These FAST Act amendments reduce regulatory burdens on small, well capitalized, and well managed institutions and allow the agencies to better focus their supervisory resources on those IDIs and U.S. branches and agencies of foreign banks that may present capital, managerial, or other issues of supervisory concern.

II. Discussion of the Final Rules

On February 29, 2016, the agencies published and requested comment on interim final rules to implement the amendments to section 10(d) made by section 83001 of the FAST Act.¹² The agencies are adopting the interim final rules as final without change. In particular, the agencies are adopting as final the increase, from \$500 million to \$1 billion, in the total asset threshold below which an IDI that meets the criteria in section 10(d) and the agencies’ rules may qualify for an 18-month, full-scope, on-site examination cycle. In addition, as authorized by section 83001 of the FAST Act, the agencies have determined that it is consistent with principles

¹⁰ Pub. L. 114-94, 129 Stat. 1312 (2015).

¹¹ *Id.*

¹² 81 FR 10063 (Feb. 29, 2016).

of safety and soundness to permit institutions with total assets of \$200 million or greater and not exceeding \$1 billion that received a composite CAMELS rating of “1” or “2,” and that meet other qualifying criteria set forth in section 10(d) and the agencies’ rules, to qualify for an 18-month examination cycle. Consistent with section 7(c)(1)(C) of the IBA, the agencies also are adopting as final conforming changes to the regulations that govern the on-site examination cycle of a U.S. branch or agency of a foreign bank. These changes permit a U.S. branch or agency of a foreign bank with total assets of less than \$1 billion to qualify for an 18-month examination cycle if the U.S. branch or agency of a foreign bank received a composite ROCA rating of “1” or “2” at its most recent examination and meets the other applicable criteria.

The FDIC analyzed the frequency with which institutions rated a composite CAMELS rating of “1” or “2” failed within five years, versus the frequency with which institutions rated a composite CAMELS rating of “3,” “4,” or “5” failed within five years. FDIC analysis indicates that between 1985 and 2011,¹³ FDIC-insured depository institutions with assets less than \$1 billion and a composite CAMELS rating of “1” or “2” had a five-year failure rate that was one-seventh as high as institutions with a CAMELS rating of “3,” “4,” or “5.” Moreover, the relationship between failure rates in the two ratings groups did not meaningfully change when the analysis was restricted to institutions with assets between \$200 million and \$500 million compared to institutions with assets between \$500 million to \$1 billion. This analysis suggests that extending the examination cycle for well-rated institutions with \$500 million to \$1 billion in assets by an additional six months, combined with the agencies’ off-site monitoring activities and ability to examine an institution more frequently as necessary or appropriate, is unlikely to negatively affect the safe and sound operations of qualifying institutions or the ability of the

¹³ A list of failed institutions can be found on the FDIC’s Web site at <https://www.fdic.gov/bank/individual/failed/banklist.html>.

agencies to effectively supervise and protect the safety and soundness of institutions with total assets of less than \$1 billion.¹⁴ Furthermore, the agencies note that, in order to qualify for an 18-month examination cycle, any institution with total assets of less than \$1 billion—including one with a CAMELS composite rating of “2”—must meet the other capital, managerial, and supervisory criteria set forth in section 10(d). The agencies estimate that the changes adopted by the final rules will increase the number of institutions that may qualify for an extended 18-month examination cycle by approximately 611 institutions (372 of which are supervised by the FDIC, 142 by the OCC, and 97 by the Board), bringing the total number of institutions that may qualify for an extended 18-month examination cycle to 4,793 IDIs.¹⁵ Approximately 89 U.S. branches and agencies of foreign banks would be eligible for the extended examination cycle based on the final rules, an increase of 30 (one of which is supervised by the FDIC, four by the OCC, and 25 by the Board).¹⁶

Finally, the FDIC is adopting as final changes made in the interim final rules to integrate its regulations regarding the frequency of safety and soundness examinations for State nonmember banks and State savings associations. Twelve CFR 390.351 was rescinded and removed because it was substantively identical to 12 CFR 337.12 and, therefore, redundant to section 12 CFR 337.12. Twelve CFR 337.12 was amended to reflect the authority of the FDIC under section 4(a) of the Home Owners’ Loan Act to provide for the examination and safe and sound operation of State savings associations. State savings associations now are within the

¹⁴ The agencies continue to reserve the right in their regulations to examine an IDI or U.S. branch or agency of a foreign bank more frequently than is required by the FDI Act or IBA. See 12 CFR 4.6(c) and 4.7(c) (OCC), 12 CFR 208.64(c) and 211.26(c)(3) (Board), 12 CFR 337.12(c), 347.211(c) (FDIC), and 390.351(c).

¹⁵ Call report data, March 31, 2016.

¹⁶ Id.

scope of 12 CFR 337.12, and, all FDIC-supervised institutions, including State savings associations, are subject to the requirements of 12 CFR 337.12.

The agencies received three comment letters in response to the interim final rules. Two commenters, both industry trade groups, supported the interim final rules. Both commenters agreed that extending the examination cycle for IDIs that meet the interim final rules' criteria would not negatively affect the safe and sound operations of the institutions or the ability of the agencies to supervise them. The third commenter, an individual, did not support the interim final rules, but offered no specific reasons for that opposition.

For the reasons described in this section, the agencies are adopting these rules as final without change.

Effective Date

The Administrative Procedure Act (APA) generally requires that a final rule be published in the Federal Register no less than 30 days before its effective date.¹⁷ Therefore, the final rules will become effective on [INSERT DATE 30 DAYS FROM DATE OF PUBLICATION IN FEDERAL REGISTER]. The interim final rules will continue to be in effect until the final rules become effective.

Section 302 of the Riegle Community Development and Regulatory Improvement Act of 1994 (RCDRIA) requires that each Federal banking agency, in determining the effective date and administrative compliance requirements for new regulations that impose additional reporting, disclosures, or other requirements on IDIs, consider, consistent with principles of safety and soundness and the public interest, any administrative burdens that such regulations would place on depository institutions, including small depository institutions, and customers of depository

¹⁷ 5 U.S.C. 553(d).

institutions, as well as the benefits of such regulations.¹⁸ Further, new regulations that impose additional reporting, disclosures, or other new requirements on IDIs generally must take effect on the first day of a calendar quarter that begins on or after the date on which the regulations are published in final form.¹⁹ The final rules adopt the interim final rules without change. The RCDRIA does not apply to the final rules because the rules do not impose any additional reporting, disclosures, or other new requirements on IDIs.

III. Regulatory Analysis

A. Plain Language

Section 722 of the Gramm-Leach-Bliley Act²⁰ requires the Federal banking agencies to use plain language in all proposed and final rules published after January 1, 2000. The agencies' staff believe the final rules are presented in a clear and straightforward manner and having received no comments on how to make the interim final rules easier to understand, the agencies adopt the final rules without change.

B. Regulatory Flexibility Act

Board: Regulatory Flexibility Act²¹ (RFA) requires an agency to prepare a final regulatory flexibility analysis (FRFA) when an agency promulgates a final rule, unless pursuant to section 605(b) of the RFA, the agency certifies that the final rule will not, if promulgated, have a significant economic impact on a substantial number of small entities. In this context, small entities include banking entities with total assets less than or equal to \$550 million.

The final rules do not have a significant impact on a substantial number of small entities. Like the interim final rules, the final rules expand the number of institutions eligible for an

¹⁸ 12 U.S.C. 4802(a).

¹⁹ 12 U.S.C. 4802(b).

²⁰ Pub. L. 106-102, section 722, 113 Stat. 1338, 1471 (1999).

²¹ 5 U.S.C. 601 *et seq.*

extended examination cycle, thus reducing the regulatory burden associated with on-site examinations for these institutions. Further, only 22 of the 122 Board-regulated institutions affected by the final rules have assets between \$500 million and \$550 million and thus would be considered small entities. These 22 institutions represent a small percentage (3.3 percent) of the 657 Board-supervised institutions with total assets less than \$550 million.²² For these reasons, the Board certifies that the final rules will not have a significant impact on a substantial number of small entities as defined in the RFA,²³ and therefore, a regulatory flexibility analysis is not required.

FDIC: The RFA²⁴ requires an agency, in connection with a notice of final rulemaking, to prepare a FRFA analysis describing the impact of the rule on small entities (defined by the Small Business Administration for the purposes of the RFA to include banking entities with total assets of \$550 million or less) or to certify that the final rule will not have a significant economic impact on a substantial number of small entities.

The final rule does not impose any significant economic impact on a substantial number of small entities. The final rule raises the asset eligibility threshold for extended examination cycles from \$500 million to \$1 billion, expanding the number of qualifying institutions and U.S. branches and agencies of foreign banks, and reduces the regulatory burden associated with on-site examinations. Of the 372 FDIC-supervised institutions that could be impacted by the rule, only 71 of the FDIC-supervised institutions have total assets between \$500 million and \$550 million which is a very small share (2.5 percent) of the 2,817 FDIC-supervised institutions with

²² Call report data, March 31, 2016.

²³ 5 U.S.C. 601 *et seq.*

²⁴ *Id.*

total assets less than \$550 million.²⁵ For this reason, the FDIC certifies that the final rule will not have a significant economic impact on a substantial number of small entities as defined in the RFA, and therefore, a regulatory flexibility analysis is not required.

OCC: The RFA applies only to rules for which an agency publishes a general notice of proposed rulemaking pursuant to 5 U.S.C. 553(b). Consistent with section 553(b)(B) of the APA, the agencies determined for good cause that general notice and opportunity for public comment were not necessary and issued an interim final rule rather than a proposed rule. Accordingly, the RFA's requirements relating to initial and final regulatory flexibility analyses do not apply.

C. Paperwork Reduction Act

The Paperwork Reduction Act of 1995²⁶ states that no agency may conduct or sponsor, nor is the respondent required to respond to, an information collection unless it displays a currently valid Office of Management and Budget (OMB) control number. Because the final rules do not create a new, or revise an existing collection of information, no information collection submission needs to be made to OMB.

D. The Economic Growth and Regulatory Paperwork Reduction Act

Under section 2222 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA),²⁷ the agencies are required to conduct a review at least once every 10 years to identify any outdated or otherwise unnecessary regulations. The agencies completed the last comprehensive review of their regulations under EGRPRA in 2006 and are currently conducting

²⁵ Call report data, March 31, 2016.

²⁶ 44 U.S.C. 3501-3521.

²⁷ Pub. L. 104-208, 110 Stat. 3309 (1996).

the next decennial review. The burden reduction evidenced in these final rules is consistent with the objectives of the EGRPRA review process.

Authority and Issuance

For the reasons set forth in the joint preamble, the interim rule published on February 29, 2016 at 81 FR 10063, is adopted as final without change.

Dated: October 19, 2016

Thomas J. Curry,
Comptroller of the Currency.

BILLING CODE: 4810-33-P

Board of Governors of the Federal Reserve System, December 6, 2016

Robert deV. Frierson,
Secretary of the Board.

BILLING CODE: 6210-01-P

Dated at Washington, D.C., this 19th day of October, 2016.
By order of the Board of Directors.
Federal Deposit Insurance Corporation.

Robert E. Feldman,
Executive Secretary.

BILLING CODE: 6714-01-P

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