



[Docket ID OCC-2026-0562]

## Uniform Financial Institutions Rating System

**AGENCY:** Federal Financial Institutions Examination Council.

**ACTION:** Notice and request for comment.

**SUMMARY:** The Federal Financial Institutions Examination Council (FFIEC) is requesting comment on proposed revisions to the Uniform Financial Institutions Rating System (UFIRS), commonly referred to as the CAMELS rating system. The proposal would strengthen the link between CAMELS ratings and a financial institution’s safety and soundness by focusing component and composite ratings on factors that materially affect an institution’s financial condition and risk profile, and by improving the transparency of CAMELS ratings.

**DATES:** Comments must be received by **[INSERT DATE 90 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

**ADDRESSES:** Commenters are encouraged to submit comments through the Federal eRulemaking Portal. Please use the title “Uniform Financial Institutions Rating System” to facilitate the organization and distribution of the comments. You may submit comments by any of the following methods:

- Federal eRulemaking Portal— Regulations.gov: Go to <https://regulations.gov/>. Enter Docket ID OCC-2026-0562 in the Search Box and click “Search.” Public comments can be submitted via the “Comment” box below the displayed document information or by clicking on the document title and then clicking the “Comment” box on the top-left side of the screen. For help with submitting effective comments please click on “Commenter’s Checklist.” For assistance with the Regulations.gov site, please

call 1-866-498-2945 (toll free) Monday-Friday, 9 a.m.-5 p.m. ET, or email [regulationshelpdesk@gsa.gov](mailto:regulationshelpdesk@gsa.gov).

- Mail: Executive Secretary, Federal Financial Institutions Examination Council, L. William Seidman Center, Mailstop: E-2035-c, 3501 Fairfax Drive, Arlington, VA 22226-3550.

- Hand Delivery/Courier: Executive Secretary, Federal Financial Institutions Examination Council, L. William Seidman Center, Mailstop: E-2035-c, 3501 Fairfax Drive, Arlington, VA 22226-3550.

Instructions: You must include “FFIEC” as the agency name and Docket ID OCC-2026-0562 in your comment. In general, all comments received will be entered into the docket and published on the Regulations.gov website without change, including any business or personal information provided such as name and address information, email addresses, or phone numbers. Comments received, including attachments and other supporting materials, are part of the public record and subject to public disclosure. Do not include any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure.

You may review comments and other related materials that pertain to this action by the following method:

- Viewing Comments Electronically— Regulations.gov: Go to <https://regulations.gov/>. Enter Docket ID OCC-2026-0562 in the Search Box and click “Search.” Click on the “Documents” tab and then the document’s title. After clicking the document’s title, click the “Document Comments” tab. Comments can be viewed and filtered by clicking on the “Sort By” drop-down on the right side of the screen or the “Refine Results” options on the left side of the screen. Supporting materials can be viewed by clicking on the “Documents” tab. Click on the “Sort By” drop-down on the

right side of the screen or the “Refine Documents Results” options on the left side of the screen checking the “Supporting & Related Material” checkbox. For assistance with the Regulations.gov site, please call 1–866– 498–2945 (toll free) Monday–Friday, 9 a.m.–5 p.m. ET, or email [regulationshelpdesk@gsa.gov](mailto:regulationshelpdesk@gsa.gov). The docket may be viewed after the close of the comment period in the same manner as during the comment period.

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## **SUPPLEMENTARY INFORMATION:**

### **I. Introduction**

The Federal Financial Institutions Examination Council Act of 1978 (“FFIEC Act”) authorizes the FFIEC<sup>1</sup> to prescribe principles and standards for the federal examination of financial institutions and to make recommendations to promote consistency and coordination in the supervision of institutions.<sup>2</sup> Pursuant to this authority, the FFIEC developed and recommended adoption of the UFIRS in 1979.<sup>3</sup> The UFIRS is a comprehensive supervisory rating system used by Federal and State supervisory agencies (together, “supervisory agencies”) for evaluating the safety and

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<sup>1</sup> The agencies represented on the FFIEC are the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC), and the Consumer Financial Protection Bureau (CFPB), plus a State Liaison Committee (SLC) representing state agencies. The SLC consists of five representatives from state regulatory agencies that supervise financial institutions. The representatives are appointed for two-year terms. The SLC Chairman, a voting member of the Council, is elected by the SLC members for a one-year term and can be re-elected for additional terms. The functions of the Council include establishing principles and standards, making recommendations regarding supervisory matters and adequacy of supervisory tools, and developing a uniform reporting system.

<sup>2</sup> 12 U.S.C. § 3301 *et seq.*

<sup>3</sup> See Circular No. 79-191 (Nov. 29, 1979) “Uniform Rating System,” available at [https://fraser.stlouisfed.org/files/docs/historical/frbdal/circulars/frbdallas\\_circ\\_19791129\\_no79-191.pdf](https://fraser.stlouisfed.org/files/docs/historical/frbdal/circulars/frbdallas_circ_19791129_no79-191.pdf).

soundness of financial institutions<sup>4</sup> on a uniform basis and for identifying those institutions requiring special attention or concern.<sup>5</sup> The supervisory agencies use the UFIRS to, among other purposes, monitor the severity of problems that financial institutions may be experiencing, determine the level of supervisory concern that is warranted, and monitor aggregate trends in the condition of financial institutions.

The 1979 UFIRS established a uniform framework to evaluate a financial institution's financial condition, compliance with laws and regulations, and overall operating soundness.<sup>6</sup> In 1996, the FFIEC revised the UFIRS to, among other changes, include a sixth component rating addressing sensitivity to market risks, place greater emphasis on risk management practices, and require examiners to consider an institution's size, complexity, and risk profile when evaluating each component rating.<sup>7</sup>

Under the current UFIRS, each financial institution is assigned CAMELS component and composite ratings on a scale of 1 to 5, with 1 being the highest rating. The composite rating is assigned based on an evaluation and rating of six essential components of an institution's financial condition and operations: Capital Adequacy, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk. The ratings assigned under UFIRS can have several implications for financial institutions.<sup>8</sup>

Given the importance of the UFIRS framework and the many changes that have

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<sup>4</sup> The term "financial institution" as used in this "Supplementary Information" section refers to those insured depository institutions whose primary Federal supervisory agency is represented on the FFIEC and includes Federally supervised commercial banks, savings and loan associations, mutual savings banks, and credit unions. Federal and State supervisory agencies may choose to adopt the UFIRS when evaluating other types of supervised organizations.

<sup>5</sup> Because the CFPB does not examine the institutions it supervises for safety and soundness, the CFPB does not use the UFIRS.

<sup>6</sup> See Circular No. 79-191 (Nov. 29, 1979) "Uniform Rating System," at 1, available at [https://fraser.stlouisfed.org/files/docs/historical/frbdal/circulars/frbdallas\\_circ\\_19791129\\_no79-191.pdf](https://fraser.stlouisfed.org/files/docs/historical/frbdal/circulars/frbdallas_circ_19791129_no79-191.pdf)

<sup>7</sup> See 61 FR 37472 (July 18, 1996) and 61 FR 67021 (Dec. 19, 1996).

<sup>8</sup> For example, under the BHC Act and the National Bank Act, a financial institution's UFIRS composite and Management component ratings are relevant to its "well managed" status, which may, among other benefits, allow the institution to engage in certain expansionary activities without prior approval from regulators. See 12 U.S.C. 1841(o)(9), 12 U.S.C. 24a(g)(6).

occurred in the banking industry and in supervisory practices since the rating system was updated in 1996, the FFIEC conducted a review of the framework to inform the proposed changes. The review considered a wide body of relevant academic literature, which indicates that CAMELS ratings contain important information about the overall condition of financial institutions, including information that is not readily available from balance sheet metrics or other publicly available materials. For a specific discussion of some of the literature, see Section IV. Expected Effects. The FFIEC review also considered existing industry commentary related to the application of CAMELS ratings. An observation from industry is that the Management rating has been overweighted relative to other CAMELS components in determining the composite rating. The supervisory agencies analyzed CAMELS ratings from 2000 to 2025 and found that while composite and component ratings generally move together, their correlation can vary significantly over time. The supervisory agencies' analysis suggested that the Management component has been the most influential factor in determining composite ratings, particularly in recent years.

## **II. Proposed Changes to the UFIRS**

Following the FFIEC's review of the UFIRS framework, the agencies are proposing to retain the basic framework of the existing rating system, with certain modifications to the composite and component rating definitions and evaluation factors. Specifically, the proposed revisions would emphasize factors that materially affect an institution's financial condition and risk profile. The proposal would emphasize consideration of material financial risks over concerns related to policies, procedures, and documentation, thus helping to ensure that ratings accurately reflect the issues most likely to impact safety and soundness. The proposed changes would also improve transparency by more clearly articulating expectations for financial institutions. These updates would improve the effectiveness of the UFIRS as a supervisory tool and increase the public's

confidence in supervisors' assessment of the banking system. Additionally, certain of the proposed changes would also be responsive to comments received from the Economic Growth and Regulatory Paperwork Reduction Act public notices and public outreach meetings.<sup>9</sup>

This section summarizes the proposed changes to the UFIRS. The text of the proposed UFIRS can be found in Appendix A of this Supplementary Information.

*A. Remove "Special Consideration" Given to the Management Rating in the Composite Rating*

The current UFIRS framework states that the Management component is given "special consideration" when assigning a composite rating. The proposal would remove the sentence directing examiners to give "special consideration" to the Management component in the composite rating.

Although the effectiveness of a financial institution's board of directors and management is an important aspect of its overall safety and soundness, the current language could be interpreted as diminishing the relative importance of the non-Management components in the determination of composite ratings. Removing the "special consideration" given to the Management component in assigning composite ratings would ensure that supervisors take a more balanced approach that appropriately considers all component ratings. This would result in a composite rating that better reflects a financial institution's overall financial condition and risk profile.

*B. Changes to the Management Component Rating*

The FFIEC proposes to make several changes to the Management component's

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<sup>9</sup> Pub. L. 104–208, Div. A, Title II, section 2222, 110 Stat. 3009–414, (1996) (codified at 12 U.S.C. 3311). See also Regulatory Publication and Review Under the Economic Growth and Regulatory Paperwork Reduction Act of 1996, 89 FR 99,751 (Dec. 11, 2024).

evaluation factors and rating definitions. The proposed changes to the evaluation factors limit the Management component's evaluation factors to the most material aspects of risk management, helping to strengthen the link between supervisory ratings and safety and soundness. Specifically, the proposal would remove factors related to: "Management depth and succession," "Responsiveness to recommendations from auditors and supervisory authorities," and "Demonstrated willingness to serve the legitimate banking needs of the community," to focus on the most material aspects of risk management. The factor related to the overall performance of the institution and its risk profile would be removed to limit redundancy, since it would be addressed through the composite and other component ratings.

The proposed changes to the Management component rating definitions include establishing a material financial risk threshold for assigning Management ratings of 3 or worse based on risk management weaknesses. Institutions would generally receive such ratings only when risk management practices result in material financial risk to the institution. Institutions that have unreliable financial or regulatory reporting, have failed to safeguard assets, or are in significant noncompliance with law or regulation may also be assigned a Management component rating of 3 or worse. These proposed revisions would better align the severity of Management ratings with the risk to the institution's safety and soundness.

### *C. Treatment of Specialty Review Findings*

Under the current UFIRS framework, supervisory findings from specialty reviews<sup>10</sup> are often incorporated into the Management component rating and can contribute to ratings downgrades even when they do not reflect material financial risks to

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<sup>10</sup> Specialty review areas include Compliance (e.g., Consumer Compliance, Bank Secrecy Act/Anti-Money Laundering), Community Reinvestment, Government Security Dealers, Information Systems, Municipal Security Dealers, Transfer Agent, and Trust.

the institution. The proposal would clarify that these specialty review findings would influence the CAMELS composite and component ratings to the extent that the findings impact a financial institution's overall financial condition, represent material financial risks, or reflect significant noncompliance with laws and regulations. The proposed changes to the influence of specialty review findings would promote component and composite ratings that better reflect material financial risks.

#### *D. Revisions to Composite Rating Definitions*

The current UFIRS framework includes a definition for composite ratings 1 through 5 to provide supervisors with specific considerations that should drive the determination of a financial institution's composite rating. The proposal would make changes to composite rating definitions to align with the broader approach of ensuring that the UFIRS focuses on an institution's financial condition and risk profile, with emphasis on material financial risks. Specifically, the proposal would revise the composite 1 and 2 definitions to clarify that financial institutions with these ratings have strong or satisfactory financial performance, respectively, and only minor or moderate risk management weakness. The proposal would change the composite 3 definition to state that financial institutions that receive this rating should exhibit less than satisfactory financial performance or inadequate risk management practices that result in material financial risk to the institution. Institutions that exhibit significant noncompliance with laws and regulations may also be assigned a 3 rating. The proposal would also change the definition of a composite rating of 4 to state that financial institutions that receive this rating should exhibit "deficient" financial performance. Risk management weaknesses that do not result in observable deterioration of financial condition or material financial risk would not alone support a composite rating of 4 or worse. Finally, the proposal would state that firms rated a composite 5 should exhibit critically deficient financial performance. By establishing clearer thresholds for these ratings, the proposal would

help ensure that ratings of 3 or worse are more fully supported by evidence of weaknesses that materially impact the safety and soundness of the institution.

#### *E. Clarifying Language on Risk Management*

Under the current UFIRS framework, the component descriptions and evaluation factors include broad language regarding the “ability of management to identify, measure, monitor, and control” risks. The proposal would remove broad language within Capital Adequacy, Asset Quality, Earnings, Liquidity and Sensitivity to Market Risk components and, where appropriate, would focus on more specific risk management factors relevant to an assessment of a given component. For example, the proposal would replace the Liquidity component’s evaluation factor referencing the “capability of management to properly identify, measure, monitor, and control the institution’s liquidity position, including the effectiveness of funds management strategies, liquidity policies, management information systems, and contingency funding plans,” to instead consider “the effectiveness of funds management practices, including contingency funding plans and cash flow forecasting.” Similarly, the proposal would replace the Capital Adequacy component’s evaluation factor concerning “the ability of management to address emerging needs for additional capital” to instead include consideration of “the institution’s effectiveness in maintaining capital levels commensurate with its risk profile and strategic priorities through a range of economic conditions.”<sup>11</sup> The Management component’s description would continue to reference the effectiveness of the board of directors and management, in their respective roles, to identify, measure, monitor, and control material financial risks associated with an institution’s activities; however, the

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<sup>11</sup> The proposal would similarly specify risk management practices in the asset quality component rating (the “effectiveness of risk monitoring practices and timely collection of problem assets”); the earnings component rating (the “effectiveness of budgeting and income and expense forecasting”); and the sensitivity to market risk component rating (the “adequacy of market risk measurement and control practices given the institution’s scale and activities”).

Management component's evaluation factors would also be revised in the proposed framework to enhance specificity and measurability.

The effectiveness of a financial institution's risk management is an important aspect of its overall safety and soundness and its supervisory ratings. Increasing the specificity of component evaluation factors related to risk management would help to ensure that risk management factors that are most impactful to financial condition and risk profile are accurately reflected in the CAMELS ratings. The proposed changes would also clarify for financial institutions what specific risk management practices are relevant to each component, thereby increasing transparency.

#### *F. Clarifying Evaluation Factors*

The current UFIRS framework states that component ratings will be based on "but not limited to" an assessment of a specific set of evaluation factors unique to each component. The proposed framework would remove the "but not limited to" language from all of the CAMELS components' descriptions and replace it with a general paragraph, applicable to all components, that would allow for additional evaluation factors to be considered only if warranted by exceptional circumstances or evolving business practices. Under the proposal, the consideration of additional evaluation factors must be critical to the assessment of an institution's financial condition or risk profile with emphasis on material financial risks. The proposal sets an explicit expectation that examiners would document and explain the rationale for inclusion of such additional factors. This proposed revision would provide greater certainty to and transparency around the rating evaluation factors that would be considered in the assessment.

The proposal would also modify certain evaluation factors to improve clarity around the scope of supervisory evaluations. For example, the proposal would revise the Capital Adequacy component to clarify that risks related to contingent liabilities would

be considered in the evaluation factors. The proposal would also revise the Earnings component's evaluation factors to clarify that a financial institution's funding costs and earnings exposure to commodity prices would be considered. Additionally, the proposal would amend the Sensitivity to Market Risk component to explicitly include an evaluation of recent net interest income performance in response to the interest rate environment, expectations for net interest income based on the balance sheet position, and exposure to interest rate volatility. More clearly defining the CAMELS components' evaluation factors would help to further standardize evaluations and better ensure that examiners and financial institutions prioritize issues that materially affect an institution's financial condition and risk profile. The proposed revisions would also improve the transparency of the UFIRS by establishing clearer expectations for financial institutions with respect to the specific evaluation factors that influence ratings and examination outcomes.

#### *G. Improving Consistency, Structure, and Approach to Ratings Definitions*

The current framework includes a description of the ratings, 1 through 5, for each component; however, they differ in language, structure, and level of detail. The proposal would introduce more consistent terminology and a more streamlined structure, focusing on the financial condition and risk management aspects of the CAMELS component rating definitions, where applicable. For example, the proposal would use the terms "strong," "satisfactory," "less than satisfactory," "deficient," and "critically deficient" to describe financial condition. For descriptions of risk management practices, the proposal would use the terms "effective," "adequate," "inadequate," and "deficient." Specific descriptions of risk management practices would be removed from the 5 ratings for all but the Management component. These proposed changes would introduce more consistent terminology and structure to these descriptions to better articulate the degree of deterioration in financial condition and/or risk management practices required to support

a given composite or component rating. Such changes would also improve transparency of the framework by establishing clearer expectations for financial institutions.

#### *H. Modernizing and Conforming Framework Language*

The FFIEC proposes to modernize and conform language throughout the framework and to update terminology to reflect current industry standards and accounting practices. For example, references to “allowances for loan and lease losses” (ALLL) would be replaced with “allowances for credit losses” (ACL) to conform with the Current Expected Credit Losses (CECL) accounting standard adopted under U.S. GAAP in 2023. The proposal would also remove all references to reputation risk, consistent with the policies of the Board, OCC, FDIC, and NCUA.<sup>12</sup>

Modernizing and conforming the framework’s language would improve clarity, precision, and accessibility for institutions of all sizes, facilitating more effective risk management and supervisory communication.

### **III. Request for Comments**

The FFIEC requests comment on the proposed changes to the rating system. In addition, the FFIEC invites comments on the following questions:

- 1. To what extent would the proposed revisions enhance the effectiveness of UFIRS as a supervisory tool for evaluating the safety and soundness of financial institutions? Should the framework be modified to further strengthen the link between supervisory ratings and safety and soundness, and if so, how?*
- 2. To what extent do the proposed revisions appropriately balance consideration of an institution’s financial condition and risk profile when assigning ratings? Should*

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<sup>12</sup> The Board, OCC, FDIC and NCUA recently issued proposals or final rules to remove the consideration of reputation risk from their supervisory frameworks; *See* 91 FR 9499 (February 26, 2026); 91 FR 18279 (April 10, 2026); 90 FR 48409 (October 21, 2025).

*the CAMELS composite or component rating definitions and/or evaluation factors be adjusted in other ways to balance consideration of financial condition and risk profile when evaluating an institution's safety and soundness? If so, how?*

*3. To what extent should the agencies consider "evolving business practices" in determining additional evaluation factors that are critical to an assessment of an institution's financial condition or risk profile with emphasis on material financial risks? What should the agencies consider as "evolving business practices"?*

*4. How should compliance with laws and regulations be considered within the composite and component ratings? To what extent is the proposal's consideration of compliance with laws and regulations in the composite and Management component ratings appropriately calibrated? What are the advantages and disadvantages of differentiating between issues that present material financial risks and those that do not? To what extent should the UFIRS framework account for the type, severity, frequency, and/or management's role with respect to a violation of law or regulation and/or the violation's connection to material financial risk?*

*5. The proposal limits inclusion of specialty review findings in the UFIRS framework to those that impact an institution's overall financial condition or pose material financial risk. What threshold of findings should warrant specialty review findings to be included in the component and composite ratings? To what extent should specialty review findings specifically influence the Management rating?*

*6. In addition to the proposed changes to rating evaluation factors and definitions, to what extent should the framework set the expectation that an institution's composite rating bears a close relationship with the CAMELS component ratings, with no single component rating driving the composite rating? What are the advantages and disadvantages of the framework setting forth the explicit expectation that if one component rating is driving the composite rating, additional justification is needed?*

7. *To what extent should the framework set the expectation that the Management rating reflects the institution's management and overall financial condition and material financial risk, and therefore it should be rare, and additional justification would be needed for Management to be rated less than satisfactory when all other components are satisfactory? What would be the advantages and disadvantages of setting such an expectation?*
8. *To what extent should the Management component's evaluation factors directly consider whether compensation is excessive? What would be the advantages and disadvantages of limiting the evaluation factor to the avoidance of self-dealing and conflicts of interest? What other factors, if any, should be considered that address misaligned incentives and principal-agent risks?*
9. *To what extent should the Management component's evaluation factors consider whether directors and management are affected by, or susceptible to, dominant influence or concentration of authority?*
10. *Do proposed framework changes to the Management component rating effectively limit consideration of a single finding when assigning multiple ratings? To what extent could inclusion of compliance with laws and regulations within the Management rating result in the redundant consideration of a single noncompliance issue?*
11. *To what extent does the additional specificity in the rating definitions and evaluation factors for the Sensitivity to Market Risk rating improve clarity of supervisory expectations? Are there ways to further refine the evaluation factors and ratings definitions to better reflect how interest rates, foreign exchange rates, commodity prices, or other financial instrument prices can affect a financial institution's earnings or capital?*

#### **IV. Expected Effects**

If adopted, the proposal would require the supervisory agencies to implement the proposed revisions described above into the process for assigning CAMELS ratings. The following sections discuss qualitatively some benefits and costs of the proposal, relative to a baseline in which the UFIRS framework that is currently applied to institutions under the supervision of the agencies remains unchanged.

#### *A. Benefits to Institutions*

The proposal, if adopted, would pose two types of benefits to supervised institutions: (1) more efficient use of management time and resources, and (2) more transparency in supervisory expectations of institutions. The expected benefits of the proposed revisions derive, in part, from focusing supervision on factors that materially impact an institution's financial condition and risk profile. This should support financial institutions in addressing their material risks in a more efficient and effective manner relative to the baseline, potentially enhancing their safety and soundness and contributing to the safety and soundness of the banking system overall. The proposed framework's reduced focus on process-related issues that do not pose material financial risk and narrowing of the deficiencies within the scope of the Management criteria, may allow institutions to reallocate resources.

Further, under the proposed framework, financial institutions with strong financial metrics and risk profiles would likely be issued satisfactory CAMELS ratings. Research suggests that CAMELS ratings significantly affect lending behavior and bank performance, after attempting to control for some other factors, with downgraded banks exhibiting substantially lower loan growth (Kupiec et al., 2017).<sup>13</sup> During the financial crisis, small banks that experienced ratings downgrades expanded commercial and

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<sup>13</sup> Paul Kupiec, Yan Lee and Claire Rosenfeld, "Does Bank Supervision Impact Bank Loan Growth?" *Journal of Financial Stability*, Vol. 28, pp. 29-48 (2017).

industrial loans and commercial real estate loans less than banks maintaining healthy ratings (Kiser et al., 2016).<sup>14</sup> To the extent that ratings downgrades owing to process-related issues that are immaterial to an institution's financial condition have historically constrained financial institutions' willingness or ability to engage in expansionary activities including lending, the new framework could support increased credit availability. Also, an overemphasis on process-related immaterial issues could have allowed material financial risks to not be appropriately reflected in the ratings under the current framework.

Additionally, the proposed changes would provide clearer supervisory expectations for financial institutions, potentially reducing compliance costs and uncertainty while maintaining desired supervisory outcomes. Institutions devote significant time and effort to meeting the expectations of supervisors. Ratings function through three key channels: as a communication tool conveying supervisory assessments, as a direct risk mitigant through regulatory restrictions, and as a broad incentive mechanism affecting bank behavior (Bergin & Stiroh, 2021).<sup>15</sup> If expectations and guideposts are unclear, a financial institution's cost of compliance may rise as it attempts to understand the factors on which ratings will be based. Research comparing supervisory and market assessments of bank performance highlights the distinct value that clear supervisory ratings provide to financial institution management in understanding the true financial condition of the institution (Berger et al., 1998).<sup>16</sup> The proposed framework seeks to provide clearer expectations and stronger signals around

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<sup>14</sup> Elizabeth K. Kiser, Robin A. Prager, and Jason R. Scott, "Supervisory Ratings and the Contraction of Bank Lending to Small Businesses." Federal Reserve Board Finance and Economics Discussion Series (2012).

<sup>15</sup> James Bergin and Kevin Stiroh, "Why Do Supervisors Rate Banking Organizations?" Economic Policy Review, Vol 27(3) (2021).

<sup>16</sup> Allen N. Berger, Sally M. Davies, and Mark J. Flannery, "Comparing Market and Supervisory Assessments of Bank Performance: Who Knows What When?" (1998), <https://ssrn.com/abstract=121651>.

supervisory ratings, which could help lower compliance costs without reducing the efficacy of the supervisory process.

### *B. Costs to Institutions*

Because the proposed framework would shift the focus toward factors that materially affect an institution's financial condition and risk profile, there could be potential costs if the shift generates unintended consequences. For instance, a financial institution's management may deprioritize certain risk management practices if those practices are not drivers of CAMELS ratings or perceived to be directly linked to material financial risk. To the extent that the proposal, if adopted, delayed the remediation of a risk that subsequently becomes material to the financial condition of the institution, such institutions could incur higher costs to deal with the risk and could also incur losses. Long-term, effective control of material financial risks requires sustained investment and improvement in risk management systems.

Although unlikely, revisions to the set of evaluation factors and ratings definitions may diminish the information content of ratings or miscalibrate ratings outcomes, potentially putting the financial condition of institutions at risk of future deterioration, thereby also potentially increasing the risk of loss to institutions. Although the agencies expect that the intended reform to the CAMELS rating system will improve outcomes, research suggests that the current formulation of supervisory ratings has been more informative about bank failure than balance sheet metrics alone (Correia et al., 2025)<sup>17</sup> and thus contains important information about the financial condition of depository institutions. However, as previously discussed, the agencies believe that the proposed changes to the framework will strengthen the link between ratings and safety and

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<sup>17</sup> Ricardo Correia, Stephan Luck, and Emil Verner, "Failing Banks" *The Quarterly Journal of Economics*. Vol. 141(1), pp. 147-204 (2026).

soundness. As such, the agencies expect the costs discussed above would be modest and believe that the benefits of the proposed revisions justify the potential costs.

## V. Regulatory Analysis

In the interest of full and fair participation of the public, and in order to give the public an opportunity to comment on the proposal, the FFIEC is publishing this proposed recommendation for notice and comment.

### *A. Plain Language*

Section 722 of the Gramm-Leach-Bliley Act requires the Federal banking agencies<sup>18</sup> to use plain language in all proposed and final rules published after January 1, 2000.<sup>19</sup> Although this proposed recommendation is not a rule, the Federal banking agencies, under the auspices of the FFIEC, have sought to present the proposed recommendation in a simple and straightforward manner and invite comment on the use of plain language. For example:

- Have the Federal banking agencies organized the material to suit your needs? If not, how could they present the proposed recommendation more clearly?
- Are the requirements in the proposed recommendation clearly stated? If not, how could the proposed recommendation be more clearly stated?
- Does the proposed recommendation contain technical language or jargon that is not clear? If so, which language requires clarification?
- Would a different format (grouping and order of sections, use of headings, paragraphing) make the proposed recommendation easier to understand? If so, what changes would achieve that?

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<sup>18</sup> See 12 U.S.C. 4809(c) (cross-referencing “Federal banking agency” as defined in 12 U.S.C. 1813); 12 U.S.C. 1813 (defining “Federal banking agency” as the OCC, the Board, and the FDIC).

<sup>19</sup> Pub. L. 106-102, sec. 722, 113 Stat. 1338, 1471 (1999), 12 U.S.C. 4809.

- Would more, but shorter, sections be better? If so, which sections should be changed?
- What other changes can the Federal banking agencies incorporate to make the proposed recommendation easier to understand?

### *B. Paperwork Reduction Act*

In accordance with the Paperwork Reduction Act (PRA),<sup>20</sup> the agencies may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid Office of Management and Budget (OMB) control number. This proposed recommendation would not involve any new, or revise any existing, collections of information pursuant to the PRA. Consequently, no information will be submitted to the OMB for review.

### *C. Regulatory Flexibility Act*

The Regulatory Flexibility Act (RFA) generally requires an agency, in connection with a proposed rule, to prepare and make available for public comment an initial regulatory flexibility analysis that describes the impact of the proposed rule on small entities.<sup>21</sup> This requirement applies to any rule for which the agency publishes a general notice of proposed rulemaking pursuant to section 553 of Title 5.<sup>22</sup> Although the RFA does not apply to this proposed recommendation, the relevant agencies have undertaken a preliminary analysis. The agencies do not believe that this proposed recommendation would have a significant economic impact on a substantial number of small entities. The proposed recommendation would not impose any obligations on supervised institutions and would not require supervised institutions to take any action in response.

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<sup>20</sup> 44 U.S.C. 3501 *et seq.*

<sup>21</sup> See 5 U.S.C. 553, 603, 604 and 605.

<sup>22</sup> 5 U.S.C. 601

#### *D. Unfunded Mandates Reform Act<sup>23</sup>*

The Unfunded Mandates Reform Act of 1995 (UMRA) generally requires an agency, in connection with any general notice of proposed rulemaking, to consider whether the proposed rule includes a Federal mandate that may result in the expenditure by State, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year (\$187 million as adjusted annually for inflation).<sup>24</sup> Pursuant to section 202 of the UMRA,<sup>25</sup> if a proposed rule meets this UMRA threshold, the agency would need to prepare a written statement that includes, among other things, a cost-benefit analysis of the proposal. Although the UMRA does not apply to this proposed recommendation, the OCC has undertaken a preliminary analysis. This proposed recommendation imposes no new mandates—and thus no direct costs—on supervised institutions. Accordingly, the proposed recommendation would not result in an expenditure of \$187 million or more annually by State, local, and tribal governments, or by the private sector.

#### *E. NCUA Analysis on Executive Order 13132 on Federalism<sup>26</sup>*

Executive Order 13132 encourages certain regulatory agencies to consider the impact of their actions on state and local interests. The NCUA, an agency as defined in 44 U.S.C. 3502(5), complies with the executive order to adhere to fundamental federalism principles. This proposed recommendation would apply to all federally insured credit unions, including state-chartered credit unions. This scope is set by statute. The NCUA works cooperatively with state regulatory agencies on all supervisory matters and will continue to do so. The NCUA expects that any effect on states or on the

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<sup>23</sup> The Unfunded Mandates Reform Act applies to the OCC and is not applicable to the other FFIEC agencies.

<sup>24</sup> 2 U.S.C. 1531 *et seq.*

<sup>25</sup> *Id.* at 1532.

<sup>26</sup> This applies to the NCUA and is not applicable to the other FFIEC agencies.

distribution of power and responsibilities among the various levels of government will be minor. The NCUA welcomes comments on ways to eliminate, or at least minimize, any potential impact in this area.

*F. NCUA Assessment of Federal Regulations and Policies on Families<sup>27</sup>*

The NCUA has determined that this proposed recommendation would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999. The proposed recommendation relates to supervision of federally insured credit unions, and any effect on family well-being is expected to be indirect.

*G. Executive Orders 12866 and 14192*

Executive Order 12866, as amended, directs agencies to assess the costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits.<sup>28</sup> This proposed recommendation was drafted and reviewed in alignment with Executive Order 12866. Within OMB, the Office of Information and Regulatory Affairs (OIRA) has determined that this proposed recommendation is a “significant regulatory action” under section 3(f) of Executive Order 12866. Accordingly, the draft proposed recommendation was submitted to OIRA for review. As noted in other sections of the SUPPLEMENTARY INFORMATION of this document, the agencies have assessed the costs and benefits of this proposed recommendation and have made a reasoned determination that the benefits of the proposed changes to the UFIRS framework justify the minimal costs on supervised institutions.

The proposed recommendation would streamline the UFIRS framework and

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<sup>27</sup> This applies to the NCUA and is not applicable to the other FFIEC agencies.

<sup>28</sup> E.O. 12866, 58 FR 51,735 (1993).

clarify the link between CAMELS ratings and safety and soundness by focusing component and composite ratings on factors that materially affect a financial institution's financial condition and risk profile. The agencies have experience in conducting examinations of the safety and soundness of supervised institutions, and supervised institutions have an existing mandate to operate in a safe and sound manner.

Executive Order 14192 further requires that new incremental costs associated with new regulations shall, to the extent permitted by law, be offset by the elimination of existing costs associated with at least ten prior regulations. The revisions to the framework, if finalized as proposed, are not expected to accrue any new incremental costs under Executive Order 14192.<sup>29</sup>

## **Appendix A: Proposed Text of the Uniform Financial Institutions Rating System**

### ***Uniform Financial Institutions Rating System***

The Uniform Financial Institutions Rating System (UFIRS) was adopted by the Federal Financial Institutions Examination Council (FFIEC)<sup>30</sup> on November 13, 1979, and updated on December 20, 1996.<sup>31</sup> Over the years, the UFIRS has generally proven to be an effective internal supervisory tool for evaluating the soundness of financial institutions<sup>32</sup> on a uniform basis and for identifying those institutions requiring special

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<sup>29</sup> E.O. 14192, 90 FR 9065 (2025).

<sup>30</sup> The agencies represented on the Federal Financial Institutions Examination Council (FFIEC) are the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Consumer Financial Protection Bureau. The chair of the State Liaison Committee serves as the sixth member of the Council.

<sup>31</sup> The 1996 revision to UFIRS included the addition of a sixth component addressing sensitivity to market risks, the explicit reference to the quality of risk management processes in the management component, and the identification of risk elements within the composite and component rating descriptions. The NCUA adopted the sixth component rating in 2021, which went into effect in 2022.

<sup>32</sup> For purposes of this rating system, the term "financial institution(s)" refers to those insured depository institutions whose primary Federal supervisory agency is represented on the FFIEC, and includes Federally supervised commercial banks, savings and loan associations, mutual savings banks, and credit unions.

attention or concern.<sup>33</sup>

The UFIRS evaluates the safety and soundness of a financial institution through an assessment of the institution's overall financial condition and its risk profile, with emphasis on material financial risks. The UFIRS considers the institution's financial condition, measured in terms of Capital Adequacy, Asset Quality, Earnings, Liquidity, and Sensitivity to Market Risk. The UFIRS also evaluates the effectiveness of an institution's risk management relative to its risk profile, including its ability to identify, measure, monitor, and control its risks.

The FFIEC has identified ways to further clarify the UFIRS system to strengthen the link between supervisory ratings and safety and soundness. Specifically, the revised UFIRS retains the basic framework of the existing rating system but emphasizes factors that materially affect an institution's financial condition and risk profile. These updates will improve the effectiveness of UFIRS as a supervisory tool and increase the public's confidence in supervisors' assessment of the banking system.

The UFIRS takes into consideration certain safety and soundness related factors that are common to all institutions. Under this system, the FFIEC member entities endeavor to ensure that all financial institutions are evaluated in a comprehensive and uniform manner, and that supervisory attention is appropriately focused on the financial institutions exhibiting material financial weaknesses or risks.

The UFIRS also serves as a useful vehicle for identifying problem or deteriorating financial institutions, as well as for categorizing institutions with deficiencies in particular component areas. Further, the rating system assists Congress in following safety and soundness trends and in assessing the aggregate strength and soundness of the

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<sup>33</sup> Because the CFPB does not examine the institutions it supervises for safety and soundness, the CFPB does not use the UFIRS.

financial industry. As such, the UFIRS assists the FFIEC member entities in fulfilling their collective mission of maintaining stability and public confidence in the nation's financial system.

### ***Overview***

Under the UFIRS, each financial institution is assigned a composite rating that measures its overall financial condition and risk profile, with emphasis on material financial risks. The composite rating is based on an evaluation and rating of six essential components of an institution's safety and soundness. These components are Capital Adequacy, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk. Evaluations of the components take into consideration the institution's size and sophistication, the nature and complexity of its activities, and its risk profile.

Composite and component ratings are assigned based on a 1 to 5 numerical scale. A 1 indicates the highest rating, the strongest performance and risk management practices, and the least degree of supervisory concern, while a 5 indicates the lowest rating, the weakest performance, and, therefore, the highest degree of supervisory concern.

The composite rating generally bears a close relationship to the component ratings assigned. Each component rating is based on a rigorous assessment of the evaluation factors comprising that component. In the revised framework, financial condition and material financial risks are the predominant considerations when making rating determinations. When assigning a composite rating, some components may be given more weight than others depending on the institution's overall financial condition and risk profile with emphasis on material financial risks. Assigned composite and component ratings are disclosed to the institution's board of directors and senior management.

Foreign Branch and specialty review findings and ratings are considered when assigning composite and component ratings under the UFIRS to the extent that they impact an institution's overall financial condition or pose material financial risk.<sup>34</sup> For institutions that primarily engage in trust activities (such as trust banks), Trust examination findings and ratings generally reflect the institution's overall financial condition or material financial risks, and examination conclusions are taken into consideration when assigning composite and component ratings under the UFIRS.

The following two sections of this document contain the composite rating definitions, and the descriptions and definitions for the six component ratings.

### ***Composite Ratings***

Composite ratings are based on a careful evaluation of an institution's financial condition and risk profile with emphasis on material financial risks. The six key components used to assess an institution are: Capital Adequacy, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk. The composite ratings are defined as follows:

#### **Composite 1**

Financial institutions in this group are sound in every respect and generally have components rated 1 or 2. These institutions exhibit strong financial performance. Risk management weaknesses are minor. These institutions are in substantial compliance with laws and regulations. As a result, these institutions give no cause for supervisory concern.

#### **Composite 2**

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<sup>34</sup> Specialty review areas include Compliance (for example, Consumer Compliance, Bank Secrecy Act/Anti-Money Laundering), Community Reinvestment, Government Security Dealers, Information Systems, Municipal Security Dealers, Transfer Agent, and Trust.

Financial institutions in this group are fundamentally sound and generally no component rating should be more severe than 3. These institutions exhibit satisfactory financial performance. Any risk management weaknesses are moderate and generally do not result in material financial risk to the institution. These institutions are in substantial compliance with laws and regulations. There are no material safety and soundness concerns and, as a result, the supervisory response is informal and limited.

### **Composite 3**

Financial institutions in this group exhibit some degree of supervisory concern and generally no component rating should be more severe than 4. These institutions exhibit less than satisfactory financial performance or inadequate risk management practices that result in material financial risk to the institution. There may be significant noncompliance with laws and regulations. These financial institutions require more than normal supervision, which may include formal or informal enforcement actions. Failure appears unlikely, however, given the overall strength and financial capacity of these institutions.

### **Composite 4**

Financial institutions in this group generally exhibit a significant degree of supervisory concern. These institutions exhibit deficient financial performance. Any risk management weaknesses range from severe to critically deficient. There may be significant noncompliance with laws and regulations that represents material financial risk. Close supervisory attention is required, which means, in most cases, formal enforcement action is necessary to address the problems. Institutions in this group pose a risk of loss to the Deposit Insurance Fund or Share Insurance Fund. Failure is a distinct possibility if the problems and weaknesses are not satisfactorily addressed and resolved.

### **Composite 5**

Financial institutions in this group exhibit the highest degree of supervisory concern. These institutions exhibit critically deficient financial performance. Immediate outside financial or other assistance is needed for the institution to be viable. Ongoing supervisory attention is necessary. Institutions in this group pose a significant risk of loss to the Deposit Insurance Fund or Share Insurance Fund, and failure is highly probable.

### ***Component Ratings***

Each of the component rating descriptions is divided into three sections: an introductory paragraph; a list of the evaluation factors that relate to that component; and a description of each numerical rating for that component. Generally, component ratings are determined by the specific evaluation factors listed in the following sections; however, exceptional circumstances or evolving business practices could give rise to additional evaluation factors that are critical to an assessment of an institution's financial condition or risk profile with emphasis on material financial risks. If any factor beyond those listed is considered when assigning a supervisory rating, examiners should document and explain the factor. The evaluation factors for each component rating are in no particular order of importance.

### ***Capital Adequacy***

The Capital Adequacy rating reflects a financial institution's ability to maintain sufficient capital to absorb unexpected losses from credit, market, and other risk exposures. An institution is expected to maintain capital commensurate with the nature and extent of risks to the institution. The types and quantity of risk in an institution's activities determine whether it may be appropriate to maintain capital at levels above required regulatory minimums to appropriately support on- and off-balance sheet exposures. Capital Adequacy is rated based on an assessment of the following evaluation factors:

- The level and quality of capital and the institution's overall financial condition.
- The institution's effectiveness in maintaining capital levels commensurate with its risk profile and strategic priorities through a range of economic conditions.
- The nature, trend, and volume of problem assets, and the adequacy of allowances for credit losses and other asset valuation allowances.
- Balance sheet composition, including the nature and amount of intangible assets, market risks, credit risks, concentration risks, and risks associated with other material activities.
- Risks posed by off-balance sheet activities and contingent liabilities.
- The quality and strength of earnings, and the reasonableness of capital distributions relative to the institution's financial condition and material financial risks.
- Access to other sources of capital, including capital markets and support provided by a sponsor, parent, or holding company.

**Ratings:**

1. A rating of 1 indicates a strong capital level relative to the institution's risk profile.
2. A rating of 2 indicates a satisfactory capital level relative to the institution's risk profile.
3. A rating of 3 indicates a less than satisfactory level of capital that does not fully support the institution's risk profile. The rating indicates a need for improvement, even if the institution's capital level exceeds minimum regulatory requirements.
4. A rating of 4 indicates a deficient level of capital. Viability of the institution may be threatened, but failure does not appear imminent. Assistance from shareholders or other external sources of financial support may be required.
5. A rating of 5 indicates a critically deficient level of capital such that the institution's

viability is threatened. Immediate assistance from shareholders or other external sources of financial support is required.

### *Asset Quality*

The Asset Quality rating reflects the quantity of existing and potential credit risks associated with a financial institution's loan and investment portfolios, foreclosed or repossessed assets, and other assets, as well as off-balance sheet exposures. The evaluation of asset quality includes the adequacy of allowances for credit losses and the exposure to obligor, issuer, borrower, or other counterparty defaults. Asset Quality is rated based on an assessment of the following evaluation factors:

- The effectiveness of credit underwriting and administration practices.
- The level, distribution, severity, and trend of problem, adversely classified, nonaccrual, restructured, modified, delinquent, and nonperforming assets for on- and off-balance sheet transactions.
- The adequacy of allowances for credit losses and other asset valuation allowances.
- The credit risk arising from or reduced by off-balance sheet transactions, such as unfunded commitments, unused lines of credit, and credit derivatives.
- The diversification and quality of the loan and investment portfolios.
- The financial risk arising from asset concentrations.
- The extent of securities underwriting activities and exposure to counterparties in trading activities.
- The adequacy of loan and investment policies and practices.
- The effectiveness of risk monitoring practices and timely collection of problem assets.

### **Ratings:**

1. A rating of 1 indicates strong asset quality and effective credit underwriting and administration practices. Any weaknesses are minor in nature and risk exposure is modest in relation to allowances for credit losses and capital protection. Asset quality in such institutions is of minimal supervisory concern.
2. A rating of 2 indicates satisfactory asset quality and adequate credit underwriting and administration practices. The level and severity of problem or adversely classified assets and any other weaknesses warrant a limited level of supervisory attention. Risk exposure is commensurate with allowances for credit losses and capital protection.
3. A rating of 3 indicates less than satisfactory asset quality or inadequate credit underwriting or administration practices. Trends may be stable or indicate deterioration in asset quality or an increase in risk exposure. The level and severity of problem or adversely classified assets, other weaknesses, and risks require an elevated level of supervisory attention.
4. A rating of 4 indicates deficient asset quality or credit underwriting or administration practices. The levels of risk and problem or adversely classified assets are significant, inadequately controlled, and subject the institution to potential losses that may threaten its viability.
5. A rating of 5 indicates critically deficient asset quality that presents an imminent threat to the institution's viability.

### ***Management***

The Management rating reflects the effectiveness of a financial institution's board of directors and management, in their respective roles, to identify, measure, monitor, and control the material financial risks associated with the institution's activities. Sound risk management practices are demonstrated through effective board of directors and senior management oversight; risk management policies, practices, and limits; audits, internal

controls, and recordkeeping; and risk monitoring and management information systems.

Management is rated based on an assessment of the following evaluation factors:

- The level and quality of oversight by the board of directors and management.
- The effectiveness of the board of directors and management, in their respective roles, to plan for and respond to risks that may arise from changing business conditions or the initiation of new activities or products.
- The effectiveness of controls addressing the operations and risks of significant activities.
- The accuracy, timeliness, and effectiveness of management information and risk monitoring systems.
- The adequacy of audits, internal controls, and recordkeeping to promote effective operations and reliable financial and regulatory reporting, safeguard assets, and ensure compliance with laws and regulations.
- Compliance with laws and regulations.
- The extent that directors and management are affected by, or susceptible to, dominant influence or concentration of authority.
- Avoidance of excessive compensation, self-dealing, and conflicts of interest.

**Ratings:**

1. A rating of 1 indicates strong risk management practices relative to the institution's size, complexity, and risk profile. All material financial risks are consistently and effectively identified, measured, monitored, and controlled.

2. A rating of 2 indicates satisfactory risk management practices relative to the institution's size, complexity, and risk profile. In general, material financial risks are adequately identified, measured, monitored, and controlled. Minor weaknesses may exist but are not material.

3. A rating of 3 indicates risk management practices including internal controls, audit, or recordkeeping, that are less than satisfactory, resulting in material financial risk to the institution. This rating also applies to institutions that have unreliable financial or regulatory reporting, have failed to safeguard assets, or are in significant noncompliance with law or regulation. The capabilities of management or the board of directors may be insufficient for the type, size, or condition of the institution.

4. A rating of 4 indicates deficient risk management practices, resulting in material financial risk to the institution. The level of problems and risk exposure is excessive. Immediate action is required to preserve the soundness of the institution. Replacing or strengthening management or the board may be necessary.

5. A rating of 5 indicates critically deficient risk management practices, resulting in material financial risk to the institution. Problems and significant risks now threaten the continued viability of the institution. Replacing or strengthening management or the board of directors is likely necessary.

### ***Earnings***

The Earnings rating reflects the quality, quantity, and trend of a financial institution's earnings. Earnings can be adversely affected by excessive or inadequately managed credit risk, which may result in loan losses and require additions to allowances for credit losses. Earnings can also be adversely affected by excessive market risk, which may unduly expose an institution's earnings to volatility in interest rates. The quality of earnings may be diminished by undue reliance on extraordinary gains, nonrecurring events, or favorable tax effects. In addition, future earnings can be adversely affected by high current or future funding and operating expenses relative to revenues, poorly executed business strategies, or other poorly managed risks. Earnings are rated based on an assessment of the following evaluation factors:

- The level of earnings, including trends and stability.
- The ability to provide for adequate capital through retained earnings.
- The quality and sources of earnings.
- The level of funding costs and noninterest expenses relative to the institution's business model.
- The effectiveness of budgeting and income and expense forecasting.
- The adequacy of provisions to maintain allowances for credit losses and other asset valuation allowances.
- The earnings exposure to market risk such as interest rate, foreign exchange, commodity price, or other financial instrument price risks.

**Ratings:**

1. A rating of 1 indicates strong earnings. Earnings are more than sufficient to support operations and maintain adequate capital and allowances for credit losses considering asset quality, growth, and other factors affecting the quality, quantity, and trend of earnings.

2. A rating of 2 indicates satisfactory earnings. Earnings are sufficient to support operations and maintain adequate capital and allowances for credit losses considering asset quality, growth, and other factors affecting the quality, quantity, and trend of earnings. Earnings that are relatively static, or experiencing a decline, may still receive a 2 rating.

3. A rating of 3 indicates less than satisfactory earnings. Earnings may not fully support operations or provide for the accretion of capital and allowances for credit losses in relation to the institution's overall condition, growth, and other factors affecting the quality, quantity, and trend of earnings.

4. A rating of 4 indicates deficient earnings. Earnings are insufficient to support

operations and maintain appropriate capital and allowances for credit losses. Institutions so rated may be characterized by erratic fluctuations in net income or net interest margin, the development of significant negative trends, nominal or unsustainable earnings, intermittent losses, or a substantive drop in earnings from prior years.

5. A rating of 5 indicates critically deficient earnings. A financial institution with earnings rated 5 is experiencing losses that represent a distinct threat to its viability through the erosion of capital.

### ***Liquidity***

The Liquidity rating reflects the current level and prospective sources of liquidity compared to funding needs. In general, funds management practices should ensure that a financial institution is able to maintain sufficient liquidity to meet its financial obligations in a timely manner. Practices should reflect the institution's ability to manage unplanned changes in funding sources, as well as react to changes in market conditions that affect the institution's ability to quickly liquidate assets with minimal loss. Liquidity should also be maintained at a reasonable cost and without undue reliance on funding sources that may not be available in the event of financial stress or adverse changes in market conditions. Contingency funding plans should enable an institution to effectively navigate funding shortfalls or stress events and include operationalized and confirmed access to reliable funds providers. Liquidity is rated based on an assessment of the following evaluation factors:

- The adequacy of liquidity sources compared to present and future needs, and the institution's ability to meet liquidity needs through a range of economic conditions without adversely affecting its operations or financial condition.
- The availability of assets that are readily convertible to cash without undue loss.
- Access to reliable external or contingent funding sources, particularly to address

potential liquidity shortfalls.

- The level of funding diversification or funding concentrations, both on- and off-balance sheet.
- The degree of reliance on short-term or less stable funding sources to fund longer-term assets.
- The trend and stability of deposits.<sup>35</sup>
- The ability to pledge, sell, or securitize assets.
- The effectiveness of funds management practices, including contingency funding plans and cash flow forecasting.

**Ratings:**

1. A rating of 1 indicates strong liquidity levels and effective funds management practices. The institution has reliable access to sufficient sources of funds on favorable terms to meet present, anticipated, and contingent liquidity needs. Any identified weaknesses in funds management practices are minor in nature.

2. A rating of 2 indicates satisfactory liquidity levels and adequate funds management practices. The institution has access to sufficient sources of funds on reasonable terms to meet present, anticipated, and contingent liquidity needs. Modest weaknesses may be evident in funds management practices.

3. A rating of 3 indicates less than satisfactory liquidity levels or inadequate funds management practices. Institutions rated 3 may lack ready access to funds on reasonable terms to meet present, anticipated, or contingent liquidity needs, or may evidence significant weaknesses in funds management practices.

4. A rating of 4 indicates deficient liquidity levels or funds management practices.

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<sup>35</sup> Deposits include credit union share accounts, if applicable.

Institutions rated 4 may not have or be able to obtain a sufficient volume of funds on reasonable terms to meet liquidity needs.

5. A rating of 5 indicates critically deficient liquidity levels that threaten the continued viability of the institution. Institutions rated 5 require immediate external financial assistance to meet maturing obligations or other liquidity needs.

### ***Sensitivity to Market Risk***

The Sensitivity to Market Risk rating reflects the degree to which changes in interest rates, foreign exchange rates, commodity prices, or other financial instrument prices can adversely affect a financial institution's earnings or capital. When evaluating this component, the primary consideration is the level, trend, measurement, and control of market risk relative to an institution's capital and earnings. For many institutions, the primary source of market risk arises from nontrading positions and their sensitivity to changes in interest rates. Foreign operations and trading activities can also be a significant source of market risk in some institutions. Sensitivity to Market Risk is rated based on an assessment of the following evaluation factors:

- The sensitivity of the institution's earnings or capital to adverse changes in interest rates, foreign exchange rates, commodity prices, or other financial instrument prices.
- Recent net interest income performance in response to the interest rate environment, and expectations for net interest income based on the balance sheet position and exposure to interest rate volatility.
- Measures of the long-term sensitivity of exposure to interest rate volatility on the institution's net economic value.
- The adequacy of market risk measurement and control practices given the institution's scale and activities.

- The degree to which assets, liabilities, and off-balance sheet exposures are appropriately aligned considering their potential impact on earnings and capital, as well as other risk mitigation strategies, such as hedging.
- The effectiveness of managing embedded options risk in assets and liabilities.
- The nature and complexity of interest rate risk exposure arising from nontrading positions.
- The nature and complexity of market risk exposure arising from foreign operations and trading activities.

**Ratings:**

1. A rating of 1 indicates that sensitivity to market risk is well controlled, and market risk management practices are effective. There is minimal potential that the earnings performance or capital position will be adversely affected by market risk.

2. A rating of 2 indicates that sensitivity to market risk is satisfactorily controlled, and market risk management practices are adequate. There is only moderate potential that the earnings performance or capital position will be adversely affected by market risk.

3. A rating of 3 indicates that control of market risk sensitivity is less than satisfactory or market risk management practices are inadequate. There is an elevated potential that the earnings performance or capital position will be adversely affected by market risk.

4. A rating of 4 indicates that control of market risk sensitivity or market risk management practices is deficient. There is high potential that the earnings performance or capital position will be adversely affected by market risk.

5. A rating of 5 indicates that control of market risk sensitivity is critically deficient and the level of market risk taken by the institution is an imminent threat to its viability.

Dated at Washington, DC, this 14 day of May 2026.

Federal Financial Institutions Examination Council.

**Amol B. Vaidya,**

*Executive Secretary.*

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