

EXAMINERS DO WALK IN WITH AN AGENDA

No doubt about it. They virtually have it in writing

* * *

Did you ever wonder if the examiners have an agenda when they walk into your bank?

Of course they do.

In fact, they have a pretty darn good idea what they are going to rate your bank before they ever walk in the door. Since the typical examination staff on the whole appears to be younger and less experienced these days, what incentive do they have to change the "pre-assigned" rating given to them by the Washington office?

The answer is—they don't.

Examination, in absentia

FDIC in particular loves the off-site monitoring program. If you want to know more about it, pick up the FDIC Case Manager Procedures Manual.

The manual indicates that there are three types of off-site monitoring conducted by the agency's Washington office.

First is the SCOR Report. This is the "Statistical CAMELS Off-site Rating" system. SCOR serves as a predictive index of whether the bank's component ratings and composite rating will be downgraded at the next examination.

So let's think about this for a minute.

The 27-year-old examiner with three years experience before he walks in the door of the bank receives a document from FDIC's Washington office that indicates the probability of a downgrade of this bank from a CAMELS 1 to a 5 is 95%. The probability of a downgrade of each of the CAMELS components, Capital, Assets, Management, Earnings, Liquidity and Sensitivity, is 90%, with the exception of Sensitivity, which is 80%.

What is a 27-year-old examiner going to do?

Spit in the eye of the Statistical CAMELS Off-site Rating? Hardly.

So if you think the examiners have an agenda when they walk in the door, they certainly do. If you want to agitate them, ask for them for a copy of the SCOR Report on your bank when they sit down with you before the start of the exam.

Beyond SCOR

This method is the most common, but the manual speaks of two others as well.

The Score-lag technique attempts to assess the condition of rapidly growing banks.

Since there are no such creatures these days, I suspect this one is probably not used terribly often.

The third technique, the "growth monitoring system," likewise, may be a bit rusty today. This system again deals with rapid growth and institutions dependent on non-core funding sources.

These monitoring systems do more than prepare the field examiners for visits. From the monitoring results, FDIC then creates an Off-site Review List. If you want to know why you may have received an interim change in your bank's CAMELS rating, it is because this Off-site Review List applies to any institution that has a CAMELS 1 or 2 that has been identified by one of the SCOR systems as having a 35% or higher probability of being downgraded to a 3 or worse.

We have had a number of our clients in the last four or five months that have received letters from FDIC indicating the bank had been downgraded in its CAMELS rating from the Off-site Review.

The deck seems stacked

So if you think your examiner had an agenda when he or she walked in the door, the bottom line is, he or she probably did.

Will they deviate from that agenda? Not likely.

There is no incentive for the 27-year-old- or 57-year-old examiner, for that matter-to deviate from the predictive index.

In fact, when our firm blew the whistle on the SCOR Report in connection with some administrative litigation a number of years ago, FDIC then conducted a study to determine whether the SCOR was a good predictive index of the results of the examination. FDIC wanted to know that if the SCOR report predicted that a bank would be downgraded, would the on-site examiner actually downgrade the bank.

Guess what?

The SCOR Report turned out to be an excellent predictive index. If the SCOR Report determined the bank should be downgraded, the examiner did too.

Big surprise.

Share your own recent examination experiences in the comments section below. The comment system will ask for your email address, but that will not be published.

About the Author

Jeff Gerrish is chairman of the board of Gerrish McCreary Smith Consultants, LLC, and a member of the Memphis-based law firm of Gerrish McCreary Smith, PC, Attorneys. He is a frequent contributor to ABA Banking Journal and ABA Bank Directors Briefing, and frequently speaks at ABA events and telephone briefings.

Gerrish formerly served as Regional Counsel for the Memphis Regional Office of the FDIC, with responsibility for all legal matters, including cease-and-desist and other enforcement actions. Before coming to Memphis, Gerrish was with the FDIC Liquidation Division in Washington, D.C. where he had nationwide responsibility for litigation against directors of failed banks.

Gerrish can be reached at jgerrish@gerrish.com, and the firm's website, www.gerrish.com.

You can get word about these columns the week they are posted by subscribing to ABA Banking Journal Report e-letter. It's free and takes only a minute to sign up for [Click here](#)