The Bank of Anytown illustrates the application of ROE instructions when presenting examination findings. The Bank of Anytown does not cover all possible examination circumstances and should not be used as boilerplate language. The Bank of Anytown is not intended to inhibit examiner judgment in situations that require other presentation methods due to unique situations.

BANK OF ANYTOWN

ANYTOWN **ANY COUNTY** **ANYSTATE**

Region:	Any Region	Certificate Number:	99999
Examiner-In-Charge:	Sandra E. Smart		
Examination Start Date:	August 01, 2016		
Examination As Of Date:	June 30, 2016		

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All dollar amounts are reported in thousands, unless otherwise indicated.

The following practices or financial conditions or operations require Board attention and corrective actions. The directorate's response to the items detailed on this Matters Requiring Board Attention (MRBA) page will be assessed by regulatory personnel prior to the next examination. Unsatisfactory conditions and practices identified during this examination, and recommendations from the previous examination that were not satisfactorily addressed, are described more fully throughout this Report of Examination (ROE).

MEMORANDUM OF UNDERSTANDING (MOU)

The MOU provisions relating to the Allowance for Loan and Lease Losses (ALLL), Call Reporting, and credit extensions to borrowers with charged-off loans remain outstanding. Failure to satisfactorily address the MOU provisions will likely impede progress in returning the bank to a satisfactory condition. The Board must put measures in place to ensure full compliance with all provisions of the MOU.

ALLOWANCE FOR LOAN AND LEASE LOSSES (ALLL)

The ALLL is underfunded by $325M due to elevated loan losses and deficiencies in the methodology for establishing the ALLL. If the Board does not correct deficiencies in the ALLL methodology, future ALLL provisions may be insufficient to protect the institution against potential loan losses and could negatively affect earnings and capital. The Board must establish a sound process for maintaining an appropriate ALLL.

INTERAGENCY GUIDELINES ESTABLISHING SAFETY AND SOUNDNESS STANDARDS

The institution is not in conformance with established safety and soundness standards in the areas of internal controls and information systems, internal audit system, loan documentation, credit underwriting, and asset quality. Failure to appropriately address these deficiencies and improve risk management practices may result in further deterioration in the bank's financial condition. In particular, the Board must ensure the following areas are corrected to improve overall risk management practices and prevent future financial deterioration:

- Asset Quality, Credit Administration, and Loan Underwriting: Inaccurately graded credits contributed to the inadequately funded ALLL. In addition, poor credit administration practices (relating to weak participation loan underwriting, the lack of construction loan inspections, and lack of on-going cash-flow analysis for commercial real estate loans) inhibit management's ability to make sound credit decisions, hamper collection efforts, and could lead to further loan losses. Also, procedures to identify and monitor asset concentrations are inadequate. Poor controls over concentrated asset positions can lead to disproportionately higher losses in the event of problems. The Board must ensure adequate resources are devoted to the loan review and credit administration functions and establish appropriate policies and procedures to identify and monitor concentrations.

- Internal Controls and Internal Audit: Internal controls have not been sufficient to provide for operations in compliance with rules and regulations. For example, the Board approved loans in apparent violation of the Federal Reserve Board's Regulation O and senior management purchased investments above its Board-approved investment authority. Moreover, the internal audit function lacks independence, as the internal auditor reports directly to the bank's president. Weak internal controls prevent the Board and management from adequately identifying, monitoring, and controlling risks, potentially exposing earnings and capital. The Board must ensure that appropriate controls and monitoring systems are in place and that management and bank staff conform to established policies.

STRATEGIC PLANNING

Despite the continued decline of the local fishing industry and the increase of local financial service providers, the bank's strategic plan does not adequately address regional economic conditions or local competition. Therefore, the plan may not provide management with adequate information to assess business opportunities or to adjust strategies and practices in light of changing conditions. The Board must review and update the strategic plan and ensure supporting data is current and comprehensive.

SUMMARY

The Board is reminded of the importance of addressing these weaknesses and its responsibility to respond appropriately to the matters highlighted above.

For additional details, including management's responses to these matters, refer to related comments included in this ROE.

Uniform Financial Institutions Rating System

	Current Exam	Prior Exam	Prior Exam
Examination Start Date	08/01/2016	11/13/2015 / S	10/21/2014
Examination As Of Date	06/30/2016	09/30/2015	09/30/2014
Composite Rating	**3**	**3**	**3**
Component Ratings:			
Capital	**3**	**2**	**2**
Asset Quality	**4**	**4**	**3**
Management	**3**	**3**	**3**
Earnings	**4**	**4**	**3**
Liquidity	**2**	**2**	**2**
Sensitivity to Market Risk	**2**	**2**	**2**
Information Technology	**2**	**1**	**2**
Trust	**2**	**2**	**2**
Compliance[1]	**2**		
Community Reinvestment Act[1]	**S**		

1 Examination dated xx/xx/xxxx

SUMMARY

This $80 million community bank is a locally owned, full-service commercial bank offering traditional deposit and credit products with particular focus on customers directly and indirectly reliant upon maritime-related businesses. The trade area is centered in a regional economic area heavily dependent upon a depressed fishing industry. The bank remains in less than satisfactory condition due to the lingering effects of poor risk selection and underwriting during an aggressive growth campaign in commercial real estate (CRE) and particularly acquisition development and construction (ADC) loans identified at the previous examination. Numerous workout credits and further deterioration in CRE due to poor credit administration have resulted in an underfunded ALLL and have negatively impacted earnings. Capital levels are less than satisfactory in relation to the present risk profile. Management needs to make additional efforts to comply with the outstanding Memorandum of Understanding (MOU). Information Technology, Trust, Bank Secrecy Act (BSA), and Anti-Money Laundering programs are satisfactorily managed. Compliance and Community Reinvestment Act programs are also satisfactory.

MEMORANDUM OF UNDERSTANDING

The bank entered into a MOU on January 21, 2015, based on the October 21, 2014, FDIC examination findings. Management and the Board have not fully addressed three MOU provisions, relating to the appropriateness of the Allowance for Loan and Lease Losses (ALLL), accuracy of the Reports of Condition and Income, and documentation for credit extensions to previously classified borrowers. Refer to the Compliance with Enforcement Actions page for additional details.

ASSET QUALITY - 4

Asset quality remains weak and is the primary impediment to improving the bank's overall financial condition. As reflected on the Examination Data and Ratios page, the volume of adversely classified items has decreased by 12 percent since the prior examination, with the volume of adversely classified loans dropping by 24 percent. Despite these improvements, adverse classifications still represent 84 percent of Tier 1 Capital and the ALLL. Additionally, the volume of Loss classifications increased from $194M at the 2014 examination to $1,015M at the current examination. (Asset Review Date: 6/30/2016.)

Loans

Examination classifications are centered in the commercial real estate (CRE) portfolio. Loans adversely classified Loss (portions of three relationships totaling $890M) are CRE loans that were adversely classified Substandard at the prior examination. Most troubled credits reflect liberal lending practices exacerbated by the depressed regional economy, particularly the local fishing industry. In response to past regulatory criticisms, management has taken affirmative steps to strengthen credit administration by tightening overall underwriting standards, strengthening collection efforts, decreasing CRE advance rates from 90 percent to 75 percent, and avoiding financing for speculative real estate acquisition and development projects. These actions have longer-term positive implications, but present credit quality remains hindered by numerous workout situations and the deterioration of existing credits not previously subject to adverse classification. Moreover, underwriting weaknesses are evident in participations purchased, and credit administration weaknesses were noted in the areas of construction loan inspections and cash-flow analysis. Additional details regarding trends in the level of adversely classified loans are included on the Analysis of Loans Subject to Adverse Classification page.

Loan Review and Internal Grading System

The institution's internal loan review and grading program is not producing timely or accurate information about the condition of the loan portfolio. Management has been unable to comply with internal review frequency standards due to elevated personnel demands associated with problem asset workouts. Assigned credit grades for several larger credits were inaccurate, as exemplified by examiner identification of the partial Loss classification of the Irma Deat, Ltd. and Last Chance Motel credits. In both cases, the credits were internally rated Substandard. Additionally, several credits adversely classified Substandard by examiners were internally rated Watch. The definitions being used by loan review and grading performed do not align with regulatory definitions. Failure to accurately grade credits on a timely basis has resulted in inadequate funding of the ALLL and may hinder management's ability to take appropriate and timely corrective action. To address this issue, management must provide adequate resources to this function.

President Allie C. Lincoln stated that management would add staff by year-end 2016, and meet review frequency standards by mid-2017.

Allowance for Loan and Lease Losses

The ALLL is inadequate by at least $325M, primarily due to inaccurate internal credit grading. Additionally, the ALLL allocation for non-watch list credits is inadequate based upon recent loan loss experience on non-watch list loans. Specifically, the institution's average loss rate on non-watch list loans since 2014 is 0.75 percent; however, management only allocates 0.1 percent for residential mortgages and 0.5 percent for all other non-watch list loans.

Institutions are expected to maintain an ALLL methodology in accordance with GAAP, which reflects consideration of the risk profile of the loan portfolio. Moreover, due to the deficiencies in the loan grading system, earnings and capital could be exposed should future loan and lease loss provisions prove inadequate. Management is directed to refer to the Interagency Policy Statement on the Allowance for Loans and Lease Losses for guidance to assist in correcting the deficiencies in the internal loan grading system and ALLL methodology. Refer to the Risk Management Assessment page for additional details.

President Lincoln indicated management intends to file amended June 30, 2016, Reports of Condition and Income to address reporting issues (see comments below) and will include a $325M loan loss provision in the amended filings. President Lincoln also initiated a review of the loan grading system during the examination and stated that all existing loss-rate percentages would be reviewed and updated to ensure full conformance with GAAP and supervisory guidance.

Credit Underwriting and Administration

Credit underwriting and administration, although improving, requires further attention. The Robert Rain LLC., credit is representative of deficiencies in the monitoring of construction loans and performing cash flow analysis; refer to the Items Listed as Special Mention for further details. As detailed on the Assets with Credit Data or Collateral Documentation Exceptions pages, the number of loans possessing potential weaknesses and documentation exceptions remains high. In particular, the following underwriting and credit administration weaknesses should be promptly addressed:

- *Credit Analysis on Participations Purchased* - The bank does not perform pre-purchase credit analysis on participations purchased. Pre-purchase analysis is necessary for management to assess the repayment capacity of the borrower(s) and assign an appropriate loan grade. An institution purchasing all or part of a loan should perform the same degree of independent credit analysis as if it were the originator.

- *Financial Statements* - Loan officers have not obtained updated financial statements from all repayment sources to perform global cash flow analysis and verify assets of guarantors. Obtaining current financial statements allows a loan officer to analyze and document a guarantor's source of strength to a loan or borrowing relationship.

- *Inspections and Lien Waivers* - The bank does not perform inspections or obtain mechanic's lien waivers prior to making construction loan advances. Timely inspections and lien waivers protect the institution's collateral and lien positions and allow management to make informed decisions regarding the ALLL, particularly if required to individually test these loans for impairment under ASC 310.

- *Rent Rolls* - Loan officers do not obtain rent rolls and vacancy figures on an ongoing basis for loans secured by commercial real estate. Rent rolls and vacancy information allow management to properly monitor these types of loans if conditions are changing, understand any changes in the condition, and make informed and timely credit decisions.

- *Lien Perfection* - The bank periodically allows perfected interests in collateral to lapse by not filing timely Uniform Commercial Code (UCC-1) continuation statements. Use of a system to assist in keeping filings current protects collateral positions determined to be appropriate in original loan underwriting.

President Lincoln stated loan officers would immediately begin performing pre-purchase analyses on participations purchased. She also stated that the volume of documentation deficiencies is primarily due to

understaffing and indicated management is in the process of hiring an additional loan clerk to assist in this area.

Other Real Estate (ORE)

Management maintains appropriate policies and procedures for acquiring, holding, and disposing of ORE. However, due to deterioration in existing credits, the dollar volume of adversely classified ORE increased $535M, or 78 percent, since the previous examination. The ORE portfolio primarily consists of CRE previously written down to fair value. The $100M ORE Loss classification reflected in this Report is based on the recently obtained (August 3, 2016), appraised value of the Rolly property.

Concentrations

Several asset concentrations, including a fishing industry concentration, are listed on the Concentrations page. Management does not currently have procedures in place to adequately identify and monitor such concentrations. Concentrations that are not monitored and managed through sound risk management practices can expose a bank's capital and earnings to disproportionately higher losses in the event of a borrower's financial problems or an industry downturn, such as is currently being experienced by the local fishing industry. Given the potential for increased risk posed by asset concentrations, appropriate policies and procedures should be established to ensure these risks are properly identified, monitored, and managed.

President Lincoln indicated that management will develop procedures for identifying, monitoring, and managing the risk of concentrations and present them to the Board for its review and approval by year-end 2016.

Disposition of Assets Classified Loss

President Lincoln stated that assets classified Loss totaling $1,015M will be charged off by September 30, 2016.

EARNINGS - 4

Earnings performance remains poor. As detailed on the Analysis of Earnings page of this Report, the bank experienced significant operating losses in 2014 and 2015. Although the bank shows net operating income of $103M for the first six months of 2016, profits are substantially overstated due to inadequate provisions for loan losses. As reflected in the footnote on the Examination Data and Ratios page, the bank will show a negative 0.58 percent Return on Average Assets, based on a net operating loss of $222M, after amending the June 30, 2016 Call Report for the additional $325M ALLL provision.

The poor earnings performance is a direct result of persistent poor asset quality and increasing ORE levels. Although improving, the high level of nonperforming assets has required high ALLL provisions and increased overhead expenses. In spite of the volume of nonaccruals and other nonearning assets remaining high, the net interest margin for the first six months of 2016 improved to 4.74 percent from 4.37 percent at year-end 2015. This improvement is primarily the result of management's ability to maintain average interest rates in the loan portfolio above 8 percent, while reducing the average cost of funds to below 3 percent.

Total Noninterest Expense as a percentage of Average Assets has steadily increased over the last three years and reached 3.82 percent as of June 30, 2016. Overhead expenses are nearly 100 basis points above comparable institutions, primarily due to expenses associated with ORE. Given the composition and level of problem assets, management does not expect ORE-related expenses to diminish in the near future. Overhead expenses will also increase due to the planned hiring of additional credit administration personnel. However, in an effort to reduce overhead, management plans to close the institution's only branch office on September 30, 2016.

The 2016 budget forecasts net income of $226M. With the exception of inaccurate assumptions related to the level of provision expense, the budgeting process is adequate and the assumptions used are reasonable. Future profitability is primarily dependent on improved asset quality and controlled overhead expenses.

Chairman of the Board Sean White stated that the directorate and senior management would revise the budget to depict provision expense levels more accurately. He directed President Lincoln to have the revised budget ready for Board review and approval at the November 2016 Board meeting.

MANAGEMENT - 3

The overall performance of senior management and the Board of Directors remains less than satisfactory. The bank's weak financial condition is primarily the result of liberal lending policies and poor credit administration practices. As documented in prior examination reports, the present management team aggressively pursued loan growth without regard for prudent lending standards and, ultimately, asset quality. Although initial signs of more prudent loan underwriting and improved credit administration are evident, asset quality remains weak and significant aspects of the credit function remain deficient.

Board Supervision

A director's duty to oversee the conduct of a bank's business necessitates that each director exercise independent judgment in evaluating management's actions and competence. Directors need to critically evaluate the issues before them, rather than routinely deferring to management. However, Board minutes lack evidence to demonstrate that directors are exercising their independent judgment. Instead, Board minutes indicate that Chairman White and President Lincoln dominate policy discussions and decisions. Moreover, Director Michael D. Brown attended only 5 of the 12 Board meetings held since the previous examination. Regular attendance at Board and committee meetings is a prerequisite to fulfilling the duty to oversee the conduct of the bank's business, and directors who are unable to meet this obligation should consider resignation. Weaknesses in the strategic planning process and the inadequacy of certain written policies are additional indicators that the Board needs to improve its oversight of the bank's operations and management's actions.

Chairman of the Board White indicated that directors are more engaged in discussions regarding the bank's business than is reflected in the minutes and that future minutes will be more descriptive regarding the input from various directors. Director Brown stated that he frequently travels out of town on business; however, he committed to attending Board meetings on a more regular basis.

Apparent Violations of Laws and Regulations

Examiners cited apparent violations of the Treasury Department's BSA regulations for late currency transaction report (CTR) filings, the Federal Reserve Board's Regulation O for two insider loans that did not receive full Board approval, and exceeding the state's legal lending limit statute. An apparent violation of the BSA was also cited at the last FDIC examination, and although the number of late filings has declined, repeat infractions reflect unfavorably on the Board and management. The Board of Directors should implement improved controls and procedures to ensure timely CTR filings, appropriate Regulation O loan approvals, and identification of concentrations of loans to one borrower. Additionally, the institution is in nonconformance with multiple parts of the Interagency Guidelines Establishing Standards for Safety and Soundness, Appendix A to Part 364 of the FDIC Rules and Regulations.

Chairman of the Board White committed to improve BSA and Regulation O controls and promised future compliance with all Safety and Soundness standards detailed in Appendix A to Part 364.

Strategic Planning

The 2014 five-year strategic plan has not been updated, and is therefore inconsistent with the present condition of the bank, the regional economy, and the local competitive environment. Specifically, the plan's assumptions do not consider the continuing decline of the local fishing industry, the potential impact of a new commercial bank in town, or the recent merger of two local savings and loan associations. Based on these factors, many of the goals and strategies in the plan may be unrealistic. Setting a bank's strategic focus, in conjunction with executive management, is one of the key responsibilities of a bank's Board. An effective strategic planning process provides for regular reviews to determine whether assumptions and strategies remain valid or should be revised. The Board and management should update the strategic plan to reflect current conditions and should adopt a process to periodically review the plan going forward.

Chairman of the Board White stated that the strategic plan would be reviewed and updated before the end of 2016 and annually thereafter.

Audit and Internal Control

The audit and internal control functions lack independence. While the scope and frequency of the internal audit program are adequate, Internal Auditor Mary Jackson reports directly to President Lincoln. Since President Lincoln is ultimately responsible for most of the day-to-day operations reviewed by the internal auditor, this situation compromises the independence of the internal audit program. The internal auditor should report directly to the Board of Directors or the Audit Committee of the Board to ensure the independence and effectiveness of the audit function. President Lincoln is also a member of the Audit Committee, which oversees the external audit function. Her presence on the committee further limits audit independence. Lack of independence in the internal control structure exposes the institution to operational and financial risks and could impact management and the Board's ability to appropriately control risks. Several outside directors are qualified to serve on the Audit Committee and it is recommended that the Board strengthen the audit function by limiting committee membership to outside directors.

Several internal control deficiencies are detailed under Item 5 of the Risk Management Assessment section of this Report. While these deficiencies are relatively minor, management incorrectly reported that two of these items were corrected in the response to the last internal audit. Failure to accurately monitor and track corrective actions of audit findings decreases the Board's ability to fulfill their oversight responsibilities.

Chairman of the Board White stated that the Board would consider these recommendations at its next meeting. He also stated the internal control deficiencies would be addressed by the end of 2016.

Reports of Condition and Income

Material errors were noted in the last three quarterly Reports of Condition and Income. In numerous cases, examiners were unable to reconcile bank records with the quarterly filings. The most significant errors relate to inaccurately reported interest and fee income on loans, the inappropriate inclusion of gains on the sale of repossessed assets in interest and fee income, and the shortfall in the ALLL. These errors misrepresent financial performance and negatively affect management's ability to make informed decisions. Management should investigate these errors and amend prior Reports of Condition and Income as appropriate.

Executive Vice President/Cashier John M. Gutierrez stated he will file amended June 30, 2016, Reports of Condition and Income, prior to September 30, 2016, to address these issues.

Bank Secrecy Act

The BSA program is generally satisfactory; however, examiners cited apparent violations of Title 31 C.F.R Chapter X Section 1010.306(a)(1) of the Treasury Department's Bank Secrecy Act regulations. The apparent violations relate to Currency Transaction Reports (CTRs) that were not filed within prescribed periods; refer to the Violations of Laws and Regulations page for additional details. Management should establish procedures to ensure CTRs are filed within prescribed timeframes.

President Lincoln indicated procedures would be implemented within 90 days to ensure CTRs are submitted in a timely manner.

Office of Foreign Assets Control (OFAC)

Effective policies, procedures, and controls are in place to ensure satisfactory compliance with OFAC regulations.

CAPITAL - 3

Capital is less than satisfactory in relation to the bank's risk profile. The Adversely Classified Items Coverage Ratio remains high at approximately 84 percent. In addition, after adjustments for provisions to fund the ALLL appropriately, the bank has had net operating losses over the past two and a half years. The existing concentration in fishing industry loans, considering the industry's current depressed condition and anticipated continuing decline, adds to capital concerns. The Leverage Capital ratio of 7.44 percent, detailed on the Examination Data and Ratios page, reflects current examination adjustments for assets classified Loss and the provision expense needed to fund the ALLL appropriately.

President Lincoln stated that dividends have not been paid for five years. She further stated that no dividends would be paid until the Tier 1 Leverage Capital ratio exceeds eight percent and earnings become positive and stable.

LIQUIDITY - 2

The bank's liquidity position is satisfactory. Asset growth has been minimal since the prior examination and the loan portfolio is shrinking. Management has increased the volume of investments in mortgage-backed securities, with the portfolio maintaining slight appreciation. Non-core funding has increased slightly but management is using these funds appropriately. While liquidity levels and funds management practices are generally satisfactory, management should develop a written funds management policy and a contingency funding plan commensurate with the bank's risk profile. Clearly articulated policies reflective of the bank's characteristics help ensure that the institution is operating within Board-approved risk tolerances, which can mitigate the negative impact of overreliance on volatile funding sources in an adverse economic environment. Off-balance sheet commitments are minimal.

President Lincoln stated a written funds management policy and a contingency funding plan would be developed by March 31, 2017.

SENSITIVITY TO MARKET RISK - 2

Sensitivity to market risk is moderate and risk management practices are satisfactory. Funding sources reasonably match the bank's asset repricing structure, and the loan portfolio includes a high volume of adjustable-rate commercial loans. Over the past two years, depositors have moved funds out of maturing time deposits and into money market demand accounts. Management actively manages rates on these deposits, as the local market is very competitive. The bank does not engage in off-balance sheet derivative activity.

Management regularly monitors the bank's rate sensitivity position using income simulations and an economic value of equity model, and presents detailed quarterly reports to the Board. However, management and the Board should establish, and monitor compliance with, policy limits that reflect the board's interest rate risk tolerance. Appropriate limits should permit management to control interest rate risk exposure, initiate discussions about opportunities and risk, and monitor actual risk taking against pre-determined risk tolerances. Establishing such limits is consistent with the prudent interest rate risk principles discussed in the Joint Agency Policy Statement on Interest Rate Risk. Refer to the Risk Management Assessment page for additional details.

Chairman of the Board White stated that management and the Board would establish interest rate risk policy limits by year-end 2016.

TRUST - 2

The Trust Department operates in general conformance with the Statement of Principles of Trust Department Management. The Board and management's performance and risk management practices are satisfactory relative to the size of the department and the complexity of trust activities. Only moderate weaknesses are present and within management's ability to correct.

Account administration is generally in compliance with originating documents. However, potential conflicts of interest exist from the trust department using own-bank deposits, as well as from holding stock of the parent holding company and an affiliate in one trust account. Trust Officer Hancock surveys local deposit rates to ensure competitive rates are being paid on deposits, but does not maintain documentation of her surveys. Appropriate policies, procedures, and practices should be developed and implemented to effectively control conflicts of interest and manage own-bank deposits and stock holdings. Without proper policies, procedures, and practices, the bank is exposed to potential litigation risk, which could negatively affect earnings and capital.

Trust Officer Hancock stated she would maintain documentation of comparable rates in the future.

Asset management practices are generally satisfactory. All account transactions, including discretionary disbursements, are included in monthly Board reports, and the Board reviews all accounts annually. However, management should annually document its needs assessment for each applicable account and/or beneficiary, and indicate whether the account's investment mix is meeting those needs. Failure to adequately document needs assessments, evaluate the mix, and document the review exposes the bank to litigation risks.

Trust Officer Hancock committed to documenting annual needs assessments for each trust account.

INFORMATION TECHNOLOGY - 2

Overall, IT operations, risk management practices, and cybersecurity are satisfactory. The IT audit program is generally adequate. Management and Board oversight of IT programs are generally satisfactory demonstrated by adequate policies and risk management practices. The bank is in general compliance with the Interagency Guidelines Establishing Standards for Safeguarding Customer Information set forth in Part 364, Appendix B, of the FDIC Rules and Regulations. Management adequately assesses its cybersecurity risk exposure including its inherent risks, and cyber maturity levels.

While the overall IT department is satisfactory, minor exceptions were noted related to:

- Audit reporting lines and scoping
- Patch Management
- Financial and audit review of critical vendors
- Control assessments on third party providers
- Detail in project documentation
- Business Continuity Plan parameters

Findings of the IT examination were discussed in detail on August 27, 2016, with Information Technology Manager William Robbins and President Lincoln.

Management indicated agreement with all findings. Refer to the Information Technology Page for details on the exceptions and management commitment and timeframes for corrective action.

MEETING WITH THE DIRECTORATE

A Board of Directors meeting was held on September 18, 2016. All directors were present with the exception of Director Henry P. Black. William E. Smith, partner in the bank's auditing firm, was also present. Deputy Commissioner of Banking Cynthia B. Jones represented the State Department of Banking. Field Supervisor James D. Gilmore, Examiner-in-Charge Sandra E. Smart, and Financial Institution Examiner Monica D. Powers represented the FDIC. All matters listed above were discussed with the Board. Most of the discussion concerned the increase in severity of adverse classifications, the need to improve the ALLL methodology, and management's efforts to improve loan administration procedures. The Directorate and management's commitments for corrective action are noted within this report. Chairman of the Board White asserted that because of the improvement in the bank's overall condition, the MOU should be removed.

DIRECTORATE RESPONSIBILITY

Each member of the Board of Directors is responsible for reviewing this Report of Examination. Each Director must sign the Signatures of Directors page, which affirms that he or she reviewed the Report in its entirety.

Examiner (Signature)	Reviewing Official (Signature) and Title
Sandra E. Smart	Dale K. Watson, Assistant Regional Director

A Memorandum of Understanding (MOU) between the FDIC and the bank became effective on January 21, 2015. Provisions of the MOU that require further efforts or are of a continuing nature are detailed below.

2(b). The bank shall maintain an Allowance for Loan and Lease Losses at an appropriate level.

Based on this examination's findings, the Allowance for Loan and Lease Losses is underfunded by at least $325M.

3(a). The bank shall maintain a Leverage Capital ratio equal to or greater than 7 percent.

As of June 30, 2015, the Leverage Capital ratio, adjusted for the additional $325M provision for loan and lease loss expense, approximates 7.44 percent.

3(d). The bank shall maintain a Total Capital ratio equal to or greater than 10 percent.

As of June 30, 2016, the Total Capital ratio, adjusted for the additional $325M provision for loan and lease loss expense is 11.75 percent.

4. The bank shall file accurate Call Reports.

Examiners noted significant errors in the December 31, 2015, and the March 31 and June 30, 2016, Call Reports which require amendments.

5. The bank shall not extend or renew, directly or indirectly, credit to, or for the benefit of, any borrower who has a loan or other extension of credit with the bank that has been charged off or classified, in whole or in part, Loss, Doubtful, or Substandard, unless rationale for the extension is noted in the official Board minutes and the appropriate credit file.

On January 30, 2016, the bank extended a $50M loan to U. R. Worth. The borrower was adversely classified Loss at the previous examination. The Board did not specifically document the reason(s) for the extension in the official Board minutes or in the appropriate credit file.

6. The bank shall not declare or pay any dividends without the written consent of the FDIC.

No dividends have been declared or paid since the previous examination.

1. Are risk management processes adequate in relation to economic conditions and asset concentration levels?

No. As discussed on the ECC pages, the Board's strategic plan is outdated and does not reflect the institution's current condition or operating environment. In addition, management does not adequately identify, evaluate and monitor asset concentrations as exemplified by the deficiencies noted in managing the correspondent bank, fishing industry, and individual borrower concentrations identified in this report. Establishment of appropriate concentration risk policies and procedures would enhance the management's ability to identify and control risks and avoid potential violations of law. Refer to the Concentrations pages for additional details.

President Lincoln stated that management will develop procedures to identify, evaluate, and monitor concentrations.

2. Are risk management policies and practices for the credit function adequate?

No. Internal credit review and grading procedures are weak, and credit administration practices are deficient. Recommendations for improvement are included under Asset Quality on the ECC page.

Due to the deficiencies noted in the institution's internal credit grading system and the use of inaccurate loan loss rates, the ALLL is insufficient. In addition, management utilized an inappropriate loan loss experience to establish a reserve rate for its non-watch list loans, which contributed to the insufficient ALLL level. Management is reminded of the safety and soundness principles provided in the Interagency Policy Statement on the ALLL (Policy Statement) which states, in part, "each institution should ensure controls are in place to consistently determine the ALLL in accordance with GAAP, the institution's stated policies and procedures, management's best judgment and relevant supervisory guidance." Further, the Policy Statement discusses supervisory expectations for institutions to have an, "effective loan review system and controls (including an effective loan classification or credit grading system) that identify, monitor, and address asset quality problems in an accurate and timely manner." The Policy Statement also notes that institutions should maintain supporting documentation for the techniques used to develop the historical loss rate for each group of loans and that resulting estimated credit losses are in conformity with GAAP. Implementation of the principles discussed in the Policy Statement will help ensure that the internal credit grading system is accurate and the ALLL is appropriate.

President Lincoln committed to filing Call Report amendments prior to the September 30, 2016 submission and to reviewing the loan grading system.

Additionally, although the bank's loan policy is generally adequate, it does not address the following matters:

- *Participation Loans* - The bank regularly purchases loans or portions of loans from other institutions. These specialized lending activities are not covered in the loan policy.

- *Construction Loans* - The bank finances the construction of 1- to 4-family residences and mixed use commercial property. While practices are generally adequate, a large construction loan listed for Special Mention reflects several weaknesses in construction lending. The policy lacks specific guidelines pertaining to construction lending. President Lincoln was provided with a detailed list of issues that should be considered.

- *<u>Environmental Risk</u>* - An environmental risk policy has not been established. Examiners provided FDIC's Financial Institution Letter FIL-98-2006, *Updated Guidelines for an Environmental Risk Program* to management for further consideration.

Development of comprehensive loan policy guidance provides management and staff with clear expectations for administering the lending function and facilitates sound risk management practices.

President Lincoln stated that management would develop guidelines for purchased loans and construction lending and revise the loan policy by December 31, 2016. She further stated management is currently developing an environmental risk policy.

3. Are risk management policies and practices for asset/liability management and the investment function adequate?

Generally, yes. Management's liquidity management practices are generally adequate; but a written funds management policy or a contingency funding plan has not been established. Similarly, overall practices for Sensitivity to Market Risk are generally adequate; however, management should establish Board approved policy parameters that reflect the bank's tolerance for interest rate risk consistent with the prudent interest rate risk management principles contained in the Joint Agency Policy Statement on Interest Rate Risk. One key principle is for the Board "to establish and guide the bank's tolerance for interest rate risk, including approving relevant risk limits and other key policies, identifying lines of authority and responsibility for managing risk, and ensuring adequate resources are devoted to interest rate risk management." Implementing appropriate limits strengthens management's ability to manage interest rate risk and monitor actual risk taking activity.

President Lincoln stated that interest rate risk policy limits would be established by year-end 2016.

Investment policy guidelines are adequate; however, management's adherence to its written investment policy is inconsistent. On at least three occasions since the previous examination, President Lincoln exceeded her purchasing authority when she purchased securities over $250M without prior Board approval. Failure to adhere to Board approved purchasing authority could increase the risk profile of the institution above Board approved risk tolerances.

The Board should ensure management purchases investments in conformance with existing policy standards or determine if it would be prudent to revise the standards to meet purchasing needs.

President Lincoln stated that she was presented with the opportunity to purchase these securities at a good price and could not wait for Board approval. She further stated she would comply with the policy in the future or discuss modifying the policy with the Board at the next Board meeting.

4. Are risk management processes adequate in relation to, and consistent with, the institution's business plan, competitive conditions, and proposed new activities or products?

No. As discussed on the ECC pages, the Board's strategic plan is outdated and does not reflect the institution's current condition or operating environment.

5. Are internal controls, audit procedures, and compliance with laws and regulations adequate (includes compliance with the Bank Secrecy Act [BSA] and related regulations)?

No. As indicated on the ECC page, apparent violations of Bank Secrecy Act regulations, Regulation O, and the state legal lending limit were cited during this examination. Additionally, the bank is not in conformance with the Interagency Guidelines Establishing Safety and Soundness Standards. Full details of these citations can be found on the Violations of Laws and Regulations pages. In addition, the audit and internal control functions lack independence.

Internal Controls

Examiners noted the weaknesses below in the bank's system of internal controls. Maintaining strong internal controls helps ensure the integrity of operations and discourages potential insider abuse.

- *Vacation Policy* – The bank's vacation policy requires employees to be absent from their normal duties for an uninterrupted period of two weeks each calendar year. Executive Vice President Leslie S. Cook did not remain absent during her two-week vacation in 2015 as she returned daily to reconcile the Federal funds sold account. Management should enforce the policy, particularly for employees who are responsible for sensitive transactions.

- *Reconcilement of Correspondent Bank Accounts* – Management has not reconciled the correspondent bank accounts for the past three months. While personnel reconciled these accounts during the examination, they should be reconciled at least monthly.

President Lincoln stated she would take action to address these deficiencies before year-end 2016.

6. Is Board supervision adequate, and are controls over insider transactions, conflicts of interest, and parent/affiliate relationships acceptable?

No. Board supervision is less than satisfactory. Numerous underwriting weaknesses and credit administration deficiencies remain uncorrected from prior examinations, and the Board has not established an effective independent internal audit function. Refer to comments under Management on the ECC page for more details. Additionally, examiners cited two loans as apparent violations of the Federal Reserve Board's Regulation O because management did not obtain the prior approval of the Board on loans to the related interests of President Lincoln and Director Larry G. Green. Refer to the Violations of Laws and Regulations page of this Report for details.

APPARENT VIOLATIONS OF LAWS AND REGULATIONS

BANK SECRECY ACT

Title 31 C.F.R Chapter X Section 1010.306(a)(1) of the Treasury Department's Bank Secrecy Act regulations requires a covered financial institution to file a Currency Transaction Report (CTR) (FinCEN Form 104) within the prescribed period.

Examiners identified numerous instances where CTRs were not filed within the required 15-day period. This infraction was also cited at the previous FDIC examination. Between October 2015 and July 2016, 289 of 944 CTRs (31 percent) were filed late. In many cases, CTRs were signed by the approving official more than 15 days after the transaction date. The time between the transaction date and receipt by the Treasury Department on these late filings was generally around 20 to 25 days, with a few exceeding 70 days.

BSA Officer Donna Ludlow stated that some of the late CTRs were filed after an internal audit noted that the forms had not been submitted; however, she could offer no explanation as to why the remaining CTRs were filed late. President Lincoln stated that new procedures would be implemented within 90 days to ensure all CTRs are submitted in a timely manner in the future.

REGULATION O

The Federal Reserve Board's Regulation O, which implements Section 22(h) of the Federal Reserve Act and is made applicable to insured nonmember institutions by Section 18(j)(2) of the Federal Deposit Insurance Act, covers transactions with bank insiders. Section 215.4(b)(1) of Regulation O requires extensions of credit by an institution to a director or related interest exceeding the greater of $25M or five percent of unimpaired capital and surplus to have prior approval of the institution's board of directors.

The bank is in apparent violation of this section for extending the following loans with the prior approval of the Executive Loan Committee, which is composed of only three Board members, rather than prior approval by the full Board.

Borrower	Date of Note	Original Amount
Lincoln, Allie C.	12/11/2015	$500M
Any Body, Inc.	12/28/2015	$250M
(A related interest of President Lincoln and Director Green.)		

President Lincoln stated that these exceptions were the result of oversight. She further indicated that bank policy requires that all insider loans receive the prior approval of the full Board. Examiners noted that all other insider loans received prior Board approval. President Lincoln and the Board of Directors promised future compliance.

LEGAL LENDING LIMIT

Section 1127 of the State Banking Code provides that the total direct or indirect loans and extension of credit or lease by a bank to one obligor or guarantor at no time shall exceed 15 percent of "statutory capital" (equivalent to total capital) of the bank, except upon approval by two-third vote of its board of directors the limit may be increased up to 25 percent of the statutory capital of the bank. On January 2, 2016, the bank extended an additional $650M to J&M Realty Trust, guaranteed by John and Mary Smith, which increased total outstanding debt to the Smiths and their companies to $1,950M, or 31 percent of statutory capital. The extension of additional credit was made without approval by the board of directors, and represents an apparent violation of Section 1127.

President Lincoln stated that the extension of credit over the lending limit was the result of oversight.

NONCONFORMANCE WITH INTERAGENCY GUIDELINES

INTERAGENCY GUIDELINES ESTABLISHING STANDARDS FOR SAFETY AND SOUNDNESS

The Interagency Guidelines Establishing Standards for Safety and Soundness (Appendix A To Part 364 of FDIC Rules and Regulations) establish expectations for banks to implement sound risk management practices. The institution is in nonconformance with the following sections of Appendix A to Part 364 Safety and Soundness Standards.

A. Internal controls and information systems. An institution should have internal controls and information systems that, in part, are appropriate to the size of the institution and the nature, scope and risk of its activities and that provide for timely and accurate financial, operational, and regulatory reports and compliance with applicable laws and regulations.

> Material errors were noted in the institution’s quarterly Call Report filings over the last three quarters, which necessitates restatement of the institution’s most recent Call Report. Additionally, three apparent violations of laws and regulations were noted, including a repeat violation regarding untimely CTR filings.

B. Internal audit system. An institution should have an internal audit system that is appropriate to the size of the institution and the nature and scope of its activities and that provides for, in part: independence and objectivity; adequate testing and review of information systems; and adequate documentation of tests and findings and any corrective actions.

> The audit and internal control functions lack independence, which jeopardizes the effectiveness of the internal audit program. Further, the lack of independence coupled with inadequate monitoring of audit findings status reports resulted in previously identified deficiencies being inaccurately reported as corrected.

C. Loan documentation. An institution should establish and maintain loan documentation practices that, in part: enable the institution to make an informed lending decision and to assess risk, as necessary, on an ongoing basis; identify the purpose of a loan and the source of repayment, and assess the ability of the borrower to repay the indebtedness in a timely manner; ensure that any claim against a borrower is legally enforceable; and demonstrate appropriate administration and monitoring of loans.

> Credit administration, although improving, remains deficient. Noted weaknesses include lapses in UCC-1 filings, absence of inspections or mechanic’s lien waivers prior to construction advances, and absence of rent roll information. As noted on the Assets with Credit Data or Collateral Documentation Exceptions page, one-third of the dollar volume of loans reviewed had documentation exceptions that impaired management’s ability to make an informed lending decision and to assess risk, as necessary on an ongoing basis.

D. Credit underwriting. An institution should establish and maintain prudent credit underwriting practices that: are commensurate with the types of loans the institution will make and, in part, provide for consideration, prior to credit commitment, of the borrower's overall financial condition and resources, the nature and value of any underlying collateral, and the borrower's character and willingness to repay as agreed; establish a system of independent, ongoing credit review and appropriate communication to management and to the board of directors; and take adequate account of concentration of credit risk.

Management does not conduct pre-purchase credit analysis for participations purchased, which precludes its ability to evaluate the underlying creditworthiness of these credits and the borrower's ability to repay. Additionally, inadequate staffing of the credit review function contributed to inaccurate loan grading for several large credits. Moreover, management does not have adequate procedures in place to identify and monitor concentrations.

G. Asset quality. An insured depository institution should establish and maintain a system that is commensurate with the institution's size and the nature and scope of its operations to identify problem assets and prevent deterioration in those assets. The institution should, in part, estimate the inherent losses in those assets and establish reserves that are sufficient to absorb estimated losses.

As detailed on the ECC page, inaccurate internal loan grading resulted in an underfunded ALLL.

President Lincoln stated that all noted deficiencies will be added to the Audit Findings Tracking Report and that applicable executive officers would begin action to address deficiencies immediately.

Uniform Rating System for Information Technology

	Current Exam	Prior Exam	Prior Exam
Examination Start Date	08/01/2016	11/13/2015 / S	10/21/2014
Composite Rating			
Component Ratings:	**2**	**1**	**2**
Audit	**2**		
Management	**2**		
Development & Acquisition	**2**		
Support & Delivery	**2**		

Overall, IT, operations, risk management, and security are satisfactory. Management's attention is directed to the items below.

Audit - 2

The IT audit program is generally adequate, and internal auditors promptly identify and report deficiencies and risks. Identified issues are formally tracked and resolved in a timely fashion, and the IT audit plan is based on a thorough risk assessment of IT assets and internal and external threats.

The majority of critical IT areas were reviewed in recent IT audits; however, examiners identified a concern with the current audit scope. Specifically, patch management and cybersecurity are not included in the bank's IT audits. Management should ensure all critical IT areas are included in the scope of IT audits, with the frequency being based on the audit risk assessment. Including all critical IT areas in the internal audits may have reduced the number of items noted in the recent external vulnerability assessment and will help ensure operations continue functioning as needed going forward.

Examiners also noted a concern with the audit reporting structure. At present, internal auditors report to President Lincoln rather than the Board's Audit Committee. In order to increase the auditors' independence and help ensure the Board is able to fulfill its oversight responsibilities, the internal auditors should report directly to the Board's Audit Committee.

President Lincoln stated that the omission of patch management and cybersecurity from the recent IT General Controls audit was an oversight and agreed to include the areas in future audits. President Lincoln also stated that she would recommend to the Board that they modify the IT audit reporting structure so auditors report directly to the Board's Audit Committee.

Management - 2

Overall IT management provides adequate guidance and direction. The oversight and supervision of the information security program and related practices are supported by adequate Board approved policies and risk management practices. Managers are well qualified and tenured for their respective positions.

Vendor Management

Overall, management monitors service providers to confirm they satisfied their contractual obligations; however, management did not review the financial statements or the Statement on Standards for Attestation Engagements (SSAE 16) reports of two critical service providers. To help ensure all service providers are appropriately monitored and to improve the effectiveness of management's monitoring activities, management should formally document all required reviews.

President Lincoln indicated the missing reviews were an oversight and stated that a tickler system would be developed to remind the vendor -review officer of upcoming vendor reviews.

Compliance with Interagency Information Security Standards

Management is in general compliance with the Interagency Guidelines Establishing Standards for Safeguarding Customer Information set forth in Part 364, Appendix B, of the FDIC Rules and Regulations. Management identified the location of all non-public personal information, both electronic and hard copy. Threats to each type of information were identified, adequate controls are in place, and an annual report of the program is presented to the Board. While the overall program is adequate, management did not conduct control assessments on all third-party providers that obtain, use, or process non-public personal information. Management should expand the scope of the control assessments to include all applicable third-party providers. Including all applicable third parties in the assessments will help ensure the providers are appropriately identified and risk rated, and will help confirm third parties have adequate internal controls to protect non-public information.

President Lincoln stated that the vendor management program would be updated to identify all vendors with access to non-public personal information and that control assessments would be conducted on all identified vendors before March 31, 2017.

Cybersecurity Preparedness

Management's assessment of the bank's cybersecurity risk exposure appropriately identifies inherent risks; however, cybersecurity preparedness could be strengthened by determining whether cyber-related controls are sufficient. By identifying cyber-related controls and determining whether they mitigate the identified inherent risks to an acceptable level, management will be better able to identify cybersecurity weaknesses and implement appropriate controls.

President Lincoln indicated that the assessment process would be expanded to include targeted maturity levels by June 30, 2017.

Development and Acquisition - 2

Development and acquisition practices, which include hardware and software implementation and change-management practices, are appropriate for the institution's size and complexity. Overall, project management processes are adequate and provide sufficient guidance to manage projects. Currently, any project exceeding $20M is rated as a major project and requires specific project documentation. However, not all project documentation complies with the internal bank guidelines. For example, the documentation of three recent projects did not include reviews of alternative project solutions or explanations of why the solutions recommended in the project proposals were the most appropriate solutions. Management should comply with internal bank guidelines to ensure project requirements are met and consistent project documentation is in place.

President Lincoln indicated the project management program was relatively new and that project requirements were being introduced in a phased approach so as to not overwhelm employees. However, she agreed to follow internal project guidelines on future projects.

Support and Delivery - 2

Overall computer operations and information security practices are adequate, and management has improved its business continuity and disaster recovery plans. Management established an information security group to set standards, monitor trends, and review system logs and alerts. Although overall operations are adequate, examiners identified areas that require management's attention such as system-log monitoring, vulnerability assessments, patch management, and business continuity planning.

<u>Logging and Monitoring</u>

Management uses different logging platforms for firewalls, internal servers, and routers, and data is not shared or correlated among the logging systems. While servers and base operating systems are logged, logging is not enabled for virtual operating system environments. Management should review its current logging program to ensure all critical systems are included and that there is sufficient data correlation between the systems. Improving the logging program will help ensure all necessary information is obtained and provide the information security group with data in a more effective, centralized format.

<u>Vulnerability Assessments</u>

Management contracts an outside third party to conduct annual, internal vulnerability assessments as part of an overall security review. The scope of the vulnerability assessment is adequate; however, having only one assessment per year could result in vulnerabilities not being promptly identified. Management should review the frequency of its vulnerability assessment to ensure the frequency of the assessments is based on appropriate risk analysis.

President Lincoln committed to revisiting the logging and monitoring program to ensure that all needed information is logged and, to the extent possible, centralized. Additionally, she stated that management would review the frequency of the vulnerability assessments and conduct more frequent assessments based on appropriate risk analysis. President Lincoln stated the reviews would be completed by the end of 2016, and appropriate corrective actions would be implemented by March 31, 2017.

<u>Business Continuity</u>

Management changed the structure of its business continuity plan this year. The new program is adequate, but the areas of business impact analysis (BIA) and disaster recovery (DR) testing require further refinement.
The BIA and risk assessments are out-of-date but are being updated to include new recovery time objectives (RTO) and to identify reasonably foreseeable threats, including cybersecurity threats. Currently, the shortest RTO is 24 hours. The 24-hour RTO may be too extended for the application, and there are several systems that may benefit from RTOs of four hours or less. The current extended RTOs may significantly affect multiple business lines and the institution's ability to restore critical systems after a disaster. Management should ensure RTOs are appropriate so that critical operations can be restored promptly after a disaster or business interruption.
While some disaster recovery (DR) testing has occurred, management has not sufficiently tested a few critical systems. Management should review its testing universe and implement a risk-based testing approach to ensure all necessary testing is completed in a timely manner. Failure to conduct appropriate tests could result in material delays in restoring critical systems if a disaster occurs.

President Lincoln agreed to conduct the BIA and risk assessments, review RTOs, and implement risk-based DR testing by March 31, 2017.

ASSET QUALITY		ADVERSELY CLASSIFIED			
		Substandard	Doubtful	Loss	Total
Loans and Leases		4,290	140	890	5,320
Securities		45			45
Other Real Estate Owned		1,125		100	1,225
Other Assets				25	25
Other Transfer Risk					
Subtotal		5,460	140	1,015	6,615
Contingent Liabilities		230			230
Totals at Exam Date	06/30/2016	5,690	140	1,015	6,845
Totals at Prior Exam	09/30/2015	7,345	220	194	7,759
Totals at Prior Exam	09/30/2014	6,655	177	67	6,899

	Exam Date 06/30/2016	Prior Exam 09/30/2015 (S)	Prior Exam 09/30/2014
Total Special Mention	854	515	
Adversely Classified Items Coverage Ratio	84.41	102.71	94.92
Total Adversely Classified Assets/Total Assets	8.21	9.93	8.20
Past Due and Nonaccrual Loans and Leases/Gross Loans and Leases	6.74	8.42	9.12
Adversely Classified Loans and Leases/Total Loans	9.86	12.68	11.30
ALLL/Total Loans and Leases	3.67	3.15	2.50

CAPITAL	Exam Date 06/30/2016	Prior Exam 09/30/2015 (S)	Prior Exam 09/30/2014
Tier 1 Capital/Average Total Assets(1)	7.44	7.55	7.67
Common Equity Tier 1 Capital/Risk-Weighted Assets(1)	10.48		
Tier 1 Capital/Risk-Weighted Assets(1)	10.48	9.88	9.90
Total Capital/Risk-Weighted Assets(1)	11.75	8.42	11.40
Prompt Corrective Action Capital Category	W	W	W
PCA Categories: W – Well-capitalized, A – Adequately capitalized, U – Undercapitalized, S – Significantly undercapitalized, C – Critically undercapitalized			

	Period Ended 06/30/2016	Peer 06/30/2016	Period Ended 12/31/2015	Period Ended 12/31/2014
Retained Earnings/Average Total Equity	3.37	9.32	(2.05)	(3.86)
Asset Growth Rate	2.66	6.78	0.42	0.20
Cash Dividends/Net Income		32.65		

EARNINGS	Period Ended 06/30/2016	Peer 06/30/2016	Period Ended 12/31/2015	Period Ended 12/31/2014
Net Income (After Tax)/Average Assets (2)	0.27	1.03	(0.15)	(0.30)
Net Interest Income (TE)/Average Earning Assets	4.74	4.64	4.37	4.64
Total Noninterest Expense/Average Assets	3.82	2.90	3.62	3.54

LIQUIDITY	Period Ended 06/30/2016	Peer 06/30/2016	Period Ended 12/31/2015	Period Ended 12/31/2014
Net Non-Core Funding Dependence(3)	14.71	1.02	8.69	6.66
Net Loans and Leases/Assets	64.45	66.20	68.79	69.24

(1) Capital ratios reflected in the example above are truncated at two decimals (not rounded). Call report instructions require banks to report capital ratios, which are used for determining the PCA capital category, as a percentage, rounded to four decimal places.
(2) After management's planned $325M adjustment to the ALLL, the 6/30/2016 Ratio will drop to (0.58)%.
(3) Ratio reflects time deposits exceeding the $250M deposit insurance limit as non-core funding.

Comparative Statements of Financial Condition | 99999

ASSETS	06/30/2016	12/31/2015
Total Loans and Leases	53,931	55,545
Less: Allowance for Loan & Lease Losses	1,979	1,748
Loans and Leases (net)	51,952	53,797
Interest-Bearing Balances	20	
Federal Funds Sold and Securities Purchased Under Agreements to Resell	4,000	9,100
Trading Account Assets		
Securities: Held-to-Maturity (at Amortized Cost)	2,787	5,993
Available-for-Sale (at Fair Value)	10,888	
Total Earning Assets	**69,647**	**68,890**
Cash and Noninterest-Bearing Balances	5,895	4,743
Premises and Fixed Assets	2,530	2,709
Other Real Estate Owned	1,225	690
Intangible Assets		
Other Assets	1,307	1,175
TOTAL ASSETS	**80,604**	**78,207**

LIABILITIES		
Deposits	67,815	66,221
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	441	516
Other Borrowed Money	5,857	5,136
Other Liabilities	301	307
Subordinated Notes and Debentures		
Total Liabilities	**74,414**	**72,180**
EQUITY CAPITAL		
Perpetual Preferred Stock		
Common Equity Capital	6,190	6,027
Includes net unrealized holding gains (losses) on available-for-sale securities.		
Other Equity Capital		
Total Bank Equity Capital	**6,190**	**6,027**
Minority Interest in Consolidated Subsidiaries		
Total Equity Capital		
TOTAL LIABILITIES AND EQUITY CAPITAL	**80,604**	**78,207**

OFF-BALANCE SHEET ITEMS		
Unused Commitments	4,333	5,893
Letters of Credit	209	824
Other Off-Balance Sheet Items		
Other Derivative Contracts		
Appreciation (Depreciation) in Held-to-Maturity Securities	56	

Footnotes:

Date: 06/30/2016

Category:	Amount	Percent
Real Estate Loans	21,938	40.53
Installment Loans	7,058	13.04
Credit Card and Related Plans	90	0.17
Commercial Loans	22,292	41.18
All Other Loans and Leases	2,753	5.09
Gross Loans and Leases	54,131	100.00

PAST DUE AND NONACCRUAL LOANS AND LEASES

Date: 06/30/2016

Category	Past Due 30 through 89 Days and Accruing	Past Due 90 Days or More and Accruing	Total Past Due and Accruing	Percent of Category	Nonaccrual	Nonaccrual Percent of Category
Real Estate Loans	800	44	844	3.85	1,402	6.39
Installment Loans	125		125	1.77	107	1.52
Credit Card and Related Plans	3		3	3.33		
Commercial and All Other Loans and Leases	626		626	2.50	554	2.21
Totals	1,554	44	1,598	2.95	2,063	3.81
Memorandum						
Restructured Loans and Leases Included in the Above Totals						

Footnotes:

Recapitulation of Securities | 99999

Description	HELD-TO-MATURITY		AVAILABLE-FOR-SALE	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
U.S. Treasury securities	1,537	1,593		
U.S. Government agency obligations				
Issued by U.S. Gov't agencies			2,550	2,554
Issued by U.S. Gov't-sponsored agencies				
Securities issued by U.S. states & political subdivisions	250	250		
Mortgage-backed securities (MBS)				
Residential pass-through securities:				
Guaranteed by GNMA			7,322	7,415
Issued by FNMA and FHLMC				
Other pass-through securities				
Other residential MBS (inc. CMOs, REMICs, & stripped MBS):				
Issued or guaranteed by U.S. Government agencies or sponsored agencies				
Collateralized by MBS issued or guaranteed by U.S. Government agencies or sponsored agencies				
All other residential MBS				
Commercial MBS				
Commercial mortgage pass-through securities:				
Issued or guaranteed by FNMA, FHLMC, or GNMA				
Other pass-through securities				
Other Commercial MBS:				
Issued or guaranteed by U.S. Government agencies or sponsored agencies				
All other commercial MBS				
Asset-backed Securities (ABS) and structured financial products				
Asset-backed securities				
Structured financial products:				
Cash				
Synthetic				
Hybrid				
Other Debt Securities				
Other Domestic Debt Securities				
Foreign Debt Securities	1,000	1,000		
Equity Securities				
Investments in Mutual Funds and Other Equity Securities with Readily Determinable Fair Values			919	919
Totals:	2,787	2,843	10,791	10,888

SECURITIES APPRECIATION (DEPRECIATION)

Description	Held-to-Maturity	Available-for-Sale	Total
Securities Appreciation (Depreciation)	56	97	153
As a Percent of Amortized Cost	2.01	0.90	1.13

Footnotes:

Items Subject to Adverse Classification	**99999**

Includes assets and off-balance sheet items which are detailed in the following categories:
Substandard Assets - A Substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.
Doubtful Assets - An asset classified Doubtful has all the weaknesses inherent in one classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.
Loss Assets - An asset classified Loss is considered uncollectible and of such little value that continuance as a bankable asset is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be effected in the future.

		CATEGORY	
AMOUNT, DESCRIPTION AND COMMENTS	Substandard	Doubtful	Loss

These sample write-ups do not reflect required or preferred formats, but simply illustrate various ways to present the required analytical elements.

LOANS

500	(1)	Nonaccrual	96 Days Past Due			
<u>250</u>	(2)	Nonaccrual	96 Days Past Due			
750				750		

AMHILL TOOL & DIE, INC.
By: Robert E. Hill, President
Gty: Roger S. Barrett

Amhill Tool & Die, Inc. manufactures custom plastic-forming dies and provides injection-molding services.

(1) Note originated 1/7/2012 at $500M to refinance a $450M mortgage on the obligor's manufacturing plant and provide $50M working capital. The note matures 1/7/2019 and requires interest-only payments, with principal due on demand. (2) Term note originated 6/10/2013 at $280M, matures 6/11/2020, and was extended to refinance a working capital note at another financial institution. The primary source of repayment for both notes is operating cash flow.

The loans are cross collateralized by a first mortgage on the manufacturing plant, located in Anytown, Anystate, and a first security interest in all business assets. A 12/7/2011 appraisal reflects a property value of $625M; however, the valuation appears stale given downward trends in local real estate values. As of 12/31/2015, management estimated the value of account receivables and inventory at $100M and assigned an estimated liquidation value of $125M to machinery and equipment. Reliance on the machinery and equipment as a secondary repayment source is restricted by their highly specialized nature and limited marketability.

Amhill Tool & Die, Inc. has been negatively impacted by cancelled contracts and high employee turnover. Weak cash flows have caused on-going delinquency problems and management placed the notes on nonaccrual on 3/31/2016. The obligor's 12/31/2015 income statement reported gross income of $800M and a net operating loss of $100M. Gross sale revenues declined steadily since year-end 2012 and operating losses of $123M and $234M were reported as of 12/31/2013 and 12/31/2014, respectively. Net worth declined to $125M at year-end 2015, and debt service coverage was calculated at 0.91 as of 12/31/2015. The guarantor's 12/31/2014 personal financial statement reflects liquid assets of $30M, a net worth of $375M, and total assets of $890M centered in his ownership interest in Amhill Tool & Die, Inc.

EVP/SLO Leslie S. Cook indicated managerial conflicts contributed to the loss of several lucrative contracts and numerous highly trained employees; however, he stated production output is increasing due to the addition of two knowledgeable managers and improved employee training. He also stated management intends to obtain a new property appraisal, restructure the notes to better match the corporation's cash flows, and to require principal and interest payments on the modified mortgage note.

Debts classified Substandard based on inadequate cash flows, continuing delinquencies, and marginal collateral protection.

Internal Rating: 6 (Watch)
Originating/Servicing Officer: Cook
Examiner: T. Hinojosa

340 BROOKS, JAMES	200	140	
1,250 IRMA DEAT, LTD.	750		500
290 KING, CHRISTOPHER Gty: Sam King, Inc.	290		
865 LAST CHANCE MOTEL, INC.	500		365
275 RAMIREZ, PETER	250		25
1,550 EIGHT LOANS LESS THAN $250,000 List left with management.	1,550		
TOTAL ADVERSELY CLASSIFIED LOANS	4,290	140	890
SECURITIES			
45 ANYCOUNTY MUNICIPAL GENERAL OBLIGATION	45		
TOTAL ADVERSELY CLASSIFIED SECURITIES	45		

Items Subject to Adverse Classification (Continued)			99999
		CATEGORY	
AMOUNT, DESCRIPTION AND COMMENTS	Substandard	Doubtful	Loss
OTHER REAL ESTATE OWNED			
550 ONE WAY HOME, INC. PROPERTY	550		
675 ROLLY PROPERTY	575		100
TOTAL ADVERSELY CLASSIFIED ORE	1,125		100
OTHER ASSETS			
25 SUN, RAYMOND Repossessed Heavy Equipment			25
TOTAL ADVERSELY CLASSIFIED OTHER ASSETS			25
CONTINGENT LIABILITIES			
230 KING, CHRISTOPHER	230		
Amount represents unfunded portion of loan commitment for construction of a single-family residence.			
TOTAL ADVERSELY CLASSIFIED CONTINGENT LIABILITIES	230		
TOTAL ADVERSELY CLASSIFIED ITEMS	5,690	140	1,015

Items Listed for Special Mention	99999

Includes assets and off-balance sheet items which are detailed as follows:
Special Mention Assets – A Special Mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in the deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special Mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

DESCRIPTION	AMOUNT

LOANS

854 RAIN, ROBERT, L.L.C. GTY: Robert Rain	854

Debt represents the balance outstanding on a $1,600M construction/permanent facility, dated 3/7/2016, to refinance an existing $1,200M loan at subject bank granted 1/5/2015. The original loan was granted to develop a 3-story mixed-use commercial and apartment building in Neighboring Town. The new loan provided the borrower with an additional $400M in funds to accommodate a revised construction budget stemming from plan modifications. Loan terms require interest-only payments at 4.375% for a 10-month period. Principal and interest payments of $8,231 based on a 25-year amortization are to commence on 1/7/2017, with the loan to mature in 2021. Collateral consists of a first mortgage on the property under construction appraised at $1,000M "as is" and $2,000M "as complete."

The following credit concerns are associated with the indebtedness:
- The project encountered numerous delays due to difficulty in obtaining permits resulting from the changes in construction plans and due to the need for additional financing.
- Guarantor analysis is inadequate, as liquid assets were not verified and a global cash flow analysis was not prepared.
- Monitoring of the project has been weak. As a result, the loan has been 53 percent funded, but the project is only 40 percent completed, with the difference representing construction funds used for soft costs.
- No feasibility analysis was performed to support the 2015 origination.
- The guarantor's experience as a construction manager is questionable considering the delays, revisions, and cost overruns.
- The appraised value may need to be updated, as it is based on the project being completed within the revised budget and assumes that projected operating results will materialize.

Given the concerns noted above and weaknesses associated with this indebtedness, a Special Mention designation is warranted. To strengthen the credit, close management oversight and monitoring is required, along with the following actions:
- Monitor construction progress and compare to budget to ensure percentage completion is brought in line with funding.
- Verify the guarantor's liquid assets and obtain financial information to perform a global cash flow analysis.
- Obtain an updated appraisal if actual rental rates significantly diverge from the appraisal's projections, if project costs outstrip the revised budget, or if further delays ensue.

Internal Rating: 3
Originating/Servicing Officer: Cook
Examiner: V. Stewart

TOTAL LOANS LISTED FOR SPECIAL MENTION	854

DESCRIPTION	SUBSTANDARD	DOUBTFUL	LOSS	TOTAL
Book Value at Last Examination: 09/30/2015	6,641	220	176	7,037
Reductions:				
Payments	1,030	58		1,088
Not Now Adversely Classified	955	162		1,117
Now Classified Substandard				
Now Classified Doubtful	140			140
Now Classified Loss	890			890
To Other Real Estate or Other Assets				
Charged-Off	209		176	385
TOTAL REDUCTIONS	3,224	220	176	3,620
Additions:				
Not Adversely Classified Previously Further Advances – Loans	873			873
Not Adversely Classified Previously Further Advances – Loans				
Adversely Classified Previously				
Credits Newly Extended				
Previously Classified Substandard		140	890	1,030
Previously Classified Doubtful				
Previously Classified Loss				
TOTAL ADDITIONS	873	140	890	1,903
Book Value at This Examination: 06/30/2016	4,290	140	890	5,320

Analysis of Other Real Estate Owned Subject to Adverse Classification | 99999

DESCRIPTION	SUBSTANDARD	DOUBTFUL	LOSS	TOTAL
Book Value at Last Examination: 09/30/2015	672		18	690
Reductions:				
Not Now Adversely Classified				
Sales With Outside Financing				
Sales With Financing Provided By Subject Institution				
Now Classified Substandard				
Now Classified Doubtful				
Now Classified Loss	100			100
Charged-Off			18	18
TOTAL REDUCTIONS	100		18	118
Additions:				
Not Adversely Classified Previously	550			550
Further Advances - ORE or Loans Not Adversely Classified Previously				
Transferred from Previously Adversely Classified Loans				
Further Advances - ORE or Loans Adversely Classified Previously	3			3
ORE From Credits Newly Extended				
Previously Classified Substandard ORE			100	100
Previously Classified Doubtful ORE				
Previously Classified Loss ORE				
TOTAL ADDITIONS	553		100	653
Book Value at This Examination: 06/30/2016	1,125		100	1,225

Assets with Credit Data or Collateral Documentation Exceptions	99999

This Page includes assets with technical defects not corrected during the examination. The appropriate number or description is noted in the "Deficiency Description" column.

1 - Appraisal
2 - Title Search or Legal Opinion
3 - Borrowing Authorization
4 - Recordation
5 - Insurance
6 - Collateral Assignment
7 - Financial Statement
8 - Inadequate Income/Cash Flow Information
9 - Livestock Inspection
10 - Crop Inspection

Name or Description	Amount	Date of Most Recent Financial Statement	Deficiency Description
LOANS			
AMHERST, MARY	400	None	7
BODY, CHARLES	1,932	12/31/14	7
C&C MARINA	1,973	06/30/14	7
GOETZ, MICHAEL	1,538	None	1
IRMA DEAT, LTD.	750		4, 6
JENNINGS, JENNIFER	1,906		5, 6
KING, CHRISTOPHER	290		4, 5, 6
Gty: Sam King		None	7
LAST CHANCE MOTEL, INC.	500		3, 4, 6
TOTAL	9,289		

Total represents 33 percent of the dollar volume of loans reviewed.

Name or Description	Amount	Date of Most Recent Financial Statement	Deficiency Description
OTHER REAL ESTATE OWNED			
ONE WAY HOME, INC. PROPERTY	550		5
TOTAL	550		

Total represents 45 percent of the dollar volume of ORE reviewed.

Listed below are material direct and indirect asset and funding concentrations, according to the following guidelines: 1) asset concentrations of 25% or more of Total Capital (loan related) or Tier 1 capital (non-loan related) by individual borrower, small interrelated group of individuals, single repayment source or individual project; 2) asset concentrations of 100% or more of Total Capital (loan related) or Tier 1 capital (non-loan related) by industry, product line, type of collateral, or short term obligations of one financial institution or affiliated group; 3) funding concentrations from a single source representing 10% or more of Total Assets; and 4) potentially volatile funding sources that when combined represent 25% or more of Total Assets (these sources may include brokered, large, high-rate, uninsured, and Internet-listing-service deposits; Federal funds purchased, or other potentially volatile deposits or borrowings.) Any other concentrations may be listed in the 25% category if desired. An appropriate percentage of total assets is used when a bank's capital is so low as to make its use meaningless. U.S. Treasury securities, obligations of U.S. Government agencies and corporations, and any assets collateralized by same are not scheduled.

DESCRIPTION	DETAIL	AMOUNT EXTENDED

These sample write-ups do not reflect required or preferred formats, but simply illustrate various ways to present the required analytical elements.

CORRESPONDENT BANK CONCENTRATIONS

FIRST NATIONAL BANK
Anothercity, Anotherstate

Due From Account	3,025	
Federal Funds Sold	4,000	
		7,025

- Concentration to First National Bank (FNB) represents 124 percent of Tier 1 Capital
- Aggregate monthly balances have averaged over $7 million for the past six quarters.
- Management does not formally measure or track the level of this concentration.
- Management does not perform formal financial analysis of FNB.
- Management stays abreast of the FNB's financial condition through routine business contacts and review of publicly available financial data.
- The overall health of regional banks is satisfactory.
- Credit risk is relatively low due to FNB’s current financial strength.
- Concentration risk is moderate due to a lack of formal monitoring procedures.
- Deterioration in FNB’s financial position could negatively affect daily operations as the Bank of Anytown uses the Due From FNB account to clear transactions and the federal funds sold account is a primary liquidity source.
- Policies and procedures for ensuring compliance with the Federal Reserve’s Regulation F are satisfactory; however, management has not established formal guidelines for identifying or limiting overall correspondent concentrations.

President Lincoln indicated management will develop and implement more formal correspondent bank risk management guidelines for FNB by September 30, 2016.

INDIVIDUAL BORROWER CONCENTRATION

John and Mary Smith Relationship

John and Mary Smith		
RE mortgage	400	
JMS Corporation		
JM: John and Mary Smith		
Secured commercial loans (3)	685	
Commercial letters of credit (2)	215	
J&M Realty Trust		
Gty: John and Mary Smith		
Commercial RE mortgage	650	
		1,950

The Smiths own JMS Corporation (JMS), which repairs and resells used wood pallets, and J&M Realty Trust, which holds their commercial property. This credit concentration represents 31 percent of Total Capital (TC).

The wood pallet industry is facing increased competition from the plastic pallet industry. However, JMS's recycling of scrap wood has allowed it to maintain solid sales and profitability levels to offset the effect of the increased competition. The borrowers have had a very positive, long-term credit relationship with the bank, the notes are well collateralized by diverse and marketable collateral, and the concentration poses limited risk to the bank.

The Loan Policy includes appropriate credit limits to one borrower, and management reports large credit relationships to the Board each month. However, the Smith's residential mortgage was not identified in the bank's relationship analysis and the Smith relationship has not been reported to the Board as a concentration. The most recent annual loan review for this credit relationship included adequate analysis of the economic and competitive factors that may affect this concentration's risk profile, and the internal risk rating is appropriate. However, the origination of the J&M Realty Trust mortgage on 1/2/2016, caused the outstanding balances for this relationship to exceed the AnyState legal lending limit statute; refer to the Violations of Laws and Regulations page for further discussion.

President Lincoln stated management will ensure all of the Smith's credits are addressed in concentration analysis and reported to the Board by September 30, 2016.

INDUSTRY CONCENTRATION

Shellfish Fishing Industry (NAICS Code 114112) 8,694

Identification **-** This credit concentration consists of loans to borrowers who specialize in shell fishing or the sale of customized fishing vessels and equipment. Although loans to the shell fishing industry represent 137 percent of TC, management does not measure or track the credits as a concentration of risk.

Economic and Competitive Factors **-** Management stays abreast of general factors and economic trends relating to the industry through local news reports and discussions with borrowers. However, management does not maintain a formal process for obtaining and disseminating economic, competitive, or regulatory information to the Board or loan staff. The informal process appears inadequate as management was unaware of some key factors adversely affecting the industry, such as federal efforts to reduce overfishing through lower fuel subsidies and State proposals to reduce daily catch limits and shorten permissible fishing hours.

Risk Stratification and Vulnerability Assessment **-** Most of the borrowers are fishermen that share the same fishing waters, as there are no alternative waters readily available. The collateral consists of specialized fishing vessels and equipment that are not easily converted to other purposes, thereby limiting their marketability.

Borrower cash flow is heavily influenced by catch volumes, market price, and operating costs. Although sustained demand has contributed to higher per-pound prices, lower catch volumes and higher fuel costs have reduced profitability levels and increased repayment risk associated with this industry.

Underwriting standards are heavily reliant on collateral values, with limited analysis of projected cash flows. Delinquencies remain relatively low, but have been increasing. Internal risk ratings, which appear to accurately reflect the characteristics of individual loans, have not been aggregated for analysis of the fishing portfolio. Additionally, as management does not formally monitor industry risks, there has been no analysis of the potential impact to the institution's asset quality, earnings, or capital if adverse trends continue.

Risk Management and Control Processes **-** Management relies on general loan delinquency reports and periodic discussions with borrowers to monitor loans to the fishing industry. Although the strategic plan identifies fishing as an important factor in the local economy, it does not address any of the unique risks or mitigating risk management practices associated with lending to this industry. Also, as noted above, management has not established formal procedures to identify, aggregate, or track loans to the fishing industry, and the loan policy does not address portfolio concentration limits.

President Lincoln indicated she is developing procedures for identifying, evaluating, and monitoring concentrations of fishing industry loans for presentation to the Board for review and approval by year-end 2016.

Capital Calculations		99999

COMMON EQUITY TIER 1 CAPITAL (CET1)

Common Stock and Surplus net of Treasury Stock and unearned ESOP shares	6,027	
Retained Earnings	103	
Accumulated Other Comprehensive Income	60	
Common Equity Tier 1 Minority Interest includable in Common Equity Tier 1		
Subtotal: Common Equity Tier 1 Capital Before Adjustments and Deductions		6190
Adjustments and Deductions to CET1		
Less: Goodwill net of Associated Deferred Tax Liabilities		
- Intangible Assets (other than Goodwill and Mortgage Servicing Assets), net of associated deferred tax liabilities		
- Deferred Tax Assets that arise from net operating loss and tax credit carryforwards, net of any related valuation allowances and net of deferred tax liabilities		
- AOCI-related Adjustments[1]	60	
- Unrealized net gain (loss) related to changes in the fair value of liabilities that are due to changes in own credit risk		
- All other deductions from (additions to) CET1 capital before threshold-based deductions		
- Non-significant investments in the capital of unconsolidated financial institutions in the form of common stock that exceeds the 10 percent threshold for non-significant investments		
- Significant investments in the capital of unconsolidated financial institutions in the form of common stock, net of associated DTLs that exceed the 10 percent CET1 capital deduction threshold		
- MSAs, net of associated DTLs that exceed the 10 percent CET1 capital deduction threshold		
- DTAs arising from temporary differences that could not be realized through net operating loss carrybacks, net of related valuation allowances and net of DTLs that exceed the 10 percent CET1 deduction threshold		
- Amount of significant investments in the common stock of unconsolidated financial institutions, net of DTLs; MSAs net of DTLs; and net DTAs from temporary differences that could not be realized through NOL carrybacks; that exceeds the 15 percent CET1 capital deduction threshold		
- Deductions for insufficient amounts of Additional Tier 1 and Tier 2 capital to cover deductions		
Subtotal: Adjustments and Deductions to CET1		60
Less: Assets Other than Held-for-Investment Loans and Leases Classified Loss	125	
- Additional Provision to be Transferred to Tier 2 for an Inadequate ALLL	325	
- Other Adjustments to and Deductions from Common Equity Tier 1 Capital[2]		
Subtotal: Other Adjustments and Deductions to CET1		450
Common Equity Tier 1 Capital		5,680

ADDITIONAL TIER 1 CAPITAL

Noncumulative Perpetual Preferred Stock and related Surplus		
Non-qualifying capital instruments subject to phase-out from Additional Tier 1 capital		
Tier 1 Minority Interest not included in CET1 Capital		
Subtotal: Additional Tier 1 Capital before Deductions		
Less: Additional Tier 1 Capital Deductions		
Additional Tier 1 Capital		
Tier 1 Capital		5,680

Capital Calculations (Continued)	99999

TIER 2 CAPITAL

Tier 2 Capital instruments and related surplus		
Non-qualifying capital instruments subject to phase-out from Tier 2 Capital		
Total capital minority interest that is not included in Tier 1 capital		
Allowance for Loan and Lease Losses	1,979	
Less: Held-for-Investment Loans and Leases Classified Loss	890	
Add: Additional Provision Transferred from Common Equity Tier 1 Capital	325	
Adjusted Allowance for Loan and Lease Losses	1,414	
Less: Excess Allowance for Loan and Lease Losses (If Applicable)	728	
Allowance for Loan and Lease Losses Includable in Tier 2 Capital	686	
Unrealized Gains on Available-For-Sale Equity Securities Includable in Tier 2 Capital		
Subtotal: Tier 2 Capital Before Deductions	686	
Less: Tier 2 Capital Deductions		
Tier 2 Capital		686
TOTAL CAPITAL		6,366

RISK-WEIGHTED ASSETS AND AVERAGE TOTAL ASSETS CALCULATIONS

Risk-Weighted Assets Before Deductions for Excess Allowance for Loan and Lease Losses and Allocated Transfer Risk Reserve	55,920	
Less: Excess Allowance for Loan and Lease Losses[2]	728	
Less: Allocated Transfer Risk Reserve		
Less: Risk-Weighted Asset Amounts Deducted from Capital	1,015	
Total Risk-Weighted Assets		54,177
Average Total Assets	76,803	
Less: Deductions from Common Equity Tier 1 Capital and Additional Tier 1 Capital[2]	450	
Average Total Assets for the Leverage Ratio		76,353

MEMORANDA

Capital Conservation Buffer (beginning January 1, 2016)		N/A
Securities Appreciation (Depreciation)		1,126
Contingent Liabilities/Potential Loss	130,787 / 0	

Footnotes:

(1) Includes AOCI adjustments by banks making the AOCI opt-out election and the adjustment for certain accumulated gains (losses) on cash flow hedges by banks not making the AOCI opt-out election as outlined in Part 324.

(2) Includes adjustment for financial subsidiaries as defined by the Gramm-Leach-Bliley Act of 1999, if applicable.

Comparative Statement of Income

	Period Ended 06/30/2016	Period Ended 12/31/2015	Period Ended 12/31/2014
Interest Income	2,519	5,582	7,329
Interest Expense	894	2,452	3,850
Net Interest Income	1,625	3,130	3,479
Noninterest Income	304	589	643
Total Noninterest Expense	1,467	2,902	2,904
Provision for Loan and Lease Losses	300	1,025	1,580
Securities Gains (Losses)	15	48	
Net Operating Income (Pre-Tax)	177	(160)	(362)
Applicable Income Taxes	74	(36)	(117)
Net Operating Income (After-Tax)	103	(124)	(245)
Extraordinary Credits (Charges), Net			
Net Income	103	(124)	(245)
Other Increases/Decreases	60		
Includes changes in the net unrealized holding gains (losses) on Available-For-Sale Securities			
Cash Dividends			
Net Change in Equity Accounts	163	(124)	(245)

Reconcilement of Allowance for Loan and Lease Losses

	Period Ended 06/30/2016	Period Ended 12/31/2015	Period Ended 12/31/2014
Beginning Balance	1,748	1,407	950
Gross Loan and Lease Losses	181	884	1,274
Recoveries	112	200	151
Provision for Loan and Lease Losses	300	1,025	1,580
Other Increases (Decreases)			
Ending Balance	1,979	1,748	1,407

Other Component Ratios and Trends

Ratio	Period Ended 06/30/2016	Period Ended 12/31/2015	Period Ended 12/31/2014
Net Interest Income (TE)/Average Earning Assets	4.74	4.37	4.64
Total Noninterest Expense/Average Assets	3.82	3.62	3.54
Net Income/Average Total Equity	3.39	(2.05)	(3.87)
Net Losses/Average Total Loans and Leases	.025	1.24	1.88
Earnings Coverage of Net Losses (X)	6.70	(1.19)	(1.08)
ALLL/Total Loans and Leases	3.67	3.15	2.50
Noncurrent Loans and Leases/ALLL	106.47	143.88	100.64

Footnotes:

Comparative Statements of Income and Changes in Equity Capital Accounts | 99999

ITEMS	06/30/2016	12/31/2015	12/31/2014
INTEREST INCOME:			
Interest and fee income on loans	2,185	4,826	6,305
Income from lease financing			
Interest on balances with depository institutions			
Income on Federal funds sold and repos	66	350	512
Interest from assets held in trading accounts			
Interest and dividends on securities	268	406	512
Other Interest Income			
TOTAL INTEREST INCOME	2,519	5,582	7,329
INTEREST EXPENSE:			
Interest on deposits	858	2,434	3,832
Expense on Federal funds purchased and repos	5	18	18
Other interest expense	31		
TOTAL INTEREST EXPENSE	894	2,452	3,850
NET INTEREST INCOME	1,625	3,130	3,479
NONINTEREST INCOME:			
Services charges on deposit accounts	234	461	415
All other noninterest income	70	128	228
TOTAL NONINTEREST INCOME	304	589	643
NONINTEREST EXPENSE:			
Salaries and employee benefits	750	1,422	1,342
Premises and fixed assets expense (net of rental income)	271	549	584
Amortization expense of intangible assets (including goodwill)			
Other noninterest expense	446	931	978
TOTAL NONINTEREST EXPENSE	1,467	2,902	2,904
Provision for loan and lease losses	300	1,025	1,580
Securities gains (losses)	15	48	
NET OPERATING INCOME (PRETAX)	177	(160)	(362)
Applicable income taxes	74	(36)	(117)
NET OPERATING INCOME (AFTERTAX)	103	(124)	(245)
Extraordinary credits (charges) net of income tax			
NET INCOME	103	(124)	(245)
Other increases in equity capital accounts	60		
Other decreases in equity capital accounts			
Cash dividends declared on common stock			
Net change in equity capital accounts for the period	163	(124)	(245)
Equity capital accounts at beginning of the period	6,027	6,151	6,396
Equity capital accounts at end of the period	6,190	6,027	6,151

Footnotes:

HOLDING COMPANY RATIOS AND TRENDS

	HOLDING COMPANY		
CONSOLIDATED HOLDING COMPANY	(Date)	(Date)	(Date)
Net Operating Income to Average Assets			
Total Risk-Based Capital Ratio			
Leverage Capital Ratio			
This Institution's Assets to Consolidated Holding Company Assets			
PARENT ONLY			
Pre-Tax Operating Income and Interest Expense to Interest Expense (X) (Fixed Charge Coverage)			
Operating Income - Tax + Non-Cash Items to Total Operating Expense and Dividends Paid (Cash Flow Match)			
Total Liabilities to Equity			
Equity Investments in Subsidiaries to Equity (Double Leverage)			
Equity Investment in Subsidiaries - Equity Capital/Net Income - Dividends (Double Leverage Payback in Years)			

EXTENSIONS OF CREDIT TO AFFILIATED ORGANIZATIONS

DESCRIPTION	DIRECT	INDIRECT	TOTAL
A. Affiliated organizations including securities issued by affiliated organizations.	250		250
B. Indebtedness of others, or portions of such indebtedness, collateralized by securities issued by affiliated organizations.			0
Total	250	0	250
Less duplications within and between groups			0
Net Total	250	0	250

Comments:

HOLDING COMPANY

Any Company, Inc.
Anytown, Anystate

SUBSIDIARY

Any Time, Inc.
Anytown, Anystate

OTHER AFFILIATES

Any Body, Inc.
Anytown, Anystate

Extensions of Credit to Directors/Trustees, Officers, Principal Shareholders, and Their Related Interests	**99999**

Description		**Total**
A. Executive Officers and their related interests		1,200
B. Directors/Trustees and Principal Shareholders and their related interests		250
TOTAL		1,450
Less duplications within and between groups		250
NET TOTAL		1,200
Capital and unimpaired surplus as of last Call Report date (Per Regulation "O")		7,094
Net total insider borrowing as a percentage of unimpaired capital and surplus		16.92%
NAME AND COMMENTS (Designate all duplications with a "D")	Detail	% of Unimpaired Capital & Surplus

GROUP A

LINCOLN, ALLIE C. Director and President	500	7.05%
GUTIERREZ, JOHN M. Executive Vice President and Cashier	450	6.34%
ANY BODY, INC. Duplication debt guaranteed by President Lincoln and Director Green.	250 D	3.52%
TOTAL	1,200	

GROUP B

ANY BODY, INC. A related interest of President Lincoln and Director Green. Both individuals guarantee the debt.	250 D	3.52%

Safety and Soundness

Composite 3. Financial institutions in this group exhibit some degree of supervisory concern in one or more of the component areas. These financial institutions exhibit a combination of weaknesses that may range from moderate to severe; however, the magnitude of the deficiencies generally will not cause a component to be rated more severely than 4. Management may lack the ability or willingness to effectively address weaknesses within appropriate time frames. Financial institutions in this group generally are less capable of withstanding business fluctuations and are more vulnerable to outside influences than those institutions rated a composite 1 or 2. Additionally, these financial institutions may be in significant noncompliance with laws and regulations. Risk management practices may be less than satisfactory relative to the institution's size, complexity, and risk profile. 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.

Information Technology

Composite 2. Financial institutions and service providers rated composite "2" exhibit safe and sound performance but may demonstrate modest weaknesses in operating performance, monitoring, management processes, or system development. Generally, senior management corrects weaknesses in the normal course of business. Risk management processes adequately identify and monitor risk relative to the size, complexity, and risk profile of the entity. Strategic plans are defined but may require clarification, better coordination, or improved communication throughout the organization. As a result, management anticipates, but responds less quickly to changes in market, business, and technological needs of the entity. Management normally identifies weaknesses and takes appropriate corrective action. However, greater reliance is placed on audit and regulatory intervention to identify and resolve concerns. The financial condition of the service provider is acceptable and while internal control weaknesses may exist, there are no significant supervisory concerns. As a result, supervisory action is informal and limited.

Trust

Composite 2. Administration of fiduciary activities is fundamentally sound. Generally no component rating should be more severe than 3. Only moderate weaknesses are present and are well within management's capabilities and willingness to correct. Fiduciary activities are conducted in substantial compliance with laws and regulations. Overall risk management practices are satisfactory relative to the institution's size, complexity, and risk profile. There are no material supervisory concerns and, as a result, the supervisory response is informal and limited.

Compliance

Composite 2. An institution in this category is in a generally strong compliance position. Management is capable of administering an effective compliance program. Although a system of internal operating procedures and controls has been established to ensure compliance, violations have nonetheless occurred. These violations, however, involve technical aspects of the law or result from oversight on the part of operating personnel. Modification in the bank's compliance program and/or the establishment of additional review/audit procedures may eliminate many of the violations. Compliance training is satisfactory. There is no evidence of discriminatory acts or practices, reimbursable violations, or practices resulting in repeat violations.

Community Reinvestment Act (CRA)

A CRA rating of "**Satisfactory**" is assigned. An institution in this group has a satisfactory record of helping to meet the credit needs of its assessment area, including low- and moderate income neighborhoods, in a manner consistent with its resources and capabilities.

Refer to *http://www.fdic.gov/regulations/examinations/ratings/index.html* for definitions of all composite ratings.

We the undersigned directors/trustees of Bank of Anytown, Anytown, Anystate, have personally reviewed the contents of the Report of Examination dated June 30, 2016.

Signatures of Directors/Trustees **Date**

Signatures of Directors/Trustees	Date
HENRY P. BLACK	
MICHAEL D. BROWN	
LARRY G. GREEN	
KERRY A. JONES	
ALLIE C. LINCOLN	
JAIME S. MARTIN	
JOHN D. SCOTT	
SEAN WHITE	

NOTE: This form should remain attached to the Report of Examination and be retained in the institution's file for review during subsequent examinations. The signatures of committee members will suffice only if the committee includes outside directors and a resolution has been passed by the full board delegating the review to such committee.

CONTROL AND RELATIONSHIPS

Any Company, Inc., a one-bank holding company, continues to own 100 percent of the bank's common stock. Bank directors own or control a combined 908,584 shares or 56 percent of holding company stock. President Lincoln is the largest individual stockholder, controlling 500,326 shares or 31 percent of the outstanding stock. Any Time, Inc. is a subsidiary of the bank and holds title to ORE. Any Body, Inc., is an on-premise insurance agency owned by President Lincoln and Director Green that sells credit life, auto, fire, and disability insurance. but does not utilize bank employees or equipment. President Lincoln stated that no ownership or management changes are planned. President Lincoln notified the bonding company of the nonbank activity being conducted on the premises and received an acknowledgement letter from the bonding company dated November 9, 2015. On January 20, 2016, the board of directors of Any Company reviewed the operations of Any Body, Inc., and approved its continued operations and lease of bank space for another year.

DIRECTOR INVOLVEMENT

Invitations for the bank’s directors to participate in examination discussions were extended during the pre-exam and on-site portions of the examination. Outside director involvement was limited to the Board meeting.

EXAMINATION SCOPE

Examination Number 12345

The examination scope was expanded from the pre-exam planning (PEP) memo in the following areas:

- *Construction Lending* – Expanded due to administrative problems identified in the original loan sample. Ten additional construction loans serviced by the two construction lenders and originated in 2016 were reviewed.
- *Bank Secrecy Act Review* – Expanded to include a review of all Currency Transaction Reports filed in 2016 due to indications that they were being filed late.
- *Call Report Review* – Expanded to include year-end 2015 in response to the volume of errors noted with the original review.

As a result, examination hours, totaling 760, are 150 over budget (25 percent). Other examination procedures were not modified from those identified in the PEP memo.

LOAN PENETRATION

Asset review date: 6/30/2016
Number of relationships reviewed: 55
Total $ of credit extensions reviewed / % of Total $28,148M / 52%
Total $ of non-homogenous credit extensions reviewed / % of Total $27,635M / 60%
Credit extension cutoff review point: $450M

INFORMATION TECHNOLOGY (IT) SCOPE

Examination Number 12348

The IT examination was conducted using the InTREx examination procedures (FIL-43-2016). This included an assessment of all URSIT component categories, as well as a review of Interagency Guidelines Establishing Standards for Safeguarding Customer Information, and an assessment of the institution’s cybersecurity preparedness. Findings of the IT review were discussed in detail on August 27, 2016, with President Lincoln and Information Technology Manager William Robbins.

TRUST EXAMINATION SCOPE
Examination Number 12346

The scope of the trust review included a review of policies, practices, and procedures, trust-related comments in Board minutes, the last external audit, selected accounts, compliance with applicable laws, and matters criticized at previous examinations. The account review included seven accounts.

Fiduciary activities pose limited risk to the institution. Total Trust Department assets are $3,318M held in 8 personal trust accounts, 44 burial trust accounts, and 1 farm management agency account. Department records are currently maintained manually, but Trust Officer Hancock is gradually migrating the accounts to a computerized system using Delta Data software running on a stand-alone computer.

A meeting was held on August 27, 2016, with President Lincoln and Trust Officer Hancock to discuss Trust examination findings in detail.

BANK SECRECY ACT (BSA)/ANTI-MONEY LAUNDERING (AML) REVIEW SCOPE
Examination Number 12347

Examiners reviewed the bank's compliance with the BSA and financial recordkeeping regulations. Core analysis procedures of the FFIEC's BSA/AML Manual were completed, as well as expanded procedures related to timely CTR filings, to summarize the findings of this review. Examiners compared bank records with information on the FinCEN CTR filing data report for October through December 2015, and year-to-date 2016. FinCEN 314(a) requests are being received and checked by management. BSA examination findings were discussed on August 27, 2016, with President Lincoln and BSA Officer Donna Ludlow.

OFFICE OF FOREIGN ASSETS CONTROL (OFAC) SCOPE

Examiners reviewed the bank's OFAC risk assessment, policies and procedures, independent testing of the bank's OFAC compliance program, blocked accounts, and correspondence received from OFAC. Examiners also conducted sample testing of the bank's OFAC compliance program.

UNLAWFUL INTERNET GAMBLING ENFORCEMENT ACT (UIGEA) / REGULATION GG

Examiners reviewed policies, procedures, and training materials for determining compliance with the UIGEA. The bank has identified no accounts exhibiting elevated risk and the bank has no accounts with entities that may conduct internet gambling.

SUGGESTIONS FOR FUTURE EXAMINATIONS
- There is sufficient working space for seven examiners.
- Management accommodated working hours of 7:30am to 5:30pm.
- The examination crew should contain at least one examiner with experience in construction loan analysis.
- ALERT data can only be provided in fixed-width format.

List alphabetically all directors/trustees, senior officers, and principal stockholders. Also indicate their titles. Number of shares owned is not rounded. (J – indicates stock jointly owned; P – indicates preferred stock owned; H – indicates holding company stock owned; C – indicates stock controlled but not owned)

Names and Comments	Net Worth		Year Joined Bank	Year of Birth	Atten-dance	Number of Shares Owned	Salary and Bonus (B)
	Amount	Date of Statement					

Biographical and background information on directors, officers, and other key management officials listed on this page should be prepared in accordance with the Report of Examination Instructions.

Names and Comments	Amount	Date of Statement	Year Joined Bank	Year of Birth	Attendance	Number of Shares Owned	Salary and Bonus (B)
<u>DIRECTORS/TRUSTEES</u>							
BLACK, HENRY P. Attorney *Address*	501	3/1/2015	1980	1961	12	50,992 (H)	
BROWN, MICHAEL D. Commercial RE Consultant (1) *Address*	7,890	6/1/2015	1983	1959	5	5,005 (H)	
GREEN, LARRY G. Automobile Dealership Owner (1) *Address* *Estimated by President Lincoln.	10,000	8/1/2016*	1981	1955	12	200,150 (H)	
JONES, KERRY A. Retired Doctor *Address*	2,500	6/1/2015	1979	1933	12	1,010 (H)	
LINCOLN, ALLIE C. President (1)(2) *Address*	1,357	2/1/2015	1982	1951	12	500,326 (H)	100 25(B)
MARTIN, JAIME S. Economist *Address*	3,565	3/1/2015	1981	1950	11	150,500 (H)	
SCOTT, JOHN D. Certified Public Accountant (2) *Address*	7,234	8/7/2015	1982	1954	11	101 (H)	
WHITE, SEAN Chairman of the Board (1)(2) *Address* *Estimated by Money Magazine.	5,000	6/24/2016*	1980	1960	12	500 (H)	24(B)
<u>OFFICERS, NOT DIRECTORS/TRUSTEES</u>							
COOK, LESLIE S. Executive Vice President - Commercial Lending (1)			1983	1960			85

Names and Comments	Net Worth		Year Joined Bank	Year of Birth	Atten-dance	Number of Shares Owned	Salary and Bonus (B)
	Amount	Date of Statement					
GUTIERREZ, JOHN M. Executive Vice President / Cashier (2)			1983	1958			70
PRINCIPAL SHAREHOLDERS, NOT DIRECTORS/TRUSTEES OR OFFICERS							
ANY COMPANY, INC. Anytown, Anystate						162,247	

(1) Loan Committee
(2) Investment Committee

Total Holding Company shares owned by the Directorate: 908,584
Percentage Holding Company ownership by the Directorate: 56 percent

There have been 12 regular Board meetings since the last regulatory examination.
Director fees are $250 per Board meeting attended.
Committee fees are $100 per committee attended.

INTERNATIONAL

REPORT PAGES

AND WORKPAPERS

		CATEGORY			
AMOUNT, DESCRIPTION, AND COMMENTS	Exposures Warranting Special Comment	Other Transfer Risk Problems	Substandard	Value Impaired	Loss

Argentina
October 21, 2010

All Other Exposures (including Bank Credits)				181	
Less: Credit Risk Adverse Classification				(181)	
Net Exposure				0	

In December 2009, the Argentine government defaulted on $50 billion of bonds held by foreign creditors and subsequently imposed strict capital controls that have severely limited the ability of private borrowers to service their external liabilities. Private Argentine borrowers have accumulated significant interest and principal arrears to external creditors. Prior to the present interruption of external debt service, the country had been current on payments since completing a Brady-plan restructuring of bank debt in the early 1990s. A Paris Club rescheduling in 1992 accompanied that exercise.

U.S. banks cut their exposures to Argentina sharply in 2010, reflecting both large reductions in business activity and credit lines, and significant write-offs. In June 2010, U.S. banks' cross-border exposure totaled $6.2 billion, down roughly 44 percent from a year earlier. Locally funded business fell by over two-thirds, to $3.3 billion.

A severe and extended …

Performing short-term trade credits …

Amount scheduled represents restructured trade exposure with Banco CMF, scheduled as Value Impaired (net of reserve). Amount is not extended for transfer risk as it is subject to a credit risk Doubtful classification.

Note that this write-up is incomplete. Refer to specific guidance for this page in the Report of Examination Instructions Section of the Manual.

DISCLAIMER: This page is provided for illustrative purposes only. It is not intended to correspond with or tie to information in the Bank of Anytown Report of Examination.

Management of the country risk process is regarded as generally satisfactory. Senior management and the Asset/Liability Management Committee continue to closely monitor the economic and political stability of countries where the bank maintains international transaction activity. Due to deteriorated economic and political situations in certain of the countries where the bank conducts business, there has been a reorientation of business strategy. The Board has strategically decided to focus future business development on its domestic banking market and to basically reduce its overall risk emanating from transfer risk exposure. As a result, the bank has substantially reduced the level of approved country limits, and it has "frozen" most assigned limits, and the resulting level of net transfer risk exposure. Also, the Board has reduced …

The current examination revealed five concentrations of transfer risk …

The International Policy is adequate; however, the following deficiencies …

Note that this write-up is incomplete. Refer to specific guidance for this page in the Report of Examination Instructions Section of the Manual.

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CROSS BORDER/CROSS CURRENCY CLAIMS AND CONTINGENT CLAIMS				**ADJUSTMENT FOR GUARANTEES**				
Amount Maturing in								
Less than 1 year	More than 1 year	Commitments / Contingent Claims	Subtotal by location of borrowers	Plus other credits guara- -nteed by residents in this country	Less credits externally guaranteed	Net local current assets of offices in this country	Exposure by Country of risk	Exposure by Country of risk as a % of Tier 1 capital
ARGENTINA								
981					800		181	1.00%
BRAZIL								
2,000							2,000	11.00%
DOMINICAN REPUBLIC								
1,000							1,000	6.00%
ECUADOR								
1,233					1,209		24	0.14%
GUATEMALA								
5,358					1,698		3,660	21.00%

Note: Adjustments for external guarantee represent available cash and/or ATRR. All dollar amounts are reported in thousands.

DISCLAIMER: This page is provided for illustrative purposes only. It is not intended to correspond with or tie to information in the Bank of Anytown Report of Examination.

International Loans, Acceptances, and Letters of Credit - Distribution | 99999

An international loan, acceptance, or letter of credit is defined as any such instrument between this bank and a resident or entity domiciled outside the United States, District of Columbia, Puerto Rico or other United States Territory or Possession.

DISTRIBUTION

Description	**Amount**
Mortgage loans (Including Ship loans of $_2,327______)	8,732
Loans insured or guaranteed by the U.S. government or its agencies	14,065
Loans to foreign governments, agencies thereof and central banks	15.971
Loans to financial institutions other than central banks	500
Loans to commercial, industrial and agricultural interests	41,689
Other Loans (Describe) Loans to religious institutions	8,572
All other loans	1,171
Total International Loans*	90,700
*Does NOT include loans to U.S. subsidiaries of foreign corporations	12,444

Description	Amount
Participation loans and paper purchased	41,505
Placed paper, direct loans and participation loans sold	5,365
Syndication and consortium financing	5,000
International acceptances outstanding	1,489
International letters of credit outstanding	7,836
Other (Describe)	

1. **Are duties and responsibilities for the conduct of international operations clearly defined? Comment briefly.**

   Yes. The bank's Board of Directors has a written policy statement setting forth the various duties and responsibilities of the operating entities within the international division.

2. **Does the bank have a definite international lending policy? If "yes", summarize such, state whether it has been approved by the board of directors/trustees, and indicate extent of compliance.**

   Yes. The subject bank's Board of Directors, in line with the directives of the parent bank, has delineated specific guidelines on clientele to be served, limits on country exposure both in the aggregate and by maturity within those limits and risks to be undertaken. Officers submit recommendations to the international loan committee which has authority to approve loans up to $5 million. Larger loans require senior loan committee approval. In all cases, these policies have been followed.

3. **(a) Comment upon policy guidelines in effect regarding country risk assets and volume limitations imposed thereon. (b) How often are guidelines reviewed? (c) Does the bank have any country risk concentrations of credit? If "yes", list the country and percentage of such extensions of credit to the bank's total capital and reserves.**

   (a) Policy calls for all extensions of credit including bank placements, formal loan commitments, and foreign exchange lines to be included within country limits. Claims are reallocated to the country of guarantor or the country where collateral is realizable. Sub-limits are provided by maturity of the obligation. Separate limits are provided for in each of the 15 countries where lending is permitted.

   (b) Reviewed quarterly.

   (c) Yes, Japan 84%, France 40%, Federal Republic of Germany 59%, United Kingdom 39%.

4. **Are guarantees of other banking institutions and/or parent or affiliated organizations of borrowers required on certain loan obligations? If "yes", under what circumstances and in what form are such guarantees extended?**

   Yes. Letters of Guarantee from two European banks have been furnished as support to financially weak borrowers. The parent bank has extended guarantees in the form of letters of credit essentially to provide additional protection to the subject bank's position. The parent's guarantee was not relied upon as a primary source for repayment of the loan.

5. **(a) Describe the general nature and character of collateral pledged, and (b) comment upon the adequacy of supporting documentation.**

   (a) Collateral includes first preferred ship mortgages, notes and bond obligations of various foreign governments, time deposits, commodities, stocks, and UCC filings.

(b) Supporting documentation appeared in order.

6. Is credit information timely in content and available in sufficient readable detail?

Credit information on loans originated at the Nassau Branch continues to be inadequate. Deficiencies include a lack of current and complete financial information on the obligor and guarantor, an absence of thorough credit analysis, and a lack of complete information on country conditions.

7. (a) Describe the general nature and types of acceptance financing extended, and (b) the general lines of business involved.

(a) Bank is primarily involved in acceptance financing in connection with international trade activity; several million dollars in dollar exchange acceptances were booked between examinations.

(b) Manufactured goods, commodities, and exchange activities of central banks.

8. (a) Describe the general nature and types of letter of credit accommodations offered, and (b) the general lines of business involved.

(a) The bank issues documentary letters of credit to importers, confirms other banks' letters of credit for export customers and, to a limited extent, engages in deferred payment letter of credit financing. Standby letters of credit are undertaken only for prime customers.

(b) Manufacturers, machinery exporters and importers, commodity importers, and foreign governments and agencies.

9. Describe the provision for repayment of (a) acceptances, and (b) drafts drawn under letters of credit. Include comment regarding extent of refinancing.

(a&b) Provisions for repayment are arranged prior to issuance and vary as individual conditions warrant. Repayment is generally accomplished by charge to customer's account or by loan accommodation under approved credit lines in the case of acceptances and by charge to the customer's account or acceptance with respect to letters of credit. In certain situations, refinancing is permitted, generally for short periods.

1. Comment on the general nature and volume of present eurocurrency operations.

Eurocurrency operations are conducted through the Nassau Branch. Investments are primarily loans to South American corporations and central governments, securities of foreign governments and bank placements. Sources of funding are IPC, bank and affiliate time deposits. At examination date, Eurocurrency loans, securities, and bank placements totaled $325 million with $285 million funded by Eurocurrency time deposits and the remainder through main office funds.

2. Describe the procedures followed and guidelines utilized in establishing lines of credit and making and approving due to (takings) and due from (placements). Comment on the adequacy of procedures enabling senior management to ascertain compliance with guidelines and directives.

The parent bank has issued general guidelines to be considered before establishing lines of credit and bank relationships. With respect to banks, these criteria center on the obligor's capital resources, country risk, and type of institution. Bank and nonbank clientele analysis includes consideration of volume and maturity factors, as well as a review of financial responsibility and reputation. Senior management receives weekly reports.

3. (a) Comment on the maturity composition of present eurocurrency takings and placements and the effect of such on the bank's liquidity position. (b) Are asset and liability maturities reasonably matched?

(a) At examination date, Eurocurrency takings totaled $285 million, while placements aggregate $195 million. All placements and 74% of takings ($210 million) mature within 90 days with no adverse effects on the bank's liquidity position.

(b) Both near-term and longer-term maturities are reasonably matched.

4. Are all interbank placements confirmed at inception and, thereafter, subject to periodic direct verification audits?

Yes.

Foreign Exchange Activities	**99999**

NOTE: A negative answer below (questions 2 through 8(e)) may be indicative of a condition in need of correction. Such answers may call for comment, or expanded treatment, below or elsewhere in the examination report.

	DESCRIPTION	YES	NO
1.	Is the bank engaged, in any manner, in foreign exchange activities? If "Yes", answer the following questions:	X	
2.	Is the net open position of each foreign currency reasonable in relation to the bank's total capital and reserves?	X	
3.	Is the aggregate net open position of all foreign currencies reasonable in relation to the bank's total capital and reserves?	X	
4.	Are the future maturities of foreign currency assets, liabilities, and contracts reasonably matched with respect to long and short positions in all time periods?	X	
5.	Does a current revaluation of the bank's foreign currencies reflect an insignificant profit or loss?	X	
6.	Has the directorate and/or head office imposed reasonable guidelines and limits with respect to foreign exchange operations?	X	
7.	Are guidelines and limits being adhered to by active management?	X	
8.	With respect to foreign exchange operations, are the following adequate:		
	(a) recording procedures?	X	
	(b) bookkeeping procedures other than 8(a)?		X
	(c) contract confirmation procedures?	X	
	(d) internal routines and controls other than 8(c)?	X	
	(e) audit procedures?	X	

8(b) Refer to comments under Audit and Internal Controls.

Position Analysis - Major Currency Positions | 99999

Country United Kingdom	**Monetary Unit Pound Sterling**			
Description	Assets and Purchases (Long Position)		Liabilities and Sales (Short Position)	
	Foreign Currency	U.S. Dollar Book Value	Foreign Currency	U.S. Dollar Book Value
Cash	1,000	2,600		
Demand Balances Due (Nostro)	50,000	19,800		
Loans	1,000,000	2,500,000		
Securities	100,000	275,800		
Deposits of Banks (Vostro)			100,000	242,000
Other Deposits			400,000	1,040,000
Spot Contracts	1,300,000	3,120,000	1,400,000	3,346,000
Forward Contracts				
Holdovers				
Other: (Specify) Accrued Interest Receivable	10,500	25,200		
Accrued Interest Payable			3,000	7,200
Gross Position	2,461,500	5,943,400	1,903,000	4,635,200
Less: Long/Short	1,903,000	4,635,200		
Net Position	558,500	1,308,200		
Net position as a % of the bank's total capital and reserves:	2.90%			

OTHER CURRENCIES

Country	Monetary Unit	Long		Short		Net Position		(%)*
		Foreign Currency	U.S. Dollar Book Value	Foreign Currency	U.S. Dollar Book Value	Foreign Currency	U.S. Dollar Book Value	Net Position
Australia	Dollar	24,600	27,900			24,600	27,900	0.06%
Canada	Dollar	66,000			90,000	66,000	(90,000)	0.20%
France	Franc	1,000,000	210,000			1,000,000	210,000	0.47%
Germany	Mark	693,000	215,000	203,000	61,000	490,000	154,000	0.34%
Italy	Lire	27,873,600	30,500	54,344,500	59,500	(26,470,900)	(29,000)	0.06%
Switzerland	France					0	0	0.00%
Subtotal (U.S.)						0	536,200	0.00%
Plus: Major Currency (U.S.)							1,308,200	
Aggregate Position (U.S.)						0	0	
* as a percentage of the bank's Total							1,844,400	3.88%
Capital and Reserves.								

DESCRIPTION	YES	NO
1a. Is the net open position of each foreign currency reasonable in relation to the bank's total capital and reserves?	X	
1b. Is the aggregate net open position of all foreign currencies reasonable in relation to the bank's total capital and reserves?	X	

Maturity Distribution (GAP) Analysis	**99999**

MATURITY DISTRIBUTION SCHEDULE

Monetary Unit	**Maturity Dates**	**Assets and Purchases Long**	**Liabilities and Sales Short**	**Net Gap for Period Long/Short**	**Spot Rate P = Prem. D = Disc.**	**Profit**	**Loss**
		F.C.	F.C.	F.C.		U.S.	U.S.
Pound (UK)	5/15	51,000	100,000	(49,000)			
	5/16	25,000		25,000			
	5/17	25,000		25,000			
	5/18	35,000		35,000			
	5/19	50,000	40,000	10,000			
	5/22		50,000	(50,000)			
	5/23	50,000	75,000	(25,000)			
	5/24	100,000	50,000	50,000			
	5/25	50,000		50,000			
	5/30	50,000	75,000	(25,000)			
	5/31		100,000	(100,000)			
	June	110,500	100,000	10,500			
	July	125,000	203,000	(78,000)			
	August	175,000	110,000	65,000			
	September		75,000	(75,000)			
	October	245,000	225,000	20,000			
	November	175,000	100,000	75,000			
	December	325,000	200,000	125,000			
	20X6	370,000	300,000	70,000			
	20X7	150,000	50,000	100,000			
	20X8	250,000	50,000	200,000			
	After	100,000		100,000			
	TOTALS	2,461,500	1,903,000	558,500		0	0
					Less: Profit/Loss		
					Future Adjustment	0	0
						YES	**NO**
2. Are future maturities of foreign assets, liabilities, and contracts reasonably matched with respect to long and short positions in all time periods?						X	

Revaluation and Income/Loss Analysis	99999

Monetary Unit	Book Value of F.C.	Net Position U.S.	Exam Date Spot Rate	Current U.S. Market Value (F.C. x Spot)	U.S. Spot Rate Profit (Loss)	U.S. Future Profit (Loss) Adjustment	U.S. Net Profit or (Loss)
Australia $	24,600	27,900	1.149500	28,300	400		400
				0	0		0
Canada $	66,000	(90,000)	0.868300	57,300	147,300	(500)	146,800
				0	0		0
France Franc	1,000,000	210,000	0.219100	219,100	9,100		9,100
				0	0		0
German Mark	490,000	154,000	0.493800	242,000	87,700		87,700
				0	0		0
Italian Lira	(26,470,900)	(29,000)	0.001176	(31,100)	(2,100)		(2,100)
				0	0		0
Swiss Franc	(60,700)	(25,300)	0.532800	(32,300)	(7,000)		(7,000)
				0	0		0
UK Pound	558,500	1,308,200	2.222000	1,241,000	(67,200)	1,000	(66,200)
				0	0		0
				0	0		0
				0	0		0
				Total	168,200	500	168,700

Does not include $ profit (loss) attributable to outstanding SWAP transactions

$ has already been taken into income/expense through accrual accounting

	YES	NO
3. Does a current revaluation of the bank's foreign currencies reflect an insignificant profit or loss?	X	

Income/Loss Schedule	**99999**

Previous Calendar Year	**Amount or Percent**
Quarterly Average of Gross Assets	562,500,000
Total Foreign Exchange Income	1,000,000
Net Foreign Exchange Income (Loss)	550,000
% of Total Foreign Exchange Income to Average Gross Assets	0.18%
% of Net Foreign Exchange Income (Loss) to Average Gross Assets	0.10%
Year to Date	**Amount or Percent**
Total Operating Income (Bank)	25,156,300
Net Operating Income (Loss)	4,192,700
Total Foreign Exchange Income	735,200
Net Foreign Exchange Income (Loss)	404,400

1. (a) Describe the net and aggregate position limits, maturity exposure limits, and any other limits placed on foreign exchange operations by the board of directors/trustees. (b) Do such limits appear reasonable?

(a) The bank's Board of Directors has authorized trading only in these currencies listed in the position schedules. Overnight limits for each currency with the exception of the pound sterling are fixed at $250M; pound sterling limit is $1,500M. The aggregate position limit for all currencies is $2,000M. Maturity gaps are authorized only on major active currencies up to $100M not to exceed 3 months. Major active currencies have been described as having an active forward market. No general ledger account limits have been formulated.

(b) Limits appear to be reasonable.

2. Describe the limits and guidelines established by the board of directors/trustees for dealing in foreign exchange with other banks and customers.

Individual customer limits are approved by the bank's International Committee based on the customer's creditworthiness and the volume of its foreign currency needs. The bank's written internal credit policy pertaining to bank and nonbank customer foreign exchange lines is:

(a) 100% of foreign exchange line may mature within 180 days;
(b) 50% of the foreign exchange line may mature within 360 days;
(c) 20% of the foreign exchange line is available for contracts with maturities up to 18 months;
(d) no maturities may exceed 18 months.

Excesses must be approved in writing by the account officer who approved the customer line. Maximum daily delivery risk limits per customer are set at 20% of the aggregate limits approved.

3. Fully describe any recent significant deviations by the bank from established limits and guidelines. Include in this description any significant deviations noted after completion of the Position Analysis, and the Maturity Distribution (GAP) Analysis.

No deviations from bank policy were noted in preparing the position analysis. Two exceptions to bank policy on GAP exposure were in evidence due to an inability to obtain forward cover. These exceptions were approved by the International Committee. No other recent deviations from policy were uncovered.

4. (a) Describe the reports (i.e., position maturity, gap, revaluation, etc.) required by the directorate and senior management to ascertain compliance with directives. (b) Is the directorate or senior management notified when actions are taken which constitute deviation from policy? If "Yes", describe the approval procedures for such deviations from policy.

(a) Net position reports enumerating all foreign currency balance sheet items, future contracts, and after-hour and holdover transactions are transmitted to the designee of the International Committee on a daily basis. Reports are prepared by the foreign exchange bookkeeping department and reconciled to the trader's blotter. Maturity gap reports are produced daily with the next month's transaction reflected on a daily basis and subsequent transactions grouped in two-week intervals. Revaluation reports detailing ledger accounts, spot contracts, and forward contracts are developed on a weekly basis.

(b) Bank's written policy provides for the immediate generation of exception reports where applicable limits are exceeded. Prior written approval of account officer is required for deviation from customer limits. Deviation from other limits is not permitted under any circumstances without prior approval of International Committee.

5. If the bank is a subsidiary of a foreign bank, (a) what controls and guidelines has the parent imposed on the bank's foreign exchange activities? (b) Describe the foreign exchange reports prepared by the bank for the parent.

(a&b) The aforementioned guidelines and limits have been implemented at the direction of the parent bank. All reports of the bank's audit department and the reporting mechanisms described in 4(a) are furnished to the parent bank for review.

6. How frequently and by whom is the foreign exchange position revalued? Briefly describe the procedures used in the revaluation. If forward contracts are not revalued at future rates, so indicate.

Revaluation is performed on a bi-weekly basis by the International Operations section. Actual realized profit or loss is calculated by applying current spot rates to balance sheet accounts, as well as contracts of very near maturities. Unrealized profit or loss on future transactions is determined by utilizing the appropriate forward rates to the net position for each future period in the bank's gap report.

7. Describe the general ledger accounts affected by the periodic revaluation and the journal entries used to effect changes in these accounts. If any accounts are being used to capitalize losses or defer immediate recognition of profit, so indicate.

Actual realized profit or loss is charged to the profit and loss account with offsetting entries to the applicable local currency ledger accounts. With respect to future transactions, the bank charges "estimated profit(loss) on foreign exchange futures" account for the amount of the adjustment with an offset to the profit and loss account. Profits and losses are recognized at the date of revaluation.

8. (a) Approximately what volume of the bank's foreign exchange dealings are with related companies or banks? (b) In what manner, if any, do the terms and conditions of such dealings vary from similar transactions with non-related companies and banks?

(a) During 2011, the bank entered into approximately $40,000M of forward contracts to purchase and sell foreign exchange with a related bank, First European Bank, London, England.

(b) Terms and conditions of contracts are substantially the same as transactions with non-related parties.

9. Regarding holdover and/or after hour transactions, (a) describe the bank's system for controlling and recording such transactions and (b) indicate how management is informed of such transactions before recordation. (c) Does the system appear to be correctly designed and adequately controlled?

(a-b-c) The foreign exchange control group prepares a list of holdover items. Holdover items are incorporated into the daily position sheet, which together with the holdover list, is furnished to management on a daily basis. Holdover items are posted as of the dates contracted. The system is considered adequately controlled.

NOTE: A negative answer below indicates a condition which may be in need of correction. Such answers may call for comment below and elsewhere in the regular examination report.

AUDIT

			YES	NO
1.		Have the directors/trustees made provision for an audit of the foreign exchange area?	X	
		If "Yes," indicate method utilized:		
	X	Employment of full time auditor.		
	X	Periodic employment of independent auditor.		
		Designation of an audit supervisor and an established program of internal audit by bank personnel.		
		Name of Audit Supervisor:		
2.		If the answer to question 1 is "yes", does the audit program include the following:		
	(a)	Periodic proof of forward and spot contracts?	X	
	(b)	Periodic proof and/or reconcilement of foreign exchange general ledger accounts?	X	
	(c)	Periodic direct verification of forward and spot contracts? Frequency: Annually Amount: $25,200,000	X	
	(d)	Review of management reports and adherence to guidelines?	X	
	(e)	Comparison of rate quotations in management reports and revaluations with outside sources?	X	
	(f)	Perusal of authorized signatures?	X	
	(g)	Briefly describe any other audit procedures conducted:		
3.		If applicable, has the bank corrected major criticisms noted in the last independent audit report? Date of audit: 12/31/2011		X
		Briefly describe major criticisms and/or recommendations in such report: The bank was criticized for not maintaining a complete and current set of instructional memoranda describing the information generated from the accounting system and the general and subsidiary ledger accounts affected by trading activity. This defect has been corrected. Deficiencies still exist with respect to confirmation procedures.		
4.		Is the foreign exchange audit program adequate as to scope and frequency?	X	
5.		Does the foreign exchange auditor or audit supervisor report regularly and directly to the bank's board of directors/trustees or a committee thereof?	X	
6.		Is a written audit report of the foreign exchange area maintained by the bank?	X	

2(c) All outstanding spot and forward contracts as of the audit date are directly verified.

NOTE: A negative answer below indicates a condition which may be in need of correction. Such answers may call for comment below and elsewhere in the regular examination report.

INTERNAL CONTROLS		YES	NO
7.	Are all contracts recorded on the date contracted?	X	
8.	Is it a firm rule that all forward and spot contracts be confirmed at inception?	X	
9.	Has the bank instituted an effective and current (within seven days) follow-up system regarding unconfirmed and/or incorrectly confirmed forward and spot contracts?		X
10.	Are foreign exchange contracts and dealing slips prenumbered and used in such order?	X	
11.	Does the bank have an effective system of controls over the trader and the trading environment?	X	
	A "Yes" answer to this question will necessarily require a "Yes" answer to each of the following (as a minimum). Is it a firm rule that:		
	(a) The trader not be allowed to receive confirmations on forward and spot contracts?	X	
	(b) The trader not be allowed to sign contracts?	X	
	(c) The trader be prohibited from initiating and receiving interbank funds transfers, opening current accounts, or receiving credits to current accounts?	X	
	(d) The trader not be involved in the revaluation procedure?	X	
	(e) Trading activities be segregated from other bank activities, in particular the accounting, confirmation, and report functions?	X	

8-9 Although the bank has a firm rule regarding the confirmation of spot and future contracts, it was observed that outgoing confirmations are frequently incomplete, with dates of trade and value dates frequently omitted. Further, the confirmation exception log is haphazardly prepared and is not reviewed by an operations officer. These deficiencies were noted by both the bank's internal and external auditors; however, correction is yet to be effected. It is recommended that these areas of potential exposure be remedied at an early date.

DISCLAIMER: This information is provided for illustrative purposes of a complex PBO. It does not correspond to the ownership/control information provided in the Bank of Anytown.

List the following information for the bank(s) and/or bank holding company(s) in the PBO.

U.S. Name: Demo International Bank[1]
City, Country: Miami, FL
Number of Outstanding Shares: 1,000,000

Foreign Name: Demo International, C.A.
City, Country: Caracas, Venezuela
Number of Outstanding Shares: 50,000

Foreign Name: Demo Bank Venezuela[2]
City, Country: Caracas, Venezuela

Foreign Name: Demo Bank Brazil[3]
City, Country: Rio de Janeiro, Brazil

Foreign Name: Demo Bank Mexico
City, Country: Mexico City, Mexico
Number of Outstanding Shares: 100,000

[1] Of the ten entities that comprise the PBO, only the three foreign banks and the foreign bank holding company that actively engage in transactions with Demo International Bank, Miami, Florida are detailed above. The remaining five entities within the PBO structure include: JMM Holdings, Caracas, Venezuela which wholly-owns Demo Bank International, Panama City, Panama; Mendosa Finance Company, Caracas, Venezuela which wholly-owns Demo Bank International, Cartegena, Colombia and Demo Bank International, Bogota, Colombia.

[2] Wholly-Owned subsidiary of Demo International, C.A., Caracus, Venezuela.

[3] Wholly-Owned subsidiary of Demo Bank Venezuela, Caracas, Venezuela.

Detail the stock owned by the beneficial owner(s) whose direct/indirect control forms the nexus of the PBO.

U.S. Name: Demo International Bank	**Number of Shares**	**Percent Owned**	**Type of Control**
Beneficial Owner: Mendosa Family Trust (Jose Mendosa controls 100%)	750,000	75.00%	Direct
Beneficial Owner: Rivera Family Trust (Juan Rivera controls 100%)	250,000	25.00%	Direct

Foreign Name: Demo International, C.A.	**Number of Shares**	**Percent Owned**	**Type of Control[1]**
Beneficial Owner: Jose M. Mendosa	5,000	10.00%	Direct
Beneficial Owner: Carlita S. Mendosa	12,500	25.00%	Direct
Beneficial Owner: Paco M. Mendosa	7,500	15.00%	Direct
Beneficial Owner: Juan H. Rivera	12,500	25.00%	Direct
Beneficial Owner: Mendosa Family Members	12,500	25.00%	Direct

[1] Mr. Jose M. Mendosa has indirect control of the shares owned by his wife, Ms. Carlita S. Mendosa.

Foreign Name: Demo Bank Mexico	**Number of Shares**	**Percent Owned**	**Type of Control[1]**
Beneficial Owner: Jose M. Mendosa	50,000	50.00%	Direct
Beneficial Owner: Carlita S. Mendosa	25,000	25.00%	Direct

[1] Mr. Jose M. Mendosa has indirect control of the shares owned by his wife, Ms. Carlita S. Mendosa.

Discuss the factor(s) or combination of the attributes (besides or in addition to common stock ownership) that was considered in determining that sufficient control is exercised to conclude that a PBO relationship exists, including whether the individual, family or group of persons acting in concert:

1) **Constitutes a quorum or a significant presence on the Board of Directors of both the U.S. depository institution and the foreign bank or the foreign bank holding company.**

The members of the Mendosa family listed above serve as the chairman, vice chairman or director for the five foreign entities except that none of them are on the Board of Demo Bank Guatemala. Their membership does not constitute a quorum on any of the three foreign or the U.S. banks' Board, but does constitute a quorum on the Board of the foreign bank holding company, Demo International, C.A.

2) **Controls, in any manner, the election of a majority of the directors of the U.S. depository institution and the foreign bank or the foreign bank holding company.**

The minutes of the shareholder meeting for the election of the directorate for Demo Bank Venezuela were not available for review. However, it is believed that Mr. Jose Mendosa and his family members controlled the election through their ability to vote a majority of the holding company's stock. Mr. Jose Mendosa's ability to vote the majority of Demo International Bank's stock indicates that he controlled the election of its directorate.

3) **Constitutes a quorum or a significant portion of the executive management of both the U.S. depository institution and the foreign bank or the foreign bank holding company.**

   The members of the Mendosa family listed above serve as the president, vice president or cashier of Demo International Bank, Demo International, C.A. and at the four foreign banks except Demo Bank Guatemala. Their positions constitute a quorum of the executive management at Demo International, C.A., but not at the three foreign banks or at the U.S. bank. However, they occupy critical positions on those teams.

4) **Exercises a controlling influence over the management and/or policies of both organizations.**

   Mr. Jose Mendosa's position as chairman of Demo International Bank and as president of Demo Bank Venezuela enables him to exert a controlling influence over the management and policies of both organizations.

5) **Engages in an unusually high level of reciprocal correspondent banking and/or other transactions or facilities between the U.S. depository institution and the foreign bank.**

   The institutions primarily engage in correspondent bank services, dollar clearings, letters of credit, and trade related transactions. Fee income from transactions with the three foreign banks accounts for slightly over 40 percent of the total fee income generated by Demo International Bank, Miami, Florida in 2011. The U.S. bank also extended a $5 million line of credit secured by a $5 million certificate of deposit to Demo Bank Venezuela, Caracus, Venezuela.

6) **Obtains financing to purchase the stock of either the U.S. depository institution or the foreign bank or the foreign bank holding company from, or arranged by, the foreign bank, especially if the shares of the U.S. depository institution are collateral for the stock-purchase loan.**

   None noted.

7) **Requires the U.S. depository institution to adopt particular/unique policies or strategies similar to those of the foreign bank, such as common or joint marketing strategies, cross-selling of products, sharing of customer information, or linked web sites.**

   The Demo International Bank's web site is linked to Demo Bank Venezuela's web site. Both offer similar loan and deposit products and banking services.

8) **Names the U.S. depository institution in a similar fashion to that of the foreign bank.**

   The titles of the banking organizations use similar naming conventions.

9) Presents any other factor(s) or attribute(s) that impacted the conclusion.

None known.

Summarize the Examination's Findings, including any concerns and criticisms relative to the PBO.

The review determined that a PBO relationship exists between Demo International Bank and three foreign banks and a foreign bank holding company through the common control of the Mendosa family, primarily through Mr. Jose Mendosa's ownership/control of the Demo International Bank in Miami, Florida, Demo International, C.A. (foreign bank holding company), and Demo Bank Mexico in Mexico City, Mexico.

Bank management acknowledges that the institutions are under common control. Management actively monitors all transactions with affiliated entities. No adverse trends were noted except that management was encouraged to devote additional time to review the banks' heightened wire activity. Refer to the Related Organizations page and the Risk Management Assessment page for additional information.

If a PBO relationship exists, then the field supervisor or case manager should forward this document under a cover letter to the Associate Director of the International and Large Bank Branch.