



# Audit Report



OIG-09-026

Audit of the Office of the Comptroller of the Currency's  
Fiscal Years 2008 and 2007 Financial Statements

January 8, 2009

Office of  
Inspector General

Department of the Treasury



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

OFFICE OF  
INSPECTOR GENERAL

January 8, 2009

**MEMORANDUM FOR JOHN C. DUGAN  
COMPTROLLER OF THE CURRENCY**

**FROM:** Michael Fitzgerald /s/  
Director, Financial Audits

**SUBJECT:** Audit of the Office of the Comptroller of the Currency's  
Fiscal Years 2008 and 2007 Financial Statements

I am pleased to transmit the attached audited Office of the Comptroller of the Currency (OCC) financial statements for fiscal years 2008 and 2007. Under a contract monitored by the Office of Inspector General, GKA, P.C. (GKA), an independent certified public accounting firm, performed an audit of the financial statements of OCC as of September 30, 2008 and 2007 and for the years then ended. The contract required that the audit be performed in accordance with generally accepted government auditing standards; applicable provisions of Office of Management and Budget Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*; and the *GAO/PCIE Financial Audit Manual*.

The following reports, prepared by GKA, are incorporated in the attachment:

- Independent Auditor's Report on Financial Statements;
- Independent Auditor's Report on Internal Control over Financial Reporting; and
- Independent Auditor's Report on Compliance with Laws and Regulations

In its audit of OCC's financial statements, GKA found:

- that the financial statements were fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America,
- no matters involving internal control and its operations that are considered material weaknesses, and
- no instances of reportable noncompliance with laws and regulations tested.

GKA also issued a management letter dated October 31, 2008, discussing certain matters involving internal control over financial reporting and its operation that were identified during the audit but were not required to be included in the auditor's reports. This letter will be transmitted separately.

In connection with the contract, we reviewed GKA's reports and related documentation and inquired of its representatives. Our review, as differentiated from an audit in accordance with generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on the financial statements or conclusions about the effectiveness of internal control or compliance with laws and regulations. GKA is responsible for the attached auditor's reports dated October 31, 2008 and the conclusions expressed in the reports. However, our review disclosed no instances where GKA did not comply, in all material respects, with generally accepted government auditing standards.

Should you have any questions, please contact me at (202) 927-5789 or a member of your staff may contact Ade Bankole, Manager, Financial Audits at (202) 927-5329.

Attachment



Comptroller of the Currency  
Administrator of National Banks

US Department of the Treasury

# *Office of the Comptroller of the Currency*

**ANNUAL REPORT**

Fiscal Year 2008



## OCC VISION

**T**he Office of the Comptroller of the Currency (OCC) seeks to assure a banking system in which national banks soundly manage their risks, comply with applicable laws, compete effectively with other providers of financial services, offer products and services that meet the needs of customers, and provide fair access to financial services and fair treatment of their customers.

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# OCC Offices Are Located Around the Country



**Figure 1: Statistical Profile of the OCC's Fiscal Year 2008**

Number of Total Employees	3,122
Number of National Bank Examiners	2,079
Number of Safety and Soundness Examinations Conducted	1,266 <sup>1</sup>
Number of Specialty Examinations Conducted	630
Number of Consumer Assistance Personnel	48
Number of Written Consumer Complaints Processed	41,656
Total Revenue	\$736.1 million <sup>2</sup>
Percentage of Revenue Derived from Assessments	96.1%

Source: OCC data for fiscal year 2008.

<sup>1</sup> Large and Midsize national banks receive continuous supervision.

<sup>2</sup> Ninety-six percent of OCC revenue is derived from assessments.

**Figure 2: Statistical Profile of the National Banking System**

Number of National Banks	1,678
Percentage of Total Commercial Banks	20%
Number of Uninsured National Trust Companies	73
Number of Federal Branches of Foreign Banks	49
Assets of National Banks (excluding Federal Branches of Foreign Banks)	\$8.3 trillion
Percentage of Total U.S. Commercial Banking Assets	62%
Total Insured Deposits	\$4.886 trillion
Number of Employees of National Banks	1,247,143
Community Development Investment Authority	\$3.7 billion

Source: OCC, 2008.



# Comptroller's Viewpoint

**F**or the financial system, both here and abroad, the fiscal year that ended September 30 was without question the most extraordinary of my lifetime. In fact, when I look back on all that has happened since we published our last annual report, I am struck by the sheer number of events involving severe credit and market stress, any one of which could have been the most serious financial problem of the year in the much quieter period before 2007.

Just naming the worst of them is both telling and exhausting. The first annual decline in nationwide house prices. Record foreclosure levels. Brutal losses on subprime loans. The near shutdown of interbank lending markets and the liquidity freeze for asset-backed commercial paper and structured investment vehicles, or SIVs. The government takeover of Fannie Mae and Freddie Mac. The failure of Lehman Brothers, IndyMac, and WaMu. The distress sales of Countrywide to Bank of America, Bear Stearns to JPMorgan Chase, and Wachovia to Wells Fargo. The administration plan to use \$700 billion to unfreeze the credit markets.

Could all of these major financial events have really happened in just one year? The answer, of course, is yes. In fact, many of the most dramatic of them happened in just over a month. In reflecting on this “100-year flood,” let me provide a few observations from the perspective of the OCC.

First, national banks took important steps to strengthen their positions. Large banks that experienced difficulties responded by aggressively raising capital to shore up their balance sheets, attracting well over \$100 billion. As a result, virtually all national banks continued to satisfy the definition of “well capitalized” on September 30. Banks of all sizes have rapidly increased loan loss reserves to address the spike in troubled loans—in some cases to unprecedented levels. While fiscal 2008 was a difficult year with many tense moments, we should not lose sight of these very tangible positive signs amid the steady drumbeat of negative news.

Second, despite the unprecedented nature of these events, the OCC anticipated many of them before they occurred and dealt with them once they arrived. We sounded early public warnings in guidance and speeches about risk layering, payment shock, and declining underwriting standards for “payment option” mortgages and home equity lending. Our higher standards for subprime mortgage underwriting kept most of that lending out of national banks. The subprime loans that national banks did make were generally of higher quality than those originated elsewhere.

For commercial real estate (CRE) concentrations in community banks, we conducted rigorous horizontal reviews in each of the four OCC districts starting in 2004; we pushed hard for the CRE guidance subsequently issued in 2006 over industry opposition; and we delivered our messages again and again in speeches, outreach meetings, and examinations all over the country.

Our annual underwriting surveys repeatedly spotlighted the trend of declining underwriting standards, particularly with respect to leveraged loans. We also recognized early on that community bank failures would accelerate in 2008; we talked about that publicly; and we planned for it. Distressed institutions—large and small—have demanded far more attention and supervision than normal, and at times, tensions have run high. OCC examiners stepped up to each unfolding event with speed, maximum effort, and teamwork. We needed the best from our examiners, and they delivered. It is no accident that banks have gotten more realistic about recognizing delinquency and loss; raised significant amounts of capital when they could; aggressively built loan loss reserves and agreed to tangible actions that would fundamentally improve their risk management. It is an examiner’s job to get banks to take these sometimes painful steps to





# Members of the Executive Committee

**John C. Dugan**  
Comptroller of the Currency



**Thomas R. Bloom**  
Senior Deputy  
Comptroller for  
Management  
and Chief  
Financial Officer



**Jennifer C. Kelly**  
Senior Deputy  
Comptroller for  
Midsize/Community  
Bank Supervision



**Mark Levonian**  
Senior Deputy  
Comptroller for  
Economics



**Timothy W. Long**  
Senior Deputy  
Comptroller and  
Chief National  
Bank Examiner



**Bajinder N. Paul**  
Chief Information  
Officer

improve their safety and soundness, but it has not always been easy.

The OCC has also initiated new data gathering to help address the recent problems. Perhaps the best example is our Mortgage Metrics project. An unprecedented effort accomplished in record time, this project gathered loan level data on over 40 percent of the mortgages serviced in the United States. Importantly, the data are both standardized and validated. We now know much more than we once did about trends in delinquency, modification, and foreclosure with respect to prime, subprime, and Alt-A mortgages, and we have begun to use that data in a variety of ways to support our supervision and our efforts to mitigate the impact of the economic crisis on homeowners. We have also begun to develop similar metrics for home equity and credit card lending, and we think that data, too, will prove very important to our supervision and our consumer protection initiatives.

But there were some problems we clearly did not anticipate, and we need to learn some lessons and make some improvements going forward. Here are a few that stand out.

- *Liquidity.* A number of banks were not as prepared to deal with liquidity strains as they should have

been, thinking that their access to funding, even in times of stress, would be much better than it proved to be. I think the regulatory community had that same misimpression, and a number of us have concluded that our liquidity metrics were not sufficiently robust. We have been working with banks all over the country to improve their liquidity positions. In addition, the Basel Committee issued a very thoughtful paper on liquidity risk management, and we have spent a considerable amount of time developing a better template for gathering data to measure liquidity risk. I believe these efforts will produce real improvement over time.

- *Risk management for complex financial instruments.* Collateralized debt obligations (CDOs) backed by subprime mortgages were the prime example of the need for better efforts here. Despite the inherent risk of the underlying collateral, the industry and regulators were lulled into a false sense of security by the triple-A ratings given to the super-senior tranches of these securities. Some of the exposure was masked in off-balance-sheet vehicles in ways that clouded the full extent of exposure. Indeed, some senior bank management thought they had avoided

this: some concentrations can be so large that even the best risk management will fall short when an economic storm focuses on that same asset class. While the jury is very much still out, and the subject is controversial, regulators and policymakers in the future may very well need to revisit the issue of appropriate levels of concentration.

A major concern I have going forward is the pressure to lower underwriting standards for loans that are sold to others as opposed to those held in portfolio. Some banks applied different underwriting standards for loans sold to Wall Street securitizers for further sale to investors, while the standards were more rigorous for loans that banks kept on their books. The same was true for leveraged loans originated by our very largest banks.

In both cases, when examiners began to criticize the lower standards for loans that were sold, we often heard the same two arguments in response. First, some argued that weaker underwriting standards should not matter if the risk leaves the bank when the loan is sold to a willing buyer who understands the increased risk. And second, some claimed that if banks were forced to raise their standards above the level required by the market, they would lose business to others who did not have to raise their standards.

Events of the last year have revealed the fundamental flaw in those arguments. When funding markets lock up, banks can get stuck holding a large pipeline of the loans they planned to sell, and the weak underwriting can translate into huge writedowns and losses. That is what happened in the leveraged loan market, and it is also what happened to a number of banks with large mortgage warehouses.

So the painful lesson learned is that banks need to underwrite loans for sale as they would for loans held in portfolio, and we need to hold banks to that standard or something very close to it. That is easy enough to say now, when the loan sale market is closed, but it will be much harder to put in practice when the market reopens and banks start making the same arguments once again. Holding the line will clearly be one of our challenges for the future.



**Douglas W. Roeder**  
Senior Deputy  
Comptroller  
for Large Bank  
Supervision



**John G. Walsh**  
Chief of Staff and  
Public Affairs



**Julie L. Williams**  
First Senior Deputy  
Comptroller and  
Chief Counsel

subprime risk by deliberately choosing to avoid originating such loans in the bank—only to find out after the fact that their investment banks had purchased subprime loans elsewhere to structure them into CDOs. And when the market seized up, some banks that structured the CDOs for sale to third parties wound up holding large positions that no one wanted to buy. That resulted in huge concentrations, which in turn led to huge losses. There was too much reliance on triple-A ratings, not enough transparency and risk aggregation, and too much tolerance for concentrations.

- *Risk concentrations in commercial real estate.* The OCC and the banks we supervise did a tremendous amount to anticipate and address potential issues before they turned into problems, and we have been especially proactive in squarely addressing these problems as they have emerged. But I have been troubled in looking at the banks that have failed thus far—both national and state banks—by some toxic combinations of real estate concentrations, rapid growth, extremely high levels of brokered deposits, and out-of-area lending. In the future, I think we will need to do more to check these combinations before they cause unmanageable problems. And let me add

And now let me turn to my final observation about the recent credit turmoil, which is this: it is a long way from over. The administration's plan to invest capital in, and guarantee the debt to, financial institutions has helped stabilize the market. But as we approach the end of 2008, the economy has plainly weakened. At least in the near term, all of this is likely to mean more credit losses; more provisions to loan loss reserves; squeezed profits; strains on capital; and, in some cases, more bank failures.

Facing all of this, I think it is critical that the OCC continues to strive for the kind of balanced professional judgment that we have shown thus far. We have to be careful to be forthright in addressing problems as we see them and leaning on bank management to do exactly the same. But we have to be equally careful not to overreact and make problems worse by acting too precipitously or being more stringent than necessary.

It is also important that in our focus on credit and liquidity issues we not lose sight of our compliance and consumer protection responsibilities. We know that compliance lapses can do significant damage to a bank's reputation—the kind of damage that can take years to repair and that diverts time and attention away from the business of running the bank. I have asked our examiners to see to it that in dealing with the industry's safety and soundness, we do not allow significant compliance problems to develop in their place.

As we attempt to strike that balance in our supervision, it is all but certain that we will see more national bank failures, and some will ask if we should not have done more to prevent one bank failure or another, or if we should have moved sooner to close a troubled bank. These are important questions. But it is just wrong to argue that any bank that fails and costs the deposit insurance fund money could have been closed sooner at less cost. It is also wrong to suggest that any bank that fails means that supervisors did not do their jobs.

While either assertion could be true with respect to a specific bank, it is just as possible—and frankly, more likely—that neither is true with respect to a particular failure. The fact is, banks take risks when

they make loans, as they should, and sometimes they fail because the risks prove larger than they reasonably anticipated; or the local economy suffers severe stress, devastating businesses to which the banks lend; or extraordinary events like the ones we have seen in the last year put strains on banks that just could not be reasonably anticipated.

When banks like these suffer large losses, examiners have to make hard judgments about viability. Should the bank be closed immediately with a certain loss to the deposit insurance fund? Or does it have a reasonable prospect of raising capital or being sold, preventing any loss to the fund? The latter option, of course, may take a little time to find out. Sometimes that time produces a positive result that avoids failure and loss altogether, and sometimes it does not. But even when it does not, it is not at all clear that the ultimate loss to the fund is greater than it would have been had the bank been closed earlier. In fact, that should not be the case if the bank is tightly regulated during the process to avoid excessive risk-taking, which is exactly what we do with a bank in these circumstances.

The bottom line is this: bank closing is an art, not a science. Sometimes it is better to do it fast, and sometimes it is much better to take the time, in controlled circumstances, to try to find a solution that avoids loss to the fund. Our most seasoned examiners make these kinds of viability determinations, working closely with the Federal Deposit Insurance Corporation (FDIC), and we think this is by far the best approach to least-cost resolution.

I am proud of the hard work and dedication OCC staff has shown in meeting the extraordinary challenges of the last year. One of my great comforts in serving as Comptroller is knowing that I can rely on such a strong corps of talented, dedicated people who are doing all they can to help ensure the safety and soundness of our national banks. The national banking system is the backbone of a strong U.S. economy, and we at the OCC will continue to work hard to ensure that it remains safe and sound, and capable of supporting American consumers and businesses.



# Introduction

**A**gainst the backdrop of one of the most tumultuous years in U.S. financial history, the OCC's *Fiscal Year 2008 Annual Report* highlights how the OCC performs its primary mission of examining, supervising, and chartering national banks. In times like these, the agency is especially sensitive to how financial institutions touch the lives of the individual Americans who, as employees, shareholders, and customers, have a direct stake in their safety and soundness. The OCC's ultimate responsibility goes beyond the banks we supervise to the broader public interest we serve.

Processes and people are central to the accomplishment of the OCC's mission. The OCC routinely provides professional and independent bank supervision, and our people are widely recognized as exceptionally competent at what they do. We provide advanced training for examiners; integrate new technologies into bank supervision; develop sophisticated risk models to inform supervisory strategy and practice; place resident examining teams in our largest, most complex institutions; maintain separate supervisory approaches for midsize and community banks; offer an appellate process for national bankers; ensure that examiners have specialized expertise in such areas as compliance, bank technology, capital markets, mortgage banking, and operational risk; and provide national bank customers a state-of-the-art means of resolving complaints.

The OCC's risk-based approach to supervision provides a framework for identifying banks with elevated risk, assessing the risk those institutions

might pose to the national banking system, and deploying supervisory resources accordingly. Risk-based supervision proved especially important given the increased number of at-risk institutions in fiscal year 2008.

Despite the heavy focus on direct examination and supervision, the fiscal year saw a large number of policy initiatives. The OCC continues to work with legislators and regulators to promote regulatory efficiency and enhance consumer protection, fair lending, and equal access to credit. Recognizing the importance of these aspects of supervision and the danger that market events might overshadow these issues, Comptroller Dugan cautioned that "market disruption could so dominate the attention of bankers and regulators that we lose focus on other still-important priorities. We simply cannot allow that to happen."

Responding to the challenges of the economy requires dedicated people with the right skills, motivation, and experience. This annual report spotlights OCC team members who represent some of the many diverse professions that must be integrated properly for the OCC to succeed—examiners working in national banks and in policy positions; attorneys who help write, interpret, and enforce laws and regulations; economists who provide data and analytical tools; management specialists who ensure efficient use of our human and material resources; information technology experts; community affairs officers; and many others, who, together, bring diverse perspectives to the OCC. This range of expertise, developed over 145 years, enables us to maintain high standards for bank supervision in good times and bad.



## OCC Supervisory Efforts in Face of 2008 Market Turmoil

Before before the damage spread throughout the U.S. financial system, OCC examiners were focused on the emerging fault lines in the credit markets. In 2005, for example, at a time when bank profitability was strong and house prices were still appreciating, the agency instructed examiners to address the risk of loan products with the potential for payment shock, such as hybrid mortgages that start with low monthly payments followed by payments that are much higher. Although national banks largely avoided subprime lending, nonbank lenders made large numbers of these loans, and the consequences eventually spilled over into the broader credit markets.

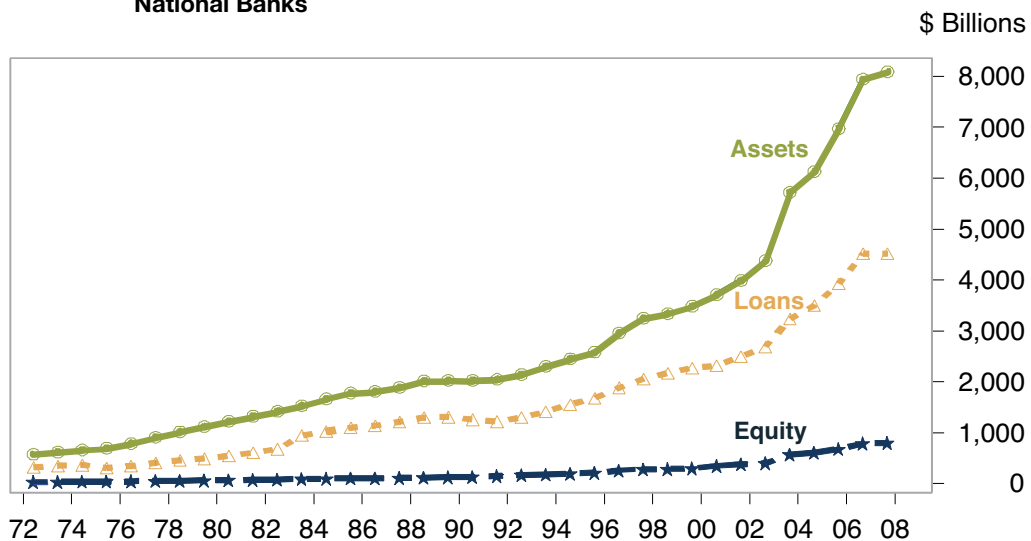
By 2008, as Comptroller Dugan noted in congressional testimony, the national banking system was being tested by two powerful and related forces that were exerting pressure on banks of all sizes in many parts of the country. “One is the large and unprecedented series of credit market disruptions, still unfolding, that was precipitated by

declining house prices and severe problems with subprime mortgages,” he told the Senate Banking Committee. The other was the slowdown in the economy, which had begun to affect credit quality adversely for a number of asset classes.

“The combination of these forces has strained the resources of many of the national banks we regulate,” Mr. Dugan said at that hearing on March 4, 2008.

While the national banking system remains fundamentally sound, the effects of these complex market dislocations are still working through the financial system. At the height of the market turmoil, banks showed increasing reluctance to lend to each other out of concern over credit quality and a desire to maintain liquidity in the face of market uncertainty. The contraction of market liquidity required some large national banks to fund and hold additional assets on their balance sheets. The rapid deterioration in credit quality of subprime mortgages led to substantial write-downs in certain structured investment products.

Figure 3: **Assets, Total Loans, and Equity from 1972 to 2008**  
National Banks

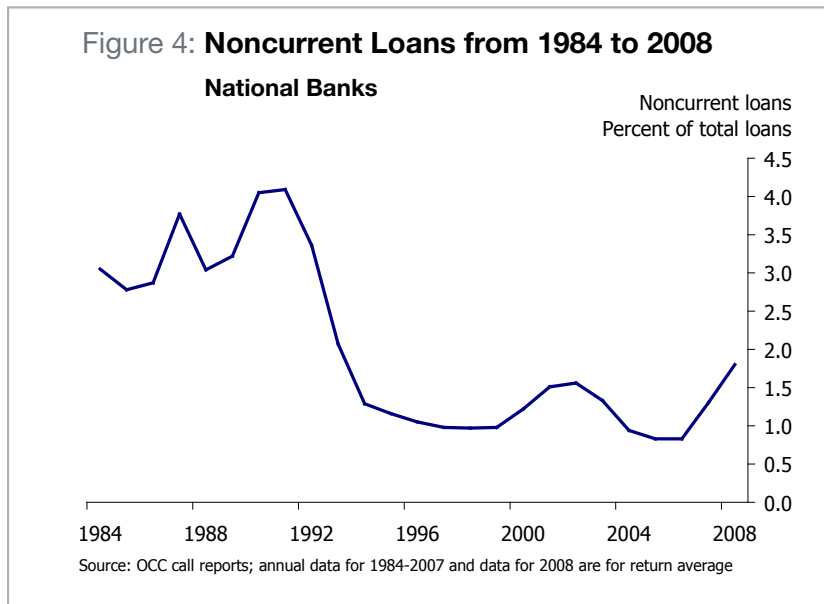


Source: Integrated Banking Information System (OCC)

Note: 2008 data as of June 30, 2008.  
All other data as of year-end.

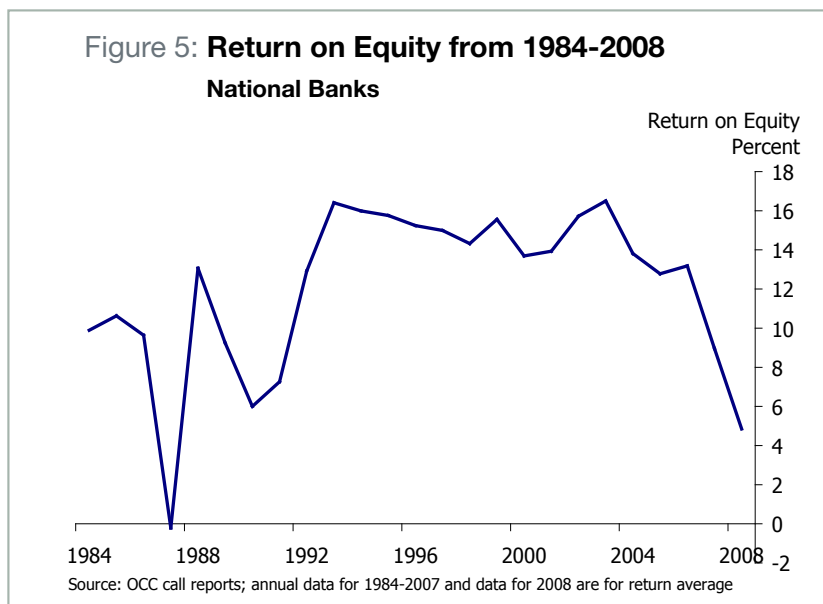
The downturn in housing and the broader economy affected national banks' loan portfolios adversely, increasing the level of nonperforming and past due loans. Noncurrent loans—the percentage of bank loans that are 90 days or more past due and on nonaccrual—rose to 1.80 percent at the end of June 2008, up from 0.86 percent a year earlier, as Figure 3 shows, and then rose again, to 2.19 at the end of September 2008. Even at that level, noncurrent loans were low by historic standards. Deterioration

in loans tied to the real estate sector, however, was more pronounced. Losses from housing loans rose to new highs, and losses on other retail credits were up sharply. Credit stress was complicated by elevated liquidity risk and, in the latter part of the year, by heightened concern about the safety of retail deposits in the wake of publicized bank failures. All of these events were reflected in lower earnings for the national banking industry.



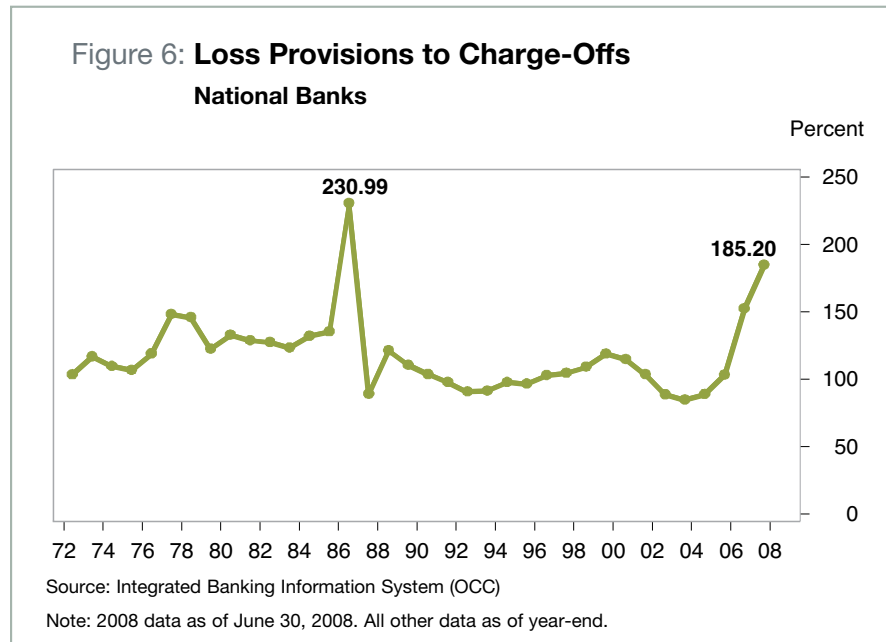
National bank net income in 2008 declined to one-third of its level a year earlier. National banks recorded income of \$6.9 billion in 2008's second quarter, down from \$21.5 billion a year earlier. Return on equity, a key measure of bank

profitability, was 3.5 percent in the second quarter of 2008 versus 12.8 percent a year earlier. As Figure 5 shows, 2008 return on equity year-to-date is averaging 4.4 percent, substantially below the level seen before the market turmoil began.



Over the last year, weak noninterest income and higher provisions were the main drags on earnings. Large banks benefited from improved

profit margins, while the margins of smaller banks deteriorated. Despite poor earnings, banks were able to increase capital and reserves over 2007 levels.



National banks were generally able to absorb the financial shocks for a number of reasons. The first, and most important, is that banks, having entered this period in overall good health, had the earnings and capital to weather market downturns. Capital levels well in excess of regulatory minimums gave banks the flexibility to absorb sizable quantities of assets on their balance sheets when liquidity in the credit and capital markets became constrained. Throughout the year, banks took steps to further strengthen their balance sheets by increasing loan loss reserves, reducing dividends, and issuing capital in both public and private offerings. Their ability to raise capital reflected investors' belief in the underlying long-term viability of these franchises. Nonetheless, should credit performance worsen, additional loan loss reserves and capital may be required.

National banks, especially larger ones, benefited from diversified lines of business and funding sources. For example, although fees from loan sales, securitizations, and trading were adversely affected by the downturn in housing, other fee income sources remained. Indeed, throughout the year, the national banking system has generally been a source of strength for the financial sector, providing credit and liquidity to both the retail and commercial sectors, and absorbing companies and product lines that faltered or failed under the strains of market dislocation.

While the vast majority of national banks have had the financial capacity and management skills to weather the challenges of the past year, a few have not. In these cases, the OCC's goal has been to effect early and least cost resolution of the bank so as to minimize losses to depositors and the FDIC insurance fund. During fiscal year 2008, the OCC appointed the FDIC as receiver in five bank failures.





## Section Two State of OCC Supervision

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## Bank Supervision in a Time of Challenge

### *Weathering the Downturn*

The volatility of the financial markets and the unprecedented nature of the events that shaped the environment for banks in 2008 posed challenges for the OCC. The OCC anticipated many of the problems the industry faced before they occurred—and dealt with them once they arrived.

The OCC sounded early public warnings in guidance and ongoing supervision about risk layering, payment shock, and declining underwriting standards for nontraditional mortgages and home equity lending. Many of the steps the agency took responded directly to early feedback from the agency's field staff, including:

- Higher supervisory standards for subprime mortgage underwriting. As a result, national banks

originated less than 10 percent of all subprime loans in 2006, the peak year for such lending, and those they did originate were generally of higher quality than those originated elsewhere.

- Rigorous horizontal reviews of bank loan portfolios across the country, starting in 2004, to better assess the performance of CRE, a lending area in which many community banks were developing concentrations. The OCC pushed for the CRE guidance that was issued in 2006 over industry opposition. The guidance described expectations for heightened risk management practices for institutions with concentrations in CRE loans.

*continued on page 14*

## Community Bank Supervision: *Assistant Deputy Comptrollers Mobilize OCC Resources To Protect Safety and Soundness*

Community banks play a vital role in the economic health of America’s towns and cities, and the bulk of the OCC’s supervisory resources are devoted to those banks.

Some 1,400 examiners work full-time on community bank supervision. They represent 68 percent of the agency’s 2,000-plus person exam force. Their work is coordinated through a national network of 49 field offices and 24 satellite offices that are located in almost every state in the country, overseen by four district offices in New York, Dallas, Chicago, and Denver. By contrast, the OCC’s large and midsize banks are supervised by teams of resident examiners assigned full-time to individual banks.

For community bank examiners especially, teamwork is crucial. While each member of the examination team focuses on his or her area of assigned responsibility—such as capital, asset quality, or compliance—examiners are also keeping an eye on the bigger picture, assessing the institution’s overall safety and soundness. When a bank’s ability to remain solvent is called into question, experts in the Special Supervision Division in Washington are there to develop and implement rehabilitation or resolution strategies.

The weakening economy led to a rising number of problem banks among the community bank population in 2008, mostly related to the deterioration of commercial real estate markets. The OCC’s response was rapid and systematic. Community banks were divided into three tiers, with the first tier comprising banks with the greatest degree of risk. Examinations of CRE risk at Tier I banks began immediately; examination of Tier II banks was underway at year’s end, with progressively fewer problems uncovered as these examinations progressed. To ensure consistency among the approximately 1,500 examiners who were involved in this effort, the OCC convened two conference calls, the first in April and the second in October, and provided written guidance on relevant topics.

Assistant Deputy Comptrollers, who manage the OCC’s field offices and are responsible for the supervision of a portfolio of community banks, play a key role in assuring that cooperation between local examination teams, OCC District offices, and headquarters staff proceeds smoothly.

With more than 29 years at the OCC, James Calhoun, an Assistant Deputy Comptroller (ADC) based in Pittsburgh, understands the importance of close working relationships among supervisory personnel, especially in challenging economic times. With experience as an analyst in Special Supervision and an EIC of problem banks, Calhoun has the perspective of a veteran who has been through several turns of the economic cycle. He also knows that the iron test of an examiner’s skill is communicating his or her findings in a constructive way to the banker. “From the bankers’ standpoint, it’s all about ensuring clarity,” Calhoun explains. “The best way I have found to do that is to take an issue and frame it in terms of how it might affect their bank’s profitability, stakeholders, and reputation.”

In challenging economic times, the need for “open, honest, and frequent” supervisory communication is greater than ever, noted Omaha ADC Troy Thornton, a 23-year OCC veteran. In 2008, Thornton increased the frequency of his meetings with bank boards and made sure that banks in his portfolio were kept well informed of supervisory expectations through quarterly letters and periodic outreach meetings. For banks under stress, supervisory action taken in a timely manner can make a big difference.

“Among the things I look for during exams are behaviors that, if they continue, can lead to problems,” says Calhoun. “We want to get the bank’s board of directors to understand that these behaviors can pose more risk unless they are changed or appropriately managed. Real-life examples or ‘war stories’ are a highly effective way to illustrate possibly adverse outcomes.”

Calhoun adds that while examiners have to respect the authority of bank managers, there is also a time to be direct. “Bankers and regulators are a team with the best interest of the bank and its customers in mind,” Calhoun explains, “and it becomes even more important in today’s time that we act as a team. You have to be open to questions and expect pushback, but if management is not performing satisfactorily, you need to make that clear to the board as soon as you can. That’s what we get paid to do, to make that call.”

### Vital Facts

Community National Banks	1,502
National Bank Examiners Dedicated to Community Bank Supervision	1,414
Examination Frequency	No less than each 18 months
OCC Field Locations	77

## Large Bank Supervision: *Examiners-in-Charge of the Most Complex Financial Institutions*

The banks supervised by the OCC include some of the largest and most sophisticated financial institutions in the world—institutions with trillions of dollars of assets. They offer a wide array of financial services, engage in millions of transactions every day, and play an enormously important role in the national and global economy.

To supervise institutions that operate on this scale, the OCC deploys teams of resident examiners who work full-time, year-round at each of the banks in the Large Bank program. More than 450 examiners are deployed at the 17 largest banking companies in the program.

This approach allows examiners to acquire a close understanding of the bank's risk-taking and risk management. With that knowledge, the OCC can identify the most significant risks and then determine whether a bank has the systems and controls it needs to measure, monitor, and control those risks. The OCC performs appropriate validation of banks' risk management through transaction testing. Concerns are then communicated directly to senior management, making it possible for corrective action to be achieved in a timely and effective manner.

The foundation of the OCC's Large Bank supervision is the EIC, who, in close collaboration with headquarters in Washington, is responsible for developing the supervisory strategy for the institution and implementing that strategy on site.

Kim Scherer, the EIC at UnionBanCal Corporation in San Francisco, sees herself as having dual roles: as the person with ultimate responsibility for the bank's supervision and as the manager of the OCC on-site staff at the bank. "While most of my staff of 15 does the supervisory work and examination activity relevant to Union Bank, it is my job to put it into overall perspective and view risk 'from the top of the house.'"

Scott J. Wilson, an EIC at Capital One Financial Corporation in McLean, Virginia, agrees: "You are both a national bank examiner responsible for the safety and soundness of a large financial institution and a manager trying to ensure that you have a professional and well-motivated workforce that feels empowered to do its job. I think it is critical that the Examiner-in-Charge have strong communication skills and the ability to build relationships with people."

Investing in the growth and development of the staff is a critical function of the job, according to Tim Greenway, the EIC at Bank of America in Charlotte,

North Carolina. Another crucial function is accurately assessing and communicating the risk in the assigned bank while securing remedial action, should it be necessary, from bank management, he says.

Being an EIC requires a high degree of flexibility. Supervisory strategies must sometimes be adjusted on the fly to reflect an institution's changing risk profile. "A strong Examiner-in-Charge must be very cognizant of the external environment and the impact that market events and the 'Street' can have on the condition and perception of the financial institution that the OCC supervises," says Scott Wilson.

And the OCC requires that EICs be prepared to move on after five years at the same institution. "This 'term limit' ensures that we do not get 'too close' to the bank," explains Wilson. "It also allows a fresh set of eyes to supervise an institution after a certain period of time."

Even in less tumultuous economic times, the EIC's life is varied and fluid. Greenway says that "because I work in a mega-bank that is active in many markets and always exploring new products, every day is unpredictable."

Scherer may find herself meeting with the chief executive officer or other executive-level bank managers to stay abreast of key issues surrounding the company; meeting with her staff to share supervisory insights; reviewing, editing, or preparing written supervisory correspondence to bank management; and attending briefings related to her institution.

Having a permanent presence makes a huge difference for both the examiners and the banks. "We are in the bank on a daily basis to assess the condition of the bank and communicate with the bank through informal and formal channels," Wilson says. "This allows us to share knowledge and perspective across large banks and the OCC, and with other regulators and bankers."

"This is a job in which we never stop learning," Greenway notes. "If the OCC is to remain a highly respected financial institutions' regulator, we must all pass what we learn on to those who follow us."

### Vital Facts

Large Banking Companies	17
Asset Range	\$49 billion to \$1,900 billion
National Bank Examiners Dedicated to Large Bank Supervision	467
Examination Frequency	Continuous

- Identifying and flagging, through targeted examinations and examiner surveys, the trend of declining underwriting standards and the difficulty increasingly encountered by large national banks in selling some corporate loans to investors.
- Development of a new mortgage metrics database.* An unprecedented effort accomplished in record time, the quarterly OCC Mortgage Metrics report provides the best available information on over 60 percent of the mortgages serviced in the United States. As Comptroller Dugan notes, “We now know a lot more than we once did about trends in delinquency, modification, and foreclosure with respect to prime, subprime, and Alt-A mortgages, and we’ve begun to use that data in a variety of ways to support our supervision.” In addition, the OCC has begun to develop similar metrics for home equity loans and is planning to do the same with credit card lending and syndicated loans.
- Tracking Shared National Credits (SNC), large syndicated loans held by multiple banks.* While participating in the review of more than 8,000 credit facilities, with commitments totaling \$2.8 trillion, the OCC contributed to a project to modernize the collection and analysis of SNC data and to improve the program’s efficiency and effectiveness.

Internally, the OCC’s market disruption procedures shifted into high gear in 2008, producing timely and critical information from institutions all over the country. Some of the market problems were new and complex—like those raised by collateralized debt obligations, structured investment vehicles, and asset-backed commercial paper conduits—and the agency’s specialists, economists, and policy experts have dissected them for use in adjusting regulatory guidance and supervisory strategies.

Perhaps most important, OCC examiners took steps to ensure that banks were more realistic about

recognizing delinquent loans and losses, that they built loan loss reserves and raised capital when necessary, and that they took tangible actions to improve risk management.

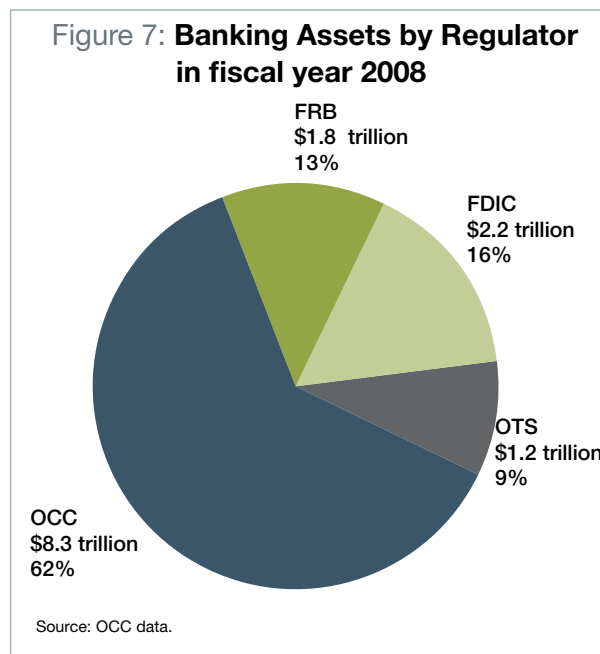
While large banks struggled with the fallout from the precipitous decline in the housing market, many community institutions were challenged by concentrations in commercial real estate. OCC examiners worked with national banks to manage those risks.

In the 17 largest national banking companies, where the OCC maintains a continuous presence through staffs of resident examiners (see “*Large Bank Supervision: Examiners-in-Charge of the Most Complex Financial Institutions*” on page 13), particular attention was paid to the banks most affected by the mortgage market disruption.

Examiners monitored capital, liquidity, and contingency plans for these national banks, and carefully assessed risks to capital and liquidity from off-balance-sheet vehicles and commitments. One focus was bank programs that continued to purchase assets originated by other firms. Another focus was bank portfolios that were vulnerable to further downgrades in the ratings of bond insurers or to deterioration in the condition of significant borrowers. Examiners

determined whether the susceptible banks needed to improve liquidity and raise capital, and they evaluated management plans to achieve those goals. Examiners closely monitored banks’ exposures to significant counterparties in derivatives markets.

Special attention was paid to contingency funding plans of banks weakened by the market disruptions. Were plans current and based on realistic balance sheet and market behaviors? Did they take into account any off-balance-sheet funding challenges? Examiners made sure that each plan’s projections considered worst-case scenarios, such as a bank undergoing a serious liquidity problem or its bonds being downgraded below investment grade. Banks



that relied heavily on securitization received extra scrutiny. In one sign of strength, large national banks raised approximately \$125 billion in new capital in fiscal year 2008.

In community banks, which the OCC supervises through offices located across the country (see “Community Bank Supervision: Assistant Deputy Comptrollers Mobilize OCC Resources to Protect Safety and Soundness” on page 12), OCC examiners focused on making sure that those institutions had risk management systems equal to their risk profiles and that they had the expertise and the resources to manage the risks involved in their business lines.

Rising concentrations of commercial real estate loans have long been a subject of OCC supervisory concern. As Figure 8 shows, CRE loans at midsize and community national banks have doubled over the past 10 years, to 200 percent of capital overall; at some national banks, the increase was several times that. About one in four community banks under OCC supervision have CRE-related concentrations exceeding one or both of the thresholds defined by the interagency guidance issued in December 2006. These concentrations presented considerable risk, particularly in geographic areas that have experienced exceptional volatility in home prices.

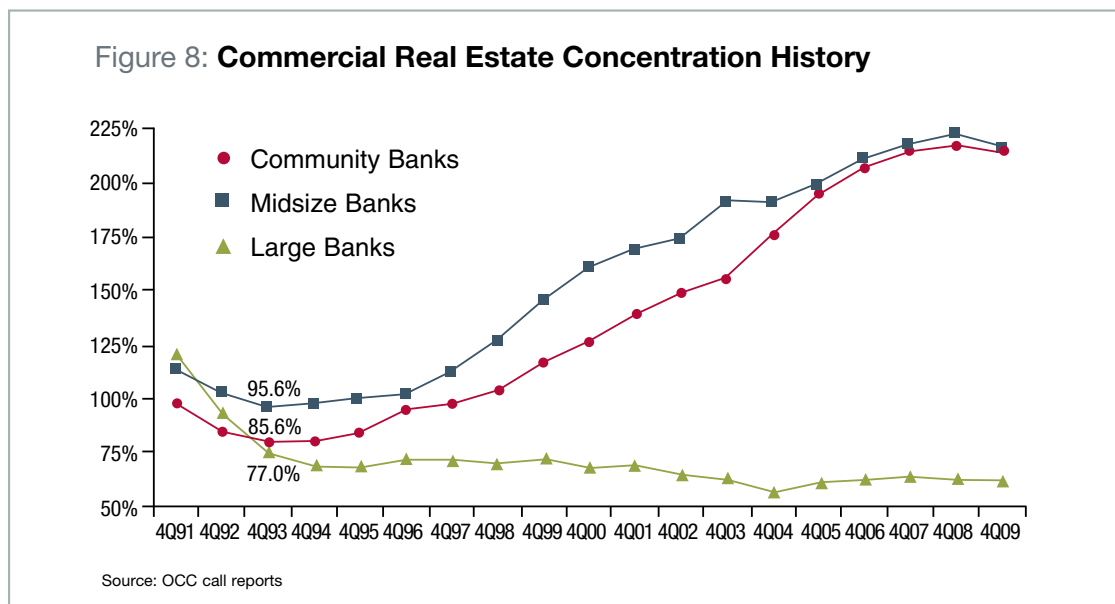
Beginning late in 2007, for each community bank that exceeded one or both of those thresholds, OCC district examination staff prepared summary information that identified the bank’s exposures, recent and current supervisory activities, and the

examiner’s assessment of management’s ability to manage the bank’s CRE exposures in the current environment. This information was reviewed and discussed with OCC management to identify those banks believed to have the highest potential risk, and to ensure the appropriateness of planned supervisory activities. Asset quality reviews targeting these banks’ CRE portfolios are under way. These reviews enable the OCC to more accurately quantify the level of risk in national banks, and determine how well it is being managed. This assessment is critical to determining what, if any, remedial action is appropriate for each bank.

### Other Areas of Concern

*Leveraged loans.* Leveraged loans, whose borrowers have high levels of debt compared with equity, were the subject of targeted examinations in our largest syndication banks. Dislocations that occurred in the credit markets during the fiscal year delayed completion of long-term financing for some leveraged loans that banks had originated with the intent to sell (that is, to syndicate) to investors. As a result, a number of large national banks retained a higher-than-usual volume of leveraged loans on their balance sheets.

In fiscal year 2008, the OCC’s Large Bank Supervision Department conducted leveraged lending targeted reviews at the largest syndication banks, with a focus on syndicated pipeline management, stress testing, and limit setting. The OCC issued the “Leveraged Lending” booklet in



## OCC Responds to Rising Tide of Mortgage Foreclosures

Perhaps no single issue defined the nation's domestic agenda in fiscal year 2008 more than the dramatic increase in mortgage foreclosures. About 1.3 million foreclosures were initiated in 2007, more than twice the average rate for the first half of the decade.

The effect of foreclosures extends beyond the individual homeowner to the neighborhood in which the foreclosure occurs. "Foreclosed properties are not just empty houses," Comptroller Dugan told the National Association of Affordable Lenders in February. "The absence of homeowners—and the gloomy sight of abandoned, deteriorating properties—can depress entire communities."

To help deal with the foreclosure crisis, the OCC joined with other federal regulators, as well as with lenders, elected officials, and nonprofit organizations, in promoting a wide range of programs designed to stabilize communities and allow homeowners to remain in their homes.

In testimony before the U.S. House of Representatives' Committee on Financial Services in April, Comptroller Dugan said that the proposed Federal Housing Administration Housing and Stabilization and Homeownership Retention Act of 2008 would provide borrowers and lenders with an alternative to the costly process of foreclosure. "By keeping more borrowers in their homes," Comptroller Dugan said, "the widespread use of such a program would also help prevent further reductions in the prices of houses financed by national banks." Use of such a program, he pointed out, would more generally make the mortgages less risky by mitigating the downward pressure on house prices caused by the foreclosures that would be avoided.

Under the program, titled "Hope for Homeowners," if a borrower met certain criteria, lenders could agree

to reduce the mortgage amount to a level the borrower could afford and could offer to refinance the original loan into a new Federal Housing Administration-insured mortgage. Accepting the loss under this voluntary arrangement could be less costly to mortgage holders than foreclosures. Homeowners would remain in their homes, and the potential risk to the government of guaranteeing the refinanced mortgages would be more acceptable than "the prospect of widespread foreclosures and all their related costs," Comptroller Dugan said. The proposed program was incorporated into the Housing and Economic Recovery Act of 2008 passed on July 30.

Because the threat of foreclosure has extended well beyond the low-income neighborhoods where subprime mortgages have been predominant and into more affluent neighborhoods, Comptroller Dugan told the Association of Affordable Lenders in February that proposed changes to 12 CFR 24 (public welfare investment authority) would restore its original scope to cover "not just low- and moderate-income areas, but also middle-income areas in need of reinvestment and revitalization." Those changes were also included in the Housing and Economic Recovery Act.

Turning policy into action, the OCC issued a consumer advisory about scams that purport to "rescue" homeowners from foreclosure but lead instead to those homeowners potentially losing their homes or the equity in their home. In addition, the OCC appointed a Community Affairs Officer specializing in community stabilization to meet with bankers, community-based organizations, and public officials across the country to find solutions to the problems communities face because of increased levels of home mortgage defaults and foreclosures.

the *Comptroller's Handbook*, which consolidates and supplements existing guidance to bankers and examiners on the risks associated with leveraged lending and the risk management systems and controls needed to mitigate those risks.

*Home equity loans.* Aggregate outstanding lines of home equity loans at national banks have doubled since 2002. National banks account for about \$500 billion, or roughly half, of the market for home equity loans. As housing prices fell, borrowers

became increasingly leveraged and the percentage of past due home equity loans increased.

Examiners made sure that banks with concentrations of home equity loans managed their risks appropriately; some banks had to increase loss reserves, write down loans, or raise capital.

*Maintaining adequate liquidity, loan loss reserves, and capital.* Prompt recognition of losses and maintenance of strong loan loss reserves and capital are critical during periods of economic stress.

Ensuring that national banks maintain adequate loan loss reserves and capital was a point of emphasis during fiscal year 2008 bank examinations. Similarly, the OCC continued to evaluate the adequacy of banks' liquidity positions and liquidity risk management processes, especially at institutions with significant concentrations in the loan or liability portfolios.

In light of market and economic conditions, national banks made substantial increases to their loan loss reserves during 2008. They bolstered capital levels by reducing dividends and raising more than \$100 billion in new capital from outside investors. So, despite the substantial increase in total assets, in part the result of loans coming back on the books of banks, capital ratios remained near the levels of a year ago, and 99 percent of all national banks met or exceeded the "well-capitalized" regulatory capital requirement.

### ***Problem Banks***

The goal of OCC supervision is to identify and correct potential problems at an early stage, before they adversely affect the safety and soundness of the banking system or the viability of any individual bank. For example, we include provisions in certain enforcement actions that require the bank to develop and implement a plan to sell, merge, or liquidate, if required minimum capital levels cannot be achieved. These provisions have resulted in banks seeking buyers or merger partners at an earlier stage, before their problems have eroded capital to the point where the bank is no longer attractive to potential purchasers. In addition to avoiding a bank failure, these options do not adversely affect depositors and customers and return some value to the bank's shareholders. This approach can be especially successful when the economy is strong, and healthy financial institutions are looking for growth and acquisition opportunities.

As a bank reaches the problem stage, the OCC focuses its efforts on developing a bank-specific plan that takes into consideration the ability and willingness of management and the board to correct deficiencies in a timely manner and return the bank to a safe and sound condition. The OCC's efforts, coupled with the commitment of bank management, often result in a successful rehabilitation. Sometimes the situation is such that the OCC requires the sale,

merger, or liquidation of the bank, consistent with the least-cost resolution provisions of the Federal Deposit Insurance Corporation Improvement Act of 1991. As previously noted, during fiscal year 2008, the OCC appointed the FDIC as receiver of five failed national banks.

In the current economic environment, the number of problem banks has increased and the resolution of problem banks has become more challenging. One serious challenge is that, as the number of banks requiring capital has grown, the interest in acquiring these institutions has softened. Some problem banks have asset quality problems of a depth and nature that makes them unattractive to potential purchasers. Many problem banks are heavily dependent on non-core funding, yet once their asset quality and capital deteriorate, they are restricted by regulation in the rates they may offer on those deposits.

### ***Improving Risk Management***

The OCC was an active participant on the President's Working Group on Financial Markets, the Senior Supervisors Group, and the Financial Stability Forum, providing insight and information that helped shape the recommendations that came from those high-level organizations on enhancing banks' risk management practices. In broad terms, these recommendations called on banks to:

- Ensure the independence of their risk management functions.
- Better manage the pipeline risk associated with originate-to-distribute lending and securitization.
- Rely more on due diligence and less on credit ratings when investing in complex structured products.
- More fully evaluate the reputation and residual risks arising from the off-balance-sheet ownership of conduits (which some large banks used to hold collateralized debt obligations) and asset management businesses.
- Enhance transparency, disclosure, and valuation practices, especially for off-balance-sheet activities.
- Improve stress-testing and capital planning processes. (These processes should incorporate off-balance-sheet activities and be appropriately forward-looking.)



The OCC worked closely with other domestic and international agencies to develop a consistent and effective response to the turmoil in global financial markets. For example, the agencies are working together to address the need for more sophisticated liquidity risk management practices and systems to replace those whose simple premise was that loans are funded by deposits. The agencies also are focused on helping banks improve the identification and management of off-balance-sheet exposures and risk concentrations and develop metrics for aggregating risks to particular counterparties. The OCC, primarily through its Large Bank Supervision program, is ensuring that banks' risk management practices incorporate these recommendations.

The OCC's efforts have included working with the Basel Committee on Bank Supervision to issue updated global principles for sound liquidity risk management and supervision. The agency has worked with the Federal Reserve Bank of New York and other key global financial regulators to strengthen the operational performance and infrastructure of the over-the-counter derivatives market.

Using lessons learned from the recent turmoil, the OCC has recommended strengthening the Basel II capital framework. For example, higher capital requirements will be proposed for resecuritizations, such as collateralized debt obligations.

The most successful banks in the future will be those that can move quickly to coordinate their risk

management frameworks with their shifting risk profiles. These institutions will have the information systems and transparency to communicate the different aspects of that coordination to regulators, depositors, shareholders, and the public. The OCC continues to do all it can to see that as many national banks as possible fit this paradigm.

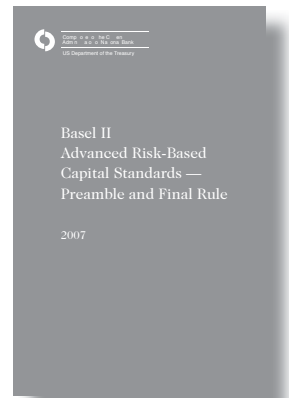
### ***Foreclosure Prevention***

The OCC encourages national banks to work constructively with borrowers who may face difficulties meeting their mortgage obligations. The OCC supports various private and public sector initiatives and programs that seek to assist these borrowers, including those initiated by the American Securitization Forum and Hope Now Alliance, as well as activities pursuant to the Housing and Economic Recovery Act of 2008.

As banks work with borrowers, examiners emphasize the need to construct loan modifications that give borrowers a reasonable prospect of performing under the new terms. Simply shifting a borrower from one unaffordable mortgage to another serves neither the borrower's nor the bank's interest. Through the OCC's ongoing supervision and fair lending processes, the agency will continue to pursue any evidence of unfair, deceptive, or unlawful discriminatory lending practices.

### ***Identity Theft and Accuracy of Consumer Reporting Information***

The OCC worked closely with the other federal financial regulators and the Federal Trade Commission to implement provisions of the Fair and Accurate Credit Transaction Act of 2003. The act enhances the ability of consumers to combat identity theft, to increase the accuracy of consumer reports, and to exercise greater control over the type and amount of certain



At Financial Literacy Day activities on Capitol Hill, Deputy Comptroller Barry Wides discusses the OCC's efforts to educate and support consumers of financial services.

marketing solicitations they receive. The November 2007 rulemakings include:

- *Final rules on identity theft “red flags.”* The new rules require each financial institution or creditor that holds any consumer account, or other account for which there is a reasonably foreseeable risk of identity theft, to develop and implement an identity theft prevention program for combating identity theft in connection with new and existing accounts.
- *Proposed rules and guidelines for ensuring the accuracy and integrity of information* furnished to consumer reporting agencies. The proposed rules would specify when an entity would be required to investigate a consumer’s claim that certain consumer report information is inaccurate.
- *Final rules requiring credit and debit card issuers to develop policies and procedures* to assess the validity of a request for a change of address that is followed closely by a request for an additional or replacement card. The agencies issued final rules requiring users of consumer reports to develop reasonable policies and procedures to apply when a consumer reporting agency sends them a notice of an address discrepancy.
- *Final rules that allow consumers to “opt out”* before a financial institution uses information provided by an affiliated company to make certain marketing solicitations about its products and services.

### ***Expanded Public Welfare Investment Authority***

Recognizing the important role that national banks play in the economic vitality of low- and moderate-income communities, the OCC actively sought legislation to expand the industry’s public welfare investment authority. In August 2008, shortly after the Housing and Economic Recovery Act of 2008 was passed and signed into law, the OCC issued an interim final rule that implements a provision of the law that amended national banks’ authority to make Part 24 public welfare investments pursuant to 12 USC 24 (eleventh). The interim final rule authorizes a national bank and its subsidiaries to make public welfare investments directly or indirectly if the investments primarily benefit low- and moderate-income persons, low- and



*Working with nonprofit community partners, national banks bring a range of financial services to previously underserved communities.*

moderate-income areas, or other areas targeted by a governmental entity for redevelopment, or if the investment would receive Community Reinvestment Act consideration as a “qualified investment.” The rule gives national banks new authority to support low- and moderate-income communities, communities affected by foreclosures and targeted for revitalization, designated disaster areas, and underserved rural communities.

### ***Working with Other Regulators***

The dynamic and global nature of today’s financial services industry presents issues that cut across regulatory and legal boundaries. Banks, securities firms, and insurance firms are active participants in the credit and capital markets and are often counterparties to each other’s transactions; electronic payment systems span the globe; and national banks have offices and customers in countries throughout the world.

The OCC worked with the other federal banking agencies (Federal Reserve Board, FDIC, Office of Thrift Supervision, and National Credit Union Administration) to coordinate supervisory policies, regulations, and regulatory reporting requirements, and to conduct examiner training on issues that cut across the U.S. banking system. Together, the agencies responded to emerging risks and issues facing the industry. They coordinated their examination and supervisory activities for institutions that are subject to multiple regulators and, as appropriate, conducted joint examinations when an activity is conducted across legal entities.



Comptroller of the Currency John C. Dugan looks on as Howard Pitkin, Banking Commissioner of the State of Connecticut, signs a Memorandum of Understanding on exchanging consumer complaint information.

Joint supervisory programs include the agencies' examination program for multiregional data processors and the Shared National Credit Program.

The OCC also worked with state regulators and other federal regulators on matters of mutual interest. Among these regulators are the Securities and Exchange Commission on various securities, brokerage, and accounting and disclosure issues; the Federal Trade Commission on various consumer protection and privacy issues; and the Public Accounting Oversight Board. The OCC has agreements with 49 state insurance departments, the District of Columbia, and Puerto Rico to share insurance-related supervision information and with 42 states and Puerto Rico to share consumer complaint information. (See *"OCC Presses Other Regulators for a Unified and Simpler Consumer Complaint Process"* on page 28.)

The OCC is a member of the administration's Financial and Banking Infrastructure Information Committee and works with that committee, the Department of Homeland Security, and other federal agencies to combat money laundering and terrorist financing activities and to enhance the resiliency of the nation's financial sector to catastrophic events.

The globalization of the financial and banking markets have accentuated the OCC's need to work with financial supervisors around the world. This

coordination is conducted in formal supervisory groups, such as the Basel Committee and the Joint Forum of banking, securities, and insurance regulators, by the Financial Action Task Force, and through direct bilateral meetings and agreements with individual foreign bank regulators. The OCC also provides technical assistance and classroom training to foreign supervisors across the globe to help them strengthen their domestic supervisory programs.

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## OCC Supervises Surge in International Activities by National Banks

While most banks in the national banking system have no direct international exposure, the largest ones conduct business across a broad range of countries. These are truly global institutions, not just banks that operate in a few overseas locations. OCC-supervised banks had \$1.8 trillion of foreign exposure on their books at the end of the second quarter, not to mention substantial additional off-balance-sheet exposure. Although most of the exposure is to developed countries, emerging market exposure has grown rapidly.

Some of the institutions the OCC supervises are under foreign ownership. The OCC supervises 29 national bank and trust companies that are foreign-owned, with more than \$550 billion in assets. The agency also supervises the activities of federally licensed branches and agencies of foreign banks. As of 2008, there were 49 of these from more than 20 countries with combined assets of about \$190 billion.

The cross-border nature of the institutions is a prime driver of the OCC's international focus. But at an operational level, to be an effective supervisor in a global financial system, we maintain extensive relationships with our colleagues throughout the international supervisory community. This includes informal meetings to exchange views on key issues, to collaborate, to compare practices, and to share relevant information. At other times, interaction is more formal, through structured bilateral meetings and through joint work with our colleagues in the Department of the Treasury.

The OCC has an office in London that has operated out of the U.S. Embassy since 1974 and is



dedicated to evaluating key risks present in national banks' European operations. When complex or stressful supervisory situations arise, there is no adequate substitute for the personal and professional working relationships established through these channels.

The OCC promotes effective supervision through its participation in a number of regional and global supervisory groups. Through the Joint Forum, which is chaired by Comptroller Dugan, supervisors from the banking, insurance, and securities sectors of 13 major countries address issues and offer guidance that is frequently used by supervisors in individual countries.

For example, the Joint Forum's paper *Credit Risk Transfer—Developments from 2005 to 2007*, released July 2008, focuses on complex financial instruments that are widely used to transfer credit risk. In 2008, the Joint Forum also issued papers on risk concentrations and customer suitability in the retail sale of financial products and services.

As a member of the Basel Committee on Banking Supervision, the OCC joins supervisors from 12 other countries in initiatives to increase the long-term resilience of the international banking system. The year saw significant progress in implementing the Basel II capital framework, which provides a more risk-sensitive and comprehensive approach to capital adequacy and sets new standards for supervisory review and public disclosures relating to risk. In December 2007, the U.S. banking agencies issued a final rule implementing the advanced measurement approaches of the framework, under which banks, in certain circumstances, may develop their own empirical models for quantifying operational risk, and, in July 2008, published a notice of proposed rulemaking on the standardized approach, which relies on external evaluations.

Closer to home, the Comptroller created the

International Banking Supervision Department in April and named Deputy Comptroller Delora Ng Jee as head of the group. "International banking issues have grown increasingly important to the OCC and the national banking system," Mr. Dugan said, "and I felt strongly that we needed to create a new group to focus on our supervisory work in this area."

Jee, who joined the OCC in 1978, brings a wealth of relevant experience to her new position, including previous responsibility for supervising large banks owned by foreign banking organizations.

She is responsible for consolidating, coordinating, and extending key international supervisory activities of the OCC, including essential elements of the agency's Federal Branches and Agencies Program, which had previously been conducted by Midsize/Community Bank Supervision's Northeastern District. This new International Banking Supervision Department enhances the OCC's supervision of international banking activities through tighter integration with Large Bank Supervision, which supervises institutions that conduct business across a broad range of countries.

"There is tremendous interest from foreign home and host regulators about the U.S. supervisors' response to the current market turmoil," Jee points out. "International Banking Supervision's ties to bank supervision have enabled the OCC to communicate more effectively with foreign supervisors."

This new department serves as the primary point of contact for international banking supervisors and as a clearinghouse for requests to the OCC for supervisory information, bilateral meetings, and participation in international working groups.



*Delora Ng Jee, the Deputy Comptroller for International Banking Supervision, explains OCC policy to a visiting group of international bankers.*

International Banking Supervision collaborates intensively with other OCC divisions, because legal, economics, policy, and examination staff members continue to play active roles in the international activities of the agency.

As Comptroller Dugan has observed, “With global financial markets, a bank regulatory agency can’t be effective if it focuses narrowly on domestic concerns. National borders are increasingly irrelevant to some of the most important issues we face, and effective policymaking has to take that into account.”

## Functional Specialists Bring Technical Expertise to Bank Supervision

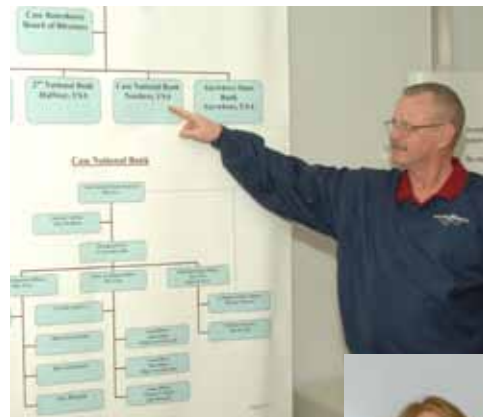
As national banks develop new and complex products and services, the OCC increasingly relies on the specialized expertise of examiners and analysts in such areas as capital markets, commercial and retail lending activities, information technology, asset management, and compliance. These specialists develop supervisory policies, provide guidance to examiners and the industry, and evaluate new products and services and the risks associated with them. Their work often requires close coordination with other regulators, lawmakers, and industry groups, assessing the impact of changes in legislation or accounting guidelines on national banks as well as the overall industry.

**Bank Information Technology** specialists evaluate technology and bank information system functions in national banks and their technology service providers. The OCC has more than 90 Bank Information Technology specialists, most with industry certifications in information technology auditing, information security, or business continuity. National Bank Examiner Carter Messick, a Lead Information Technology Expert in Midsize Bank Supervision, says that banks have adopted new

technologies to improve their infrastructure, broaden their product offerings, and expand their services. “Bankers and customers take the availability and performance of bank technology for granted,” he notes, “but Bank Information Technology Specialists and the bank information technology professionals understand the critical role technology plays.”

Messick says that national banks have faced a number of challenges during the past year, particularly in information security, as criminals continued to level multilayered attacks on banks, retailers, and customers to perpetuate sophisticated fraud schemes. At the same time, Messick explains, industry financial concerns impose limits on spending for technology staff and controls. The OCC reminds bankers that failures in technology or technology-related controls can jeopardize a bank’s safety and soundness or its ability to comply with laws and regulations. “Bank Information Technology Specialists must champion technology issues when supervising banks and collaborate with other examiners to ensure that bankers are managing and controlling technology-related risk consistently regardless of the economic cycle.”

Messick believes that his ability to communicate effectively with bankers and examiners is critical. “Bank Information Technology examiners cannot function effectively as pure technicians;



*Bank Supervision School instructors pool their experience as examiners to develop realistic training scenarios.*

we have to understand the business impact our technical issues may raise. We also need a broad understanding of bank operations and the ability to communicate technical issues in safety and soundness or regulatory compliance terms.”

**Commercial and Retail Credit Risk Policy** specialists develop and interpret policies to promote strong credit risk management and ensure safe and sound banking practices. They stay abreast of banking activities and industry developments to ensure that the policies are timely, practical, and effective.

“We support field examiners and the industry by providing interpretations of policy, writing guidance and handbooks, training examiners, participating in on-site examinations, and conducting industry outreach meetings,” says National Bank Examiner Johnna Cook, a Commercial Credit Specialist.

“We support executive management and the Comptroller by providing technical expertise and research for congressional testimony. We also prepare briefing documents in support of the Comptroller’s many national and international supervisory activities.”

Kevin Russell, a Retail Credit Specialist and National Bank Examiner, adds, “We routinely analyze industry performance and highlight potential risk issues.

We work extensively with all supervisory lines of business on lending reviews and inquiries, monitoring lending risks and concentrations, and we work jointly with other areas to address accounting, legal, and capital issues.”

Cook and Russell agree that the past year presented many challenges, particularly in keeping abreast of emerging risks that could affect safe and sound banking practices. “The volume of issues and the velocity at which they were presented have required strong organizational, analytical, and technical skills,” explains Cook. And for the foreseeable future, she adds, they will have to hone those skills even more. “We will be further challenged to maintain a balanced approach in dealing with economically stressed conditions.”

**Compliance** specialists like National Bank Examiner Paul Utterback make sure that the

OCC’s supervisory policies effectively promote consumer protection and compliance with anti-money laundering laws. In addition to preparing guidance, examination procedures, and answers to frequently asked questions, Utterback serves as a contact to answer questions from examiners and industry sources about consumer protection laws and regulations. By participating in OCC Web and telephone seminars and speaking at trade association conferences, he provides examiners and the industry with a better understanding of compliance issues.

Consumer specialists rely on good technical and analytical skills. “Many of the consumer protection regulatory and statutory provisions are very detailed and need clarification at times,” says Utterback. “As a compliance specialist, part of my job is to review the facts and apply and interpret the law or regulation correctly.”

Changing regulations makes the job of a compliance specialist extremely challenging. “The number of consumer protection laws and regulations continues to increase

and evolve to afford consumers with enhanced protections,” he adds. “As a compliance specialist, you have to really enjoy change.”



*National Bank Examiner Karen Tucker and Director of Community and Consumer Law Michael Bylsma discuss compliance policy with participants around the country. OCC teleconferences served more than 3,000 listeners in fiscal year 2008.*

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## Economic and Financial Analysis Supports the OCC’s Work

The Global Banking and Financial Analysis unit houses a team of economists who analyze potential risks to the national banking system and share this critical information with national bank examiners.

The economists also participate, as needed, in bank examinations.

The team was heavily involved in helping examiners assess portfolio risks from exposures to commercial real estate and provided several large banks with tools to establish priorities for more intensive review. Economists joined examiners on

*continued on page 25*

# New Mortgage Metrics Report Increases Visibility of Mortgage Loan Data

In June 2008, the OCC took on the challenge of making key aspects of national bank mortgage lending more transparent to regulators and the public by publishing the first quarterly OCC Mortgage Metrics Report.

The publication is part of the OCC's intensified focus on mortgage supervision. It is a product of the OCC's realization that the substantial amount of mortgage data previously collected from banks did not provide the level of detail necessary to fully understand mortgage performance and rising foreclosures.

"The OCC seized the opportunity to improve the way mortgage performance is measured, producing better information for supervision of our banks and better information for policymakers, other regulators, market participants, and the public," Comptroller Dugan said upon unveiling the report at the American Securitization Forum.

The initial report analyzed more than 23 million mortgage loans held or serviced by the nine national banks with the largest mortgage portfolios from October 2007 through March 2008. The loans had a value of more than \$3.8 trillion. That volume represented more than 90 percent of all mortgages serviced by national banks and approximately 40 percent of all mortgages across the nation.

The OCC used loan-level data and standardized terms and definitions that allow deeper analysis and better comparisons over time. With regard to the value of standardized reporting, Comptroller Dugan said, "The more we can use standardized metrics across the board, the better we can measure, monitor, and manage mortgage risk."

In September, the OCC, along with the Office of Thrift Supervision (OTS), produced the *OCC and OTS Mortgage Metrics Report*, which expanded the standardized reporting approach by combining mortgage loan data serviced by national banks with data from thrifts regulated by the OTS. The report covered January 2008 through June 2008 and presented data on loan performance, delinquencies, and foreclosures from the 14 national banks and thrifts with the largest mortgage portfolios. During that period, these lenders made up 60 percent of the overall mortgage industry and combined to hold or service 34 million loans worth \$6.1 trillion.

"By combining national bank and thrift data," Comptroller Dugan said, "we are able to present a more

complete picture of the practices and state of the federally regulated mortgage lending industry."

The most significant findings from the second quarter report include:

- Total monthly loss mitigation actions reached more than 90,000 in June, with new loan modifications accounting for 46 percent of those actions. New loan modifications increased by more than 80 percent from January to June 2008 and, on a quarterly basis, increased by 56 percent from the first to second quarter. By comparison, new payment plans grew only 8 percent from January to June 2008, and increased just more than 2.7 percent from the first to second quarter.
- New loss mitigation actions (loan modifications and payment plans) relative to new foreclosures averaged more than 87 percent during the second quarter, about 12 percentage points higher than during the first quarter.
- More than nine out of 10 mortgages remained current. However, credit quality declined during the first two quarters across all risk categories.
- There were increases in early stage delinquencies (30-59 days past due) and seriously delinquent mortgages (60 or more days past due plus loans to bankrupt borrowers who are 30 or more days past due).

The agencies will produce the report quarterly and have shared their standardized terms and definitions with the Department of the Treasury and with the Hope Now Alliance to promote standard data collection and analysis industry wide.

In addition to providing important information to the public, the data gathered in the *OCC and OTS Mortgage Metrics Report* support the supervision of national bank and thrift mortgage practices. The report provides an additional tool to help examiners assess emerging trends, identify anomalies, compare federally regulated mortgage lenders with the rest of the industry, evaluate asset quality and loan-loss reserve needs, and evaluate the effectiveness of loss mitigation actions.



horizontal reviews of banks with high concentrations of commercial real estate and provided an assessment of potential problem assets. A horizontal review is an examination across a portfolio of banks with similar characteristics. These tools and economic assessments are designed to support the examination process and ultimately to support targeted discussions with bank staff.

Their analyses aren't just limited to market conditions in the United States. "The banking industry that we supervise is increasingly international, either directly or indirectly," Nancy Wentzler, the Deputy Comptroller for Global Banking and Financial Analysis, explains. "You might have very large banks with international exposures, but you also have banks in Iowa that are lending to agricultural companies that may be hit hard by sudden shifts in international agricultural markets. We are a global marketplace, so our analysis must recognize those influences even on seemingly small local markets."

Indeed, the appetite for economic analysis has grown tremendously in the past year. "There's a lot of interest, internationally, in finding out how supervisors can do better. I think we'll learn a lot from each other as we assess the events of the last 12 months."

In the meantime, the department is working on a series of "dashboards" that displays the major economic and financial drivers for the major business lines—commercial, retail, international, commodity. "We're asking what indicators we should be watching—those factors that are key influences on activity in each area—to assess the potential risks under alternative economic paths," says Wentzler, who equates the dashboards to the control panel in an airplane's cockpit. "You can't put everything on there. You have limited room and limited ability to interpret, but you have to know if you have gas, if the wheels are up or down, and if the wings are level."

"Same goes for these economic dashboards. You have to limit them to 10 charts or indicators, so we can focus on the most important features and make timely decisions based on that information. No one has the time to read 100 pages of economic data. We have to be focused and timely in our analytical efforts, and dashboards provide that discipline."

The idea is to make these dashboards accessible on the OCC's intranet, so everybody in the agency can look, she explains. "You can log on each morning and know what's going on in the retail market, the credit market, the housing market." This tool also will aid in tracking the economic development that affects the banks the OCC regulates.

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## Risk Analysis Unit Bolsters OCC Supervision

Complex, trillion-dollar financial institutions rely increasingly on statistical analysis and sophisticated mathematical models to help run their businesses. To evaluate the effectiveness of those models—and help national bank examiners make sense of them—the OCC relies on a team of mathematicians and economists in its Risk Analysis Division.

The Risk Analysis Division evaluates the broad range of risk modeling used in the industry and advises examiners and bankers on best and standard practices. Examples of supervisory reviews benefiting from economists' participation are retail credit risk reviews, in which models are used for credit rating and scoring; interest rate risk reviews, which rely on asset-liability models; and examinations of derivative dealers, which use trading-risk models. The economists advise policymakers on issues that require quantitative analysis, including issues related to Basel II capital requirements. Examinations related to implementation of the Basel framework are an area of increasing emphasis for the division.

Roughly one-third of the professionals in the Risk Analysis Division are fair lending modeling experts. They use data from the Home Mortgage Disclosure Act as well as a bank's internal loan data to develop statistical models that test for potential unlawful discrimination by comparing information from large numbers of files. The results assist OCC fair lending examiners in their assessment of the risks of unlawful behavior involving overt discrimination, underwriting and pricing discrimination, steering, and discriminatory redlining and marketing.



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## Compliance Policy Helps Banks and Examiners Stay on Top of Changing Regulations

The Compliance Policy Department helps define and implement OCC policies as they relate to consumer protection and anti-money laundering laws. The department is responsible for developing written examination procedures, preparing guidance to the banking industry and to OCC examiners, and analyzing data required under the Home Mortgage Disclosure Act (HMDA) and the Bank Secrecy Act (BSA). OCC examiners evaluate bank compliance and, when weaknesses are noted, take corrective action.

Because regulations do change, one of Compliance Policy's most important functions is training other OCC staff in classroom settings and in virtual workshops that allow examiners to share knowledge with their peers around the country. Compliance Policy works closely with OCC legal staff in interpreting the supervisory impact of often complex compliance laws and regulations.

Compliance Policy's employees are also involved in outreach to the industry, speaking at trade association meetings and educational forums. They partner with the OCC's Banking Relations division in telephone seminars, where they can explain regulatory changes to bank compliance officers and discuss how the OCC will implement those changes.

Changing regulations is just one of many compliance challenges facing banks, says Ann Jaedicke, the OCC's Deputy Comptroller for Compliance Policy. Large banks that conduct millions of consumer transactions from thousands of branches around the country face large compliance risks and responsibilities. For smaller banks with perhaps a few dozen employees, the main challenge is often that the compliance officer may have many additional duties and still have to stay current with dozens of changing government regulations.

Jaedicke relies on her staff of experienced examiners—many with 25 years or more experience—to

provide the judgment needed to deal with difficult compliance issues. The Community Reinvestment Act (CRA) is a good example. "It's not easy to figure out if the banks have done enough to serve a community's credit needs. How much is enough? Or to determine which bank's businesses are more susceptible to money laundering. Or to determine if a particular practice by a bank is unfair or deceptive. These are not easy decisions." OCC's Community Affairs Officers, who are part of the Chief Counsel's office, have regional and local expertise on community and consumer organizations and issues and provide technical support to compliance examiners on such matters as CRA assessment area delineation, community development and investments, and other aspects of CRA compliance.

For Jaedicke, these are "issues that are large in scale, and many deal directly with the everyday lives of people. There's a real human element to compliance work—anyone with a credit card or a mortgage loan feels the effects of what we do."

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## Fair Lending, Fair Treatment, and Fair Access Are Key Priorities

The OCC deployed a broad range of resources to ensure national bank compliance with fair lending, consumer protection, and CRA requirements. That kind of commitment, as Comptroller Dugan noted in a July speech to OCC compliance specialists, is particularly important in challenging times, because

no bank, struggling or otherwise, can afford to assume the additional reputation and compliance risk that can be associated with potential compliance lapses.

Compliance complacency is most likely to arise when bank management is preoccupied with safety and soundness issues. Yet bankers cannot rest on a past record of success. They must be as attentive to their compliance responsibilities in difficult times as they are when the pressure of events eases.

To ensure that banks meet these responsibilities, the OCC



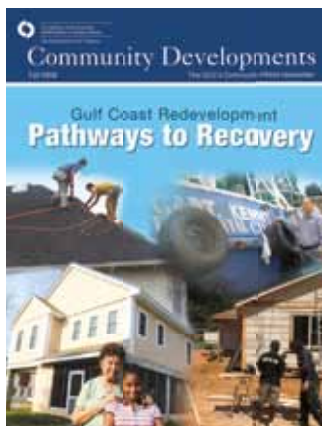
*Comptroller Dugan addresses the OCC's 2008 Fair Lending Conference.*

assesses and monitors compliance risk in each of the institutions under its supervision. Examiners can call on the OCC's economics team, which supplies statistical analysis that can aid in targeting portfolios that may have higher potential for fair lending problems. OCC Community Affairs Officers, located throughout the country, provide examination support on CRA requirements and compliance.

To underscore the OCC's commitment to fair lending supervision and advance the state-of-the-art in fair-lending risk modeling, the agency's Economics Department sponsored a fair lending conference in New Orleans that brought econometric specialists, bankers, and regulators together in an effort to improve identification of fair lending issues that may require supervisory attention.

Another key compliance resource is the OCC's Office of the Ombudsman. The Ombudsman and staff serve not only as an outlet for bank consumer complaints and for resolving supervisory disputes between examiners and bankers; they are also a valuable supervisory resource, helping to identify consumer compliance issues at their earliest stages. This information can become a crucial resource to the OCC in developing risk-based supervisory strategies for national bank compliance examinations. (See *"Office of the Ombudsman Ensures Fair, Expedient Resolution of Complaints"* on page 38.)

Ultimately, the OCC believes compliance is inseparable from safety and soundness. But compliance is also vital in its own right. Especially when consumer confidence in the financial services industry is being tested by events, it's critical that banks demonstrate their commitment to fair play, fair lending, and fair treatment for all consumers. The OCC's compliance program is there to provide further support to public confidence.



## Attorneys Provide Counsel, Expertise to Supervisory Team

Payment transactions in our economy are increasingly processed through automated systems with complex network rules and contractual relationships. If not properly controlled, transactions conducted through these mechanisms can pose significant risk to banks and counterparties. To monitor and respond to developments in connection with these automated systems, the OCC established a Payments System Working Group in 1994. Special Counsel Jonathan Fink represents the OCC's Law Department on that working group.

For Fink, who works in the Bank Activities and Structure Division, it's been an opportunity to add a new specialization to an already impressive list of practice areas that include problem bank resolutions, lending limits, affiliate and insider transactions, "golden parachute" payments, and uniform commercial code issues. He also serves as a mentor to less experienced OCC attorneys—a side of his job that he says "gives me as much satisfaction as anything else I do."

His work on payments systems requires him to be expert and up-to-date on developments in the law, technology, and banking. Payment systems are not only susceptible to hardware and software failures but also to fraud, malicious damage, user error, and other operational risks. As evidenced by several recent cases—one involving criminal interception of credit card data and another of a national bank accepting fraudulent checks generated by a processor for telemarketers—such risks can lead to enormous harm to merchants, consumers, and the financial institutions that serve them.

Fink and his colleagues in the working group have addressed those issues through several key pieces of supervisory guidance, which elaborate on the operational and other risks that can arise in connection with payments system and funds transfer activities. The guidance also spells out the safeguards national banks should put in place to manage those risks, to protect themselves and their customers.

But Fink recognizes that it is not enough to release supervisory guidance and hope for the best. With others, he works hard to explain that guidance in presentations to both banker and examiner audiences. “I’ve also been out in the field with the examiners, in the banks, helping them to identify problems. And, at the same, taking part in our exams has helped enrich my own understanding of payments-system practices—and malpractices.” Although technology keeps advancing and it takes continued effort to stay ahead of those who would misuse the systems, the agency’s comprehensive, hands-on approach to payments-system risk management seems to be working: the agency’s automated clearinghouse (ACH) risk management guidance has caused banks to tighten their risk management and internal controls.

The OCC’s risk-based approach to supervision also extends to the Office of the Chief Counsel, and in a time of financial turmoil attorneys like Fink find themselves devoting larger chunks of their time to problem bank issues: preparing legal analyses, supporting administrative actions, contributing to supervisory strategy, and helping to evaluate a troubled bank’s prospects. “At a time like this, we all have to be prepared to do whatever the situation demands of us,” he says. Fink brings a breadth and depth of experience that makes him an invaluable OCC resource.

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## OCC Presses Other Regulators for a Unified and Simpler Consumer Complaint Process

Consumer complaints about lenders and depository institutions made national news in fiscal year 2008. One of the most common sources of consumer frustration related to the difficulty of identifying and reaching the right regulator of a particular bank, thrift, or credit union.

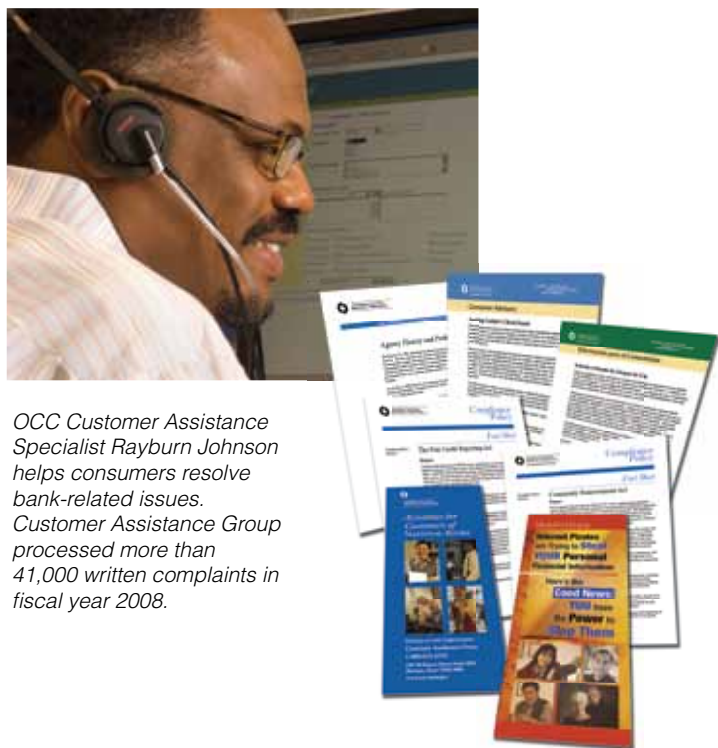
Federal agencies, including the OCC, agree that the best way for consumers to resolve their concerns is to contact their banks directly, but the agencies also recognize that individual customers cannot always reach fair or satisfactory resolutions on their own.

“When direct contact with the bank does not resolve an issue, figuring out where to turn next may be very challenging. The OCC believes this burden should not fall upon the consumer,” OCC Chief of Staff and Public Affairs John G. Walsh says. “It is incumbent upon federal banking agencies to make improvements in these areas to better serve consumers.”

“Frankly, our comprehensive approach to consumer protection—integrating guidance, supervision, enforcement, and complaint resolution—is not well understood,” Comptroller Dugan has said in testimony to members of the Committee on Financial Services of the U.S. House of Representatives.

Throughout the year, the OCC continued the process of simplifying customer assistance and increasing public awareness. The agency’s efforts involved working with state and federal regulators and making its own customer assistance group more accessible to customers of national banks.

In August 2008, the OCC reached a significant milestone in state and federal collaboration by signing the latest of 42 memoranda of understanding with state banking regulators. The memoranda establish a formal basis for sharing complaint information among regulators while also protecting confidential customer information. Further easing the burden of sharing complaint



*OCC Customer Assistance Specialist Rayburn Johnson helps consumers resolve bank-related issues. Customer Assistance Group processed more than 41,000 written complaints in fiscal year 2008.*

information, the OCC is promoting use of its new Web-based system, Complaint Referral Express. Among the first states to take advantage of the system are California, Colorado, Florida, New York, and Texas. The system allows the OCC and other regulators to exchange complaint information electronically, thus eliminating the time-consuming and costly process of mailing and faxing.

Through the Federal Financial Institutions Examination Council, the OCC also continues to work with federal regulators on making the consumer assistance process more streamlined and consumer-friendly. The council has been working on proposals to create a toll-free number to assist customers of all federally regulated banks, thrifts, and credit unions; to develop a joint Web site to allow bank customers to look up a bank's regulator more easily; and to conduct a campaign to increase public awareness of federal customer assistance programs.

Because the national banking system touches so many lives, the OCC recognizes the importance of working independently as well. The agency's Public Affairs Department continues to produce and distribute public service items to local newspapers and radio stations around the country to educate consumers about banking regulatory issues and to promote awareness of OCC customer assistance products and services, such as HelpWithMyBank.gov and the toll-free customer assistance number, 800-613-6743.

Since launching our public service campaigns, articles and radio spots have run nearly 8,000 times in 41 states and covered such topics as gift cards, foreclosure prevention, debt-elimination scams, and promotion of the agency's customer assistance process and consumer Web site. These public service announcements, which provide important information to America's financial consumers, have been seen or heard by a potential audience of more than 900 million people. The effort contributed to the increasing popularity of HelpWithMyBank.gov. During an average month in fiscal year 2008, the site received more than 28,000 visits from people looking for answers to basic

banking questions and information about how to contact a bank's regulator.

In June 2008, the National Association of Consumer Agency Administrators recognized the OCC for its educational outreach efforts and outstanding Web site.

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## OCC Steps Up Efforts To Support Minority Banks

The OCC remains committed to preserving the health of minority banks and recognizes them as key contributors to the economic viability of minority and low-income communities. This commitment links directly to the OCC's objective of ensuring that national bank customers receive fair and equal access to financial services. It's a commitment that's been evident in the agency's minority bank initiatives that have evolved over the years.



*Public Affairs Specialist Stephanie Powell's work with minority bankers underscores the OCC's commitment to this important sector of the banking system.*

Responding to valuable feedback from chief executive officers of minority banks and an analysis of data from a recent survey, the OCC in fiscal year 2008 revised its policy, initiated new activities, and modified previous efforts regarding minority banks.

For example, the OCC issued an updated Policy Statement on Minority-Owned National Banks to reaffirm its support for this banking sector. Comptroller Dugan says the OCC took this step in part to "take account of changes in the business environment in which minority national banks operate. But I also wanted to reissue the statement to reaffirm my own commitment—and that of the

OCC—to minority institutions. These banks provide vital services to minority communities, and the OCC is strongly committed to supporting them.”

To keep minority banks up-to-date on agency policies, guidelines, and activities, the OCC’s Senior Advisor for External Outreach and Minority Affairs, part of the agency’s Public Affairs Department, launched *OCC Highlights*, an e-mail newsletter with regulatory and legislative matters of interest to minority financial institutions. The OCC sends the newsletter to national and other minority banks and posts it on the agency’s Web site, along with a feedback mechanism to help the agency determine whether its online resources are meeting minority bankers’ needs.

However, online resources cannot serve as substitutes for face-to-face communication. So when two agency executives assumed new responsibilities that included working closely with minority national banks, the appointees participated in meetings and roundtables with minority bank chief executive officers. Such interaction—initiated by the Senior Deputy Comptroller for Midsize and Community Bank Supervision and the Ombudsman—won the agency considerable praise among its minority bank constituents. “Mere words cannot adequately express how appreciative I am of OCC representatives’ professionalism and willingness to provide assistance when needed,” Commonwealth National Bank Chairman Michael Pierce says.

Feedback from surveys and roundtable discussions with minority bank chief executive officers also revealed this banking sector’s diversity. Taking into account differences among these banks, Midsize and Community Bank Supervision staff members have encouraged Assistant Deputy Comptrollers and portfolio managers to develop and implement supervisory strategies tailored to meet the technical assistance needs of every national community bank.

To learn more about the diversity and commonalities among minority banks, the OCC participates in interagency efforts, such as the Interagency Minority Depository Institutions National Conference, which the OCC cohosted for a third consecutive year. In 2008, Comptroller Dugan served on a regulatory panel, and other OCC experts served on panels that addressed such topics as measuring and monitoring risk exposures and restructuring debt.

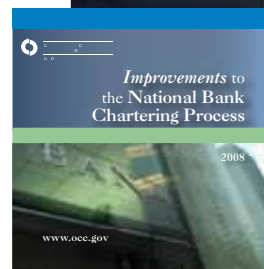
## OCC Improves the National Bank Chartering Process

The OCC has a longstanding commitment to a vibrant national community bank program, so it was a matter of concern that only 15 percent of newly chartered community banks chose the national bank charter over the last 10 years. To understand why so few new community banks have chosen the national charter, Comptroller Dugan in 2007 created a de novo (or new) bank charter working group. He charged this group with identifying the considerations most relevant to bank organizers making charter decisions, as well as determining any impediments to obtaining a national bank charter.

The working group’s recommendations led the OCC in 2008 to simplify and enhance the chartering process, which now features decreased application costs, increased assistance prior to formal filing, better communications, fewer impediments to raising capital, and greater efficiency.

These changes are consistent with the OCC’s goals of improving operations and reducing unnecessary regulatory burden. National bank officers and directors have ready access to a significant package of OCC resources and professional staff, including bank chartering and related corporate specialists, seasoned examiners and their senior managers, and legal staff. While the bank chartering process continues to evolve, one thing remains constant: the OCC’s high-quality, professional supervision across the nation.

*Application costs and processing delays have been reduced.* The OCC has suspended licensing application fees for those seeking national bank



charters as well as for other licensing transactions, such as business combinations. Many of these changes significantly reduce the overall cost of obtaining a national bank charter. At the bank organizers' request, the OCC can begin personal background checks earlier in the process to help avoid delays later on. Draft applications and business plans can be submitted for preliminary review and feedback.

*More assistance is provided prior to filing.*

When an organizing group contacts the OCC about becoming a national bank, agency staff members organize an exploratory meeting to explain the charter process, offer technical assistance, and discuss options to address the unique features of the group's proposal. Bank charter experts are available to travel to the organizers for exploratory and pre-filing meetings. On request, these experts review draft applications, business plans, and other pertinent documents and respond as needed with feedback. District licensing staff members work with organizers, answer questions, and provide reports on application status. Organizers meet key OCC personnel who in turn maintain close contact with FDIC officials regarding the bank's insurance

application. The examiners who will provide supervision once the bank is chartered may meet with the organizers as well.

*Impediments to raising capital have been reduced.* The OCC has expedited its review of bank securities offering materials. No fidelity insurance is required for raising capital if the escrow agent has insurance or is bonded, and audited financial statements are no longer required at the in-organization phase. From now on, only national banks with 500 or more shareholders will be required to file reports under the provisions of the Securities Exchange Act. Previously the threshold was 300.

*Greater efficiencies have been achieved.* The OCC has streamlined policies and procedures to focus on safety and soundness issues and the overall viability of the proposal. The OCC's special legal lending limit rules expanding lending opportunities are now available to new national banks. The actions of district offices are better coordinated with those of OCC headquarters. More than ever before, the OCC and its examining staff stand behind a commitment to a robust system of national community banks.



## Section Three Organizational Highlights

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### Chief Counsel’s Office Focuses on Bank Safety and Soundness, Customer Products and Services

#### *Bank Safety and Soundness*

The OCC strives to maintain a flexible legal and regulatory framework that enables the national banking system to provide a full, competitive array of financial services. In fiscal year 2008, the OCC published a final rule to reduce unnecessary regulatory burden and revise and update OCC regulations. The final rule updated and revised the qualifying standards and after-the-fact notice procedures that apply to national bank operating subsidiaries. The rule also expanded the list of operating subsidiary activities that are permissible upon filing an after-the-fact notice.

Other revisions in the rule reduced the burden associated with applications for fiduciary powers and intermittent branches, change-in-bank control notices, and requirements to make securities filings. The final rule incorporated previously published interpretive opinions concerning, for example, electronic banking activities, to harmonize the OCC rules with those of other federal agencies, to reflect recent statutory changes, and to make technical and conforming amendments to improve clarity and consistency. The OCC amended our securities offering disclosure rules to eliminate the general requirement that a national bank in organization include audited financial statements in a public offering.

As described in the “State of OCC Supervision” section, the OCC published several rules implementing sections of the Fair and Accurate Credit Transaction Act of 2003 and rules implementing the aspects of the Basel II Capital Accord.

Comptroller Dugan stated in March 2008 that the OCC would play a positive and constructive role in the discussion of the Department of the Treasury’s Blueprint for a Modernized Financial Regulatory Structure.

The OCC provides regulatory oversight practices and interpretive letters that support national banks’ ability to compete while maintaining safety and soundness. We issued our annual publication, *2007 Significant Legal, Licensing, and Community Development Precedents for a National Bank*, as well as the cumulative companion edition of *Activities Permissible for a National Bank: 2007*. Interpretive letters issued during fiscal year 2008 included opinions on permissible types of derivatives transactions, including property index derivative transactions and derivative transactions associated with designated types of natural events and catastrophes, as well as a specification of types of securities a bank may purchase and hold to hedge permissible equity derivatives transactions.

Other interpretive letters dealt with risk-based capital requirements for synthetic securitizations



based on home equity lines of credit and loans, and risk-based capital credit conversion factors applicable to a liquidity facility.

We issued a preemption opinion on the ability of an operating subsidiary to export interest rates and fees from the bank's home state, on charges to non-account holders for cashing official checks, and on the offering of debt cancellation contracts through auto dealers. In addition, the Second Circuit Court of Appeals denied the New York Attorney General's petition for rehearing on prior court findings that the Attorney General did not have authority to investigate real estate lending by national banks or their operating subsidiaries, with reference to the OCC's exclusive visitorial authority.

The agency will continue in fiscal year 2009 to consider and issue opinions on the safe and sound implementation of bank activities and products. The OCC will also continue to provide case-by-case analysis, when appropriate, for the applicability of state law and the exclusivity of the agency's visitorial authority under the national banking laws, in order for national banks to operate efficiently under uniform national standards.

### ***Protecting Consumers***

The OCC examination program addresses problems and noncompliance arising from unfair treatment of bank customers, including failure to meet requirements for proper disclosures relating to financial products and services.

In fiscal year 2008, the OCC entered into a formal agreement with a large national bank, directing the bank to make restitution to consumers harmed by its relationships with telemarketers and third-party processors. The estimated restitution could exceed \$125 million. In addition to the restitution payments, the bank was also required to contribute approximately \$8.9 million to consumer education programs directed at the elderly, and to pay a \$10 million Civil Money Penalty (CMP). The OCC found that the bank engaged in unsafe and unsound practices in its relationships with payment processors and telemarketers and unfair practices under the Federal Trade Commission Act. The practices cited by the OCC involved the

use of remotely created checks after telemarketers obtained bank account information over the phone to offer consumers a range of questionable products and services. The OCC found that the bank profited from the fees and bank balances generated by these activities and failed to take action to terminate the account relationships when it became aware of the problem.

### ***Addressing Criminal and Terrorist Misuse of the Banking System***

The OCC is committed to preventing criminals and terrorists from misusing the financial system and to supporting law enforcement efforts to detect and prosecute criminal activities. This work is often carried out in partnership with other federal financial institutions regulatory agencies, the Financial Crimes Enforcement Network (FinCEN), and law enforcement.

OCC examiners evaluate each national bank's compliance with Bank Secrecy Act/Anti-Money Laundering (BSA/AML) requirements; when they observe problems with a bank's BSA compliance program, the agency seeks corrective action from the bank. The OCC investigates national banks that fail to meet BSA/AML requirements and takes enforcement actions against them. In fiscal year 2008, for example, the FinCEN and the OCC each assessed CMPs of \$15 million against a federal branch of a foreign bank for alleged violations of the Bank Secrecy Act, which the bank agreed to pay under a consent order. The bank had a history of noncompliance with OCC cease and desist orders relating to Bank Secrecy Act deficiencies and requirements to terminate wire transfers, dollar drafts, and pouch transactions.

### ***Enforcement Actions Against Bank Insiders and Third Parties***

Actions against insiders included cease and desist orders, restitution orders, the assessment of CMPs, and prohibition orders. Insiders may be the subject of these actions for misrepresentations in regulatory filings, self-dealing, or misappropriating bank funds, and other improper practices in loan administration, use of bank premises, bank expenses, and exercise of fiduciary duty.

The OCC also takes action against institution-affiliated parties whose actions in a professional capacity in relation to the bank meet certain standards of misconduct or are otherwise illegal.

The OCC's Fast Track Enforcement Program uses information from suspicious activity report filings to pursue prohibition or other enforcement actions when bank insiders and other institution-affiliated parties committed criminal acts or acts of significant wrongdoing involving banks, but no action was taken by law enforcement.

Figure 9 summarizes enforcement actions taken in fiscal year 2008.

of national bank assets, and foreign branches and agencies.

The department works closely with bank supervision and other legal units on the viability and legality of proposals for dealing with problem banks. Proposed restructurings that may avoid bank failures and their associated costs can include mergers, purchases and assumptions, and chain bank structures.

The OCC made several significant licensing decisions involving national bank business realignments and acquisitions. In addition, the OCC implemented streamlined regulatory requirements and process improvements for de novo bank

Figure 9: **Enforcement Actions**

<b>Enforcement Actions, FY 2008</b>	<b>Against Banks</b>	<b>Against Institution-Affiliated Parties</b>
Cease and Desist Orders	20	14
Temporary Cease and Desist Orders	0	0
12 USC 1818 Civil Money Penalties	3	27
12 USC 1818 Civil Money Penalties Amount Assessed	\$25,007,500	\$662,000
Flood Insurance Civil Money Penalties	7	0
Flood Insurance Civil Money Penalties Amount Assessed	\$323,725	\$0
Restitution Orders	1	2
Amount of Restitution Ordered	\$125,000,000	\$11,100
Formal Agreements	51	0
Individual Minimum Capital Ratio Letters	9	0
Memoranda of Understanding	17	0
Commitment Letters	7	0
Suspension Orders	0	0
Letters of Reprimand	0	13
12 USC 1818 Removal/Prohibition Orders	0	32
12 USC 1829 Prohibitions	0	203
<b>Total Enforcement Actions</b>	<b>115</b>	<b>291</b>

Source: OCC data for fiscal year 2008.

### ***Licensing Decisions***

The Licensing Department establishes policies and procedures for OCC's processing of corporate applications involving national banks and foreign banking organizations. These functions are performed on a decentralized basis. Corporate structure changes requiring OCC approval include new bank charters, conversions to the national charter, national bank merger (or business combinations), corporate reorganizations, changes in control, operating subsidiaries, branches, relocations, capital and subordinated debt issuances, contraction

charters, resulting in reduced costs and barriers and enhanced value of the national bank charter.

To address potential safety and soundness problems before they arise, the OCC may impose conditions upon bank transaction approvals covering capital and liquidity arrangements and deviations from business plans.

In fiscal year 2009, the OCC plans to implement improved methods for accessing licensing application information from the agency's public Web site.

*Continued on page 38*

Figure 10: Licensing and Customer Service Performance Measures

Performance Measures	Target	Actual
Percentage of licensing applications and notices filed electronically	40%	46%
Percentage of licensing applications and notices completed within established time frames	95%	95%
Average survey rating of the overall licensing services provided by OCC	≤ 1.50	1.22

Source: OCC data for fiscal year 2008.

Figure 11: Corporate Application Activity

	Applications Received		Fiscal Year 2008 Decisions			
	Fiscal Year 2007	Fiscal Year 2008	Approved	Conditionally Approved <sup>4</sup>	Denied	Total <sup>5</sup>
Branches	1,673	1,251	1,247	12	0	1,259
Capital / Sub Debt	135	170	69	7	0	76
Change in Bank Control	8	5	0	2	0	4
Charters	32	33	1	27	0	28
Conversions <sup>1</sup>	25	7	3	5	0	8
Federal Branches	1	3	0	3	0	3
Fiduciary Powers	6	11	3	0	0	3
Mergers <sup>2</sup>	49	46	44	1	0	46
Relocations	277	291	279	2	0	283
Reorganizations	108	111	93	17	0	111
Stock Appraisals	2	1	0	0	0	0
Subsidiaries <sup>3</sup>	14	23	13	5	0	18
12 CFR 5.53 Change in Assets	4	5	0	4	0	4
LTD NB Upgrade	2	0	0	0	0	0
<b>Total</b>	<b>2,336</b>	<b>1,957</b>	<b>1,752</b>	<b>85</b>	<b>0</b>	<b>1,843</b>

Source: OCC data for fiscal years 2007 and 2008.

<sup>1</sup> Conversions are conversions to national bank charters.

<sup>2</sup> Mergers include failure transactions when the national bank is the resulting institution.

<sup>3</sup> This count does not include 81 after-the-fact notices received in fiscal year 2007 and 84 after-the-fact notices received in fiscal year 2008.

<sup>4</sup> On April 14, 2000, the Licensing Department issued guidance imposing special conditional approval for all bank charters requiring the OCC to be notified before a significant deviation or change in the operating plan during the first three years of operation.

<sup>5</sup> Total includes alternative decisions or no objections.

Figure 12: OCC Licensing Actions and Timeliness

Application Type	Fiscal Year 2007				Fiscal Year 2008		
	Target Time Frames in Days <sup>1</sup>	Number of Decisions	Within Target		Number of Decisions	Within Target	
			Number	Percent		Number	Percent
Branches	45/60	1,729	1,690	98	1,259	1,222	97
Capital / Sub Debt	30/45	71	59	83	76	70	92
Change in Bank Control	NA/60	6	6	100	4	3	75
Charters 2		30	13	43	28	17	61
Conversions	30/90	11	9	75	8	8	73
Federal Branches	NA/120	0	0	0	3	2	67
Fiduciary Powers	30/45	4	3	75	3	3	100
Mergers	45/60	40	54	84	46	36	90
Relocations	45/60	257	251	98	283	274	97
Reorganizations	45/60	94	84	89	111	98	88
Stock Appraisals	NA/90	0	0	0	0	0	0
Subsidiaries	NA	31	31	100	18	15	83
12 CFR 5.53 Change in Assets	NA/60	4	2	50	4	4	100
LTD NB Upgrade 3		1	0	0	0	0	0
<b>Total</b>		<b>2,278</b>	<b>2,183</b>	<b>96</b>	<b>1,843</b>	<b>1,758</b>	<b>95</b>

Source: OCC data for fiscal years 2007 and 2008.

Note: Most decisions (99 percent in 2007 and 98 percent 2008) were decided in the district offices and Large Bank Licensing under delegated authority. Decisions include approvals, conditional approvals, and denials.

<sup>1</sup> Those filings that qualified for the “expedited review” process are subject to the shorter of the time frames listed. The longer time frame is the standard benchmark for more complex applications. New time frames commenced in 1997 with the adoption of the revised Part 5. The target time frame may be extended if the OCC needs additional information to reach a decision, permits additional time for public comment, or processes a group of related filings as one transaction.

<sup>2</sup> For independent charter applications, the target time frame is 120 days. For holding-company-sponsored applications, the target time frame is 45 days for applications eligible for expedited review, and 90 days for all others.

<sup>3</sup> Ibid. 2.

Figure 13: Change in Bank Control Act <sup>1</sup>

Year	Received	Acted On	Not Disapproved	Disapproved	Withdrawn
2008	5	4	4	0	0
2007	6	6	0	0	0
2006	9	8	4	0	4
2005	17	17	17	0	0
2004	16	14 <sup>2</sup>	13	0	0

Source: OCC data for fiscal years 2004–2008.

<sup>1</sup> Notices processed with disposition.

<sup>2</sup> Includes one notice with no activity. The OCC considered it abandoned.

Figure 14: **List of Applications Presenting Community Reinvestment Act Issues Decided**

<b>Bank, City, State</b>	<b>Interpretations and Actions Publication Date</b>	<b>Document Number</b>
PNC Bank, National Association, Pittsburgh, Pennsylvania (merger)	February 2008	CRA Decision No. 141
TD Banknorth, National Association, Portland, Maine (merger)	May 2008	CRA Decision No. 142
Wachovia Bank, National Association, Charlotte, North Carolina (new branches)	May 2008	CRA Decision No. 143

Source: OCC data for fiscal year 2008.

### **Community Affairs**

The Community Affairs Department provides technical support to OCC compliance examiners, conducts consultations with bankers on CRA and community development, and trains bank CRA officers through the OCC’s national network of Community Affairs Officers.

The department also processes national bank community development filings. In fiscal year 2008, national banks made 329 community development investments, which totaled \$3.7 billion, under the public welfare investment authority of 12 CFR 24.

In fiscal year 2008, Community Affairs sponsored or represented the OCC at nearly 100 conferences and meetings focused on community investment and development structures and opportunities, including cosponsoring the annual National Interagency Community Reinvestment Conference and a Minority-Owned Institutions Conference. The department worked with other government entities and engaged in discussions with community and consumer organizations on such topics as affordable housing, foreclosure avoidance, preservation of foreclosed properties, payment and debit card products, and alternatives to traditional credit-scoring models. Community Affairs staff also supported the agency’s participation in NeighborWorks America, a national nonprofit organization created by Congress to provide financial support, technical assistance, and training for community-based revitalization efforts, as well as federal financial literacy and consumer protection programs. The department organized Comptroller Dugan’s tour of New York City neighborhood community development projects benefiting from national bank investments.

Community Affairs provided loan and foreclosure data and community mapping analyses in support of OCC policy and processes. The department also continued the community development-oriented publications program with the issuance of a consumer advisory on avoiding mortgage fraud and publications on low-income housing tax credits, the Small Business Administration 7(a) loan program, multibank community development banks, and preservation of affordable rental housing. Publications and related information are made available through a variety of media, including the OCC Web site and Web-based seminars.

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### **Office of the Ombudsman Ensures Fair, Expedious Resolution of Complaints**

In March 2008, Comptroller Dugan appointed Larry Hattix as the agency’s second Ombudsman since the office was created in 1993. The Ombudsman serves as an objective arbiter to resolve bank appeals independent of the OCC’s supervisory process.

The Office of the Ombudsman is organized around the core principles of dispute resolution and customer service. The office seeks to ensure that national banks and customers of national banks receive fair and expeditious resolution of their complaints through two distinct processes within the office. The National Bank Appeals Process is designed to resolve disputes of national banks arising from the supervisory process. The Customer Assistance Group (CAG) focuses on ensuring that customers of national banks receive fair treatment in resolving their complaints with national banks.

## ***National Bank Appeals Process***

The appeals process is designed to provide banks with an independent, fair, and binding means of settling disagreements that can arise from OCC supervisory actions or decisions. National banks can make informal inquiries or file formal appeals in strict confidence without fear of retaliation. With the Comptroller's consent, the Ombudsman can stay a pending decision or action until the appeal is resolved. In fiscal year 2008, the Ombudsman received 21 formal and informal appeals and substantive inquiries, in addition to numerous general inquiries.

Separate from the appeals process, the OCC assesses the effectiveness of the supervisory process through an examination questionnaire administered by the Office of the Ombudsman. The questionnaire is provided to all national banks at the conclusion of their 12- or 18-month supervisory cycle. The questionnaire is designed to gather direct and timely feedback from bankers on the OCC's supervisory program.

## ***Customer Assistance Group***

For Fiscal Year 2008, the OCC's CAG received more than 90,000 telephone calls from customers of national banks and processed more than 41,000 written complaints. While credit cards remain the product with the highest number of complaints, comprising nearly 40 percent of all complaints received, complaints related to both home mortgage loans and home equity products increased significantly. In 2008, national banks returned more than \$10 million in fees and charges to customers.

The OCC launched HelpWithMyBank.gov in July 2007. This is a consumer-focused Web site designed to provide self-service assistance to bank customers on a wide array of topics. It includes a frequently asked questions area, tools to determine if a particular financial institution is regulated by the OCC, and step-by-step instructions on how to file a complaint. In its first year of operation, over 333,000 individuals visited the site and downloaded more than 26,500 consumer complaint forms.

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## **Management, Information Technology, and Governance Help the OCC Maintain Skilled Workforce**

### ***Human Resources***

The OCC's success in supervising and regulating the national banking system depends on the capabilities, effectiveness, and efficiency of our employees. Comptroller Dugan and the rest of the Executive Committee are committed to maintaining a diverse, highly skilled, motivated, and well-placed workforce.

The OCC's hiring and training programs are producing a high-quality staff. A large part of this effort is focused on successfully developing entry-level examiners into commissioned examiners with the skills to conduct and lead national bank examinations in a challenging economic environment.

Succession planning and transmitting institutional knowledge will be critical for the OCC to fulfill the agency's mission. Twenty-eight percent of the OCC's total workforce and 26 percent of examiners become eligible to retire over the next five years. The Committee on Bank Supervision oversees several programs designed to increase and strengthen examiner and leadership pools. For example, the OCC's Specialty Skills initiative provides examiners with a road map to develop their skills in eight specialty areas and will help ensure that the agency can supervise the increasingly complex array of activities and institutions in the national banking system.

The OCC recruits most of its entry-level employees on college campuses across the nation. In fiscal year 2008, the agency hired 122 entry-level examiners. This pool of examiners was distinctive not only for quality but also for diversity. Since the inception of this hiring program in 2003, the OCC has employed about 705 entry-level examiners. Of this group, 52 percent are women and 35 percent are minorities.

The agency's personnel strategy also encompasses an experienced-hire program, which brings in employees directly from the banking and finance industry, and programs that seek to identify and develop talent among existing employees.

The OCC has established an “on-boarding” program to acclimate newly hired examiners, new managers, and executives. All newly hired industry specialists are assigned mentors to smooth their transition. Mentors provide instruction in agency culture and policies, provide regular feedback on performance, and solicit comments on their initial experiences at the OCC.

Having recruited the highest quality people, the OCC works hard to retain them. To that end, the agency instituted an aggressive retention program. At regular intervals, surveys and focus groups give precommissioned examiners an opportunity to provide feedback on their OCC experiences and hear the OCC’s response. The OCC holds career forums at the three-year point to allow precommissioned examiners to interact with OCC senior leadership, learn about the Uniform Commission Examination, and plan for future opportunities in their OCC careers.

At the beginning of fiscal year 2008, the OCC ranked fourth on the Partnership for Public Service’s list of *Best Places to Work in the Federal Government* out of 222 subcomponents of large federal agencies. This independent rating is based on OCC employees’ responses to the Federal Human Capital Survey and reflects the OCC’s efforts to provide a professional, supportive workplace that helps to attract and retain outstanding employees. To that end, we strive to provide a comprehensive and competitive program of pay and benefits as stipulated in the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. In August 2008, Comptroller Dugan announced compensation and benefits decisions that allow the OCC to remain competitive among the federal bank regulatory agencies with which it competes most directly for personnel.

The agency has taken steps to encourage experienced examiners to transfer into the supervision policy group in headquarters and to large banks in major cities. To attract internal candidates, the OCC emphasized the importance of these assignments to career advancement and provided incentives, including relocation bonuses, mortgage subsidies, financial assistance for renters, and transitional cost-of-living reimbursements.

## ***Equal Opportunity and Workplace Fairness***

The OCC demonstrated commitment to equal employment opportunity and workplace fairness by:

- Continuing investment in a cadre of experienced third parties to assist employees in improving conflict management and communication skills through mediation, facilitation, and coaching techniques. OCC mediators conducted eight internal and nine external mediations. Participants rated the mediation experience as being “above satisfactory,” with participation rates exceeding the goals set forth by the Department of the Treasury.
- Using “Crucial Conversations” training as a shared approach to communicating difficult messages, clarifying expectations, and resolving disagreements. A cadre of 12 OCC employees, who are certified instructors, delivered “Crucial Conversations” training to more than 15 percent of the OCC workforce. Participants reported that the course exceeded their expectations.
- Enhancing dispute prevention, organizational awareness, and accountability by briefing the Executive Committee on equal employment opportunity and diversity program requirements. The OCC sponsored workshops on equal employment opportunity, alternative dispute resolution, diversity, and antiharassment principles in 20 field offices, in the Office of the Ombudsman, and for 12 Large Bank Supervision teams.
- Serving as a colead with the Department of the Treasury with the strategic goal of transforming the human capital occupation and as colead with the Bureau of Engraving and Printing on the Treasury Shared Neutrals (third-party servicers, such as mediators and facilitators) program.

## ***Technology***

In fiscal year 2008, OCC Information Technology Services (ITS) strived to improve front line customer service, optimize support for business applications, and stabilize the agency’s technical infrastructure. Highlights include:

- Improving front line customer support by realigning the ITS Technical Support organization to empower our technical support agents in the field.

- Enhancing remote access services to provide users in the field with better access to OCC information and applications. By deploying mobile.occ.gov, users can access OCC data and common applications anytime, anywhere, from any computer connected to the Internet.
- Enabling the Large Bank Supervision department to modernize its strategic resource planning by using the newly developed Strategies and Resources (STARS) application. With deployment in 2009, STARS will eliminate duplicative reporting processes and ease the burden of drafting the strategy document, while providing Large Bank Deputy Comptrollers with consistent information to supervise the entire large bank portfolio.
- Modernizing OCC's core messaging infrastructure to improve e-mail security reliability, capacity, and performance.
- Providing faster, more reliable deployments of new systems and IT products by strengthening and streamlining internal IT processes and procedures, such as the OCC System Development Lifecycle process.
- Deploying the Treasury Learning Management System. The system provides OCC staff with a robust training management portal through which users can register, track, and request approval for external training. Users of this system can identify and register for classes and participate in online training that is essential for their jobs or that promotes career growth.

In addition, as recognition of OCC's IT accomplishments in 2007, the OCC received the prestigious Archivist's Achievement Award at the 2008 National Archives and Records Administration Conference for the design and implementation of the Workflow and Information Systems and Document Manager electronic recordkeeping system.

### ***Information Technology Security and Emergency Preparedness***

In fiscal year 2008, the OCC Information Security Program expanded to achieve increased focus on policy, compliance, training, technical oversight, and audit. We published a revised Federal Information Security Management Act-compliant Information Technology Security Policy (Policy and Procedures

Manual 4000-1(REV)). The new policy aligned the OCC information security program with the Federal Information Security Management Act requirements and established a procedure for addressing other information security-related issues.

The OCC's Information Technology Services Department also improved documentation of the Information Security Program by identifying key policies, standards, and procedures. These were codified as information security goals, objectives, and strategies in the security policy. These policies are being measured with a comprehensive metrics program. The department's plan to improve and institutionalize information security at the OCC, known as "Information Security 2012," will be detailed in a forthcoming "Information Security Concept of Operations" publication.

A corrective actions process known as the OCC Plan of Actions and Milestones program, which was compliant with the National Institute of Standards and Technology and the Office of Management and Budget, was implemented with associated procedures, templates, and reports. The OCC reports program activities on a quarterly basis to the Department of the Treasury, which will use the information to provide overall departmental status to the Office of Management and Budget.

Using new engineering resources, our ITS Department strengthened its ability to detect and respond more quickly to computer security incidents and improved its coordination with other OCC units, the Treasury Computer Incident Response Center, and the Treasury Office of the Inspector General. OCC information infrastructure components and major computer applications are assessed regularly for risk. This includes undergoing full, continuous monitoring that is compliant with the National Institute of Standards and Technology and is required for the OCC to maintain accreditations awarded in fiscal year 2007. In fiscal year 2008, the department provided a security training program to all employees and contractors. The training focused on the confidentiality and integrity of OCC's information, regulations that govern OCC information systems, and potential threats and vulnerabilities that can undermine those systems.

The OCC continued to correct and mitigate management control deficiency findings from last year's financial audit. A project team worked collaboratively with all financial audit stakeholders



to implement the improvements needed to resolve the previous year's findings. A separate verification and validation process was established to test the effectiveness of the remediation activities on six of the repeat findings.

The OCC's Emergency Management Program prepares the agency to respond to emergencies that disrupt normal operations. The program ensures that the necessary plans, resources, and training exist to deal effectively with the full spectrum of emergencies the OCC could face. The OCC tested various elements of the OCC's Continuity of Operations Plan during fiscal year 2008 by participating in the government-wide Eagle Horizon National Level Exercise. This comprehensive exercise involving OCC staff throughout the country was designed to test the OCC's ability to perform mission-essential functions from multiple locations, including OCC headquarters, the OCC's designated primary site for continuity of operations, and the OCC's devolution site. Multiple response cells participated from these and other locations to test the OCC's response to scenarios that included a hurricane and terrorist activities. The OCC also participated with other financial sector entities in the three-week nationwide Financial and Banking Information Infrastructure Committee/Financial Services Sector Coordinating Council Pandemic Exercise. The OCC continues to update emergency strategies and plans with information from these tests to ensure that it is ready to respond to any threat to the safety of OCC employees or the interruption of our mission.

The OCC continued to develop a Homeland Security Presidential Directive 12 (HSPD-12) Program for Smartcard ID issuance. Employees will use that card to access OCC facilities and information systems. The OCC coordinated closely with the Treasury HSPD-12 Program Management Office and General Services Administration Managed Service Office to implement the Treasury Enterprise Solution for HSPD-12. The OCC acquired and installed an HSPD-12 card enrollment and activation station in the headquarters facility and began issuing HSPD-12-compliant credentials to employees. The OCC also established an HSPD-12 lab and began developing and testing solutions for using the new Smartcard IDs with the bureau's nationwide Physical Access Control System. The

OCC has begun to upgrade our control system infrastructure so that the new cards can be used to provide physical security at OCC offices.

### ***Process Improvement***

The OCC strives to enhance its business processes to improve the quality of process outputs and reduce rework and costs. An emphasis on support activities enables the Bank Supervision staff to better focus on supervision activities. During fiscal year 2008, the OCC initiated a review to determine how support processes deliver value to the agency. All critical processes will be evaluated by the end of fiscal year 2010, and deficiencies and problems discovered from the review will become key elements of OCC's organizational and process improvement agenda. During fiscal year 2008, the evaluation model was developed, and process improvement plans were completed for eight critical support processes. Processes reviewed included how the OCC determines compensation and contract administration processes.

Other improvement efforts are identified by management from internal customers' feedback or from efforts to continually improve business practices. Examples of efforts to improve the effectiveness and efficiency of programs in fiscal year 2008 included:

- Reengineering the performance evaluation process to stress the value added by managers and staff while reducing the OCC's administrative costs and burdens on managers and staff.
- Reviewing the customer assistance complaint review process to increase OCC's ability to address consumer complaints.
- Reengineering the contract examiner process to reduce the time to fill those positions and comply with regulations.
- Reengineering the contracting process to improve contract administration and controls.
- Reengineering the payroll processes to expedite and simplify payroll corrections and collections.
- Implementing a "Quick Wins" program throughout the Office of Management that encourages innovation and creativity by all staff to improve operations. The program suggestions improve the quality of outputs and reduce OCC

costs. Results range from saving a few hours to saving hundreds of hours and significant dollars.

For some reengineering projects, the OCC uses the Lean Six Sigma methodology, also used by many of the larger banks it regulates. The method allows the OCC to analyze business processes to improve quality and efficiency. This approach improves those business processes, eliminates waste, reduces the burden of compliance with statutory and regulatory requirements, and delivers more value to customers. Since fiscal year 2005, OCC has completed 70 of these projects for an annual savings in excess of \$5.5 million and allowed the OCC to make more effective use of employees.

### ***Improving Enterprise Governance***

To better align OCC's strategic planning, quality management, and business process improvement activities with strategic objectives and legal governance responsibilities, Comptroller Dugan established the Enterprise Governance unit in fiscal year 2007.

### ***Creating the Enterprise Governance Subcommittee of the Executive Committee***

The OCC established the Enterprise Governance Subcommittee during fiscal year 2008 to develop and coordinate issues related to strategic planning and enterprise risk management. The subcommittee oversees, on behalf of the Executive Committee, the following governance-support processes:

- Ensuring that strategic goals, objectives, and strategies are current and measured.
  - Updating the "Strategic Risk Management Plan" quarterly and placing it on the Executive Committee agenda for discussion.
  - Preparing the Comptroller's Annual Statement of Assurance.
  - Testing quality management programs for all major agency business processes.
  - Reviewing the results of other assurance activities, such as the external financial audit and the Treasury Office of the Inspector General and Government Accountability Office audits, and tracking corrective actions.
- Complying with applicable federal sector governance laws, regulations, directives, and standards.

### ***Program for Periodic Testing of Quality Management Practices***

During fiscal year 2008, the Enterprise Governance unit expanded testing of departmental quality management processes to all business units. Testing was completed within the Office of Management's Acquisitions Management unit, the Office of the Ombudsman, and Public Affairs Department. The unit is in the process of consulting with ITS to improve the quality management program. Testing will occur later in the Chief Counsel's Office, the Chief National Bank Examiner's Office, and Economics Department.

The process begins with an introductory consultation with the departmental manager about the nature of the risks inherent in the department's major business processes and the quality management practices that are used to manage those risks. The Enterprise Governance team tests sample aspects of these quality management programs for testing. The criteria used for evaluation are generally accepted as authoritative and provide a transparent framework for the consistent testing and evaluation of quality management programs across the OCC. They include:

- Applicable Office of Management and Budget (OMB) Circulars (primarily A-123), *Management's Responsibility for Internal Control*.
- Quality management principles (control/assurance/business process improvement).
- Government Accountability Office Standards for Internal Control in the Federal Government.
- *Criteria for Performance Excellence* (published by the National Institute of Standards and Technology).

## External Outreach Promotes Understanding of the OCC's Mission

OCC Public Affairs educates and informs the public about issues affecting the agency, the national banking system, and consumers. Reporting to the Chief of Staff and Public Affairs, the department manages the agency's internal communications and outreach to the media, Capitol Hill, bank customers, industry groups, civil rights organization, and the general public.

Through a series of public service announcements, Public Affairs promoted public education on such topics as foreclosure prevention; debt elimination schemes; gift cards; customer assistance; and the OCC's consumer Web site, HelpWithMyBank.gov, which provides information to consumers and facilitates the process of filing complaints when necessary. These public service messages, which promote financial literacy, have run more than 7,700 times in print and on radio, in 41 states, in both English and Spanish, since the program began in fiscal year 2007.

Public Affairs continued to improve the quality and quantity of information available on the OCC Web sites last year. HelpWithMyBank.gov, which has been answering common questions

about the national system since its launch in July 2007, reached nearly 200,000 national bank customers in fiscal year 2008 and earned recognition from the National Association of Consumer Agency Administrators as Web site of the year for its contribution to consumer education. Nearly 7,000 people have signed up for the OCC's RSS service, which provides an alternate source of news and information about the agency. In addition, over 20,000 people belong to the OCC's e-mail subscription lists.

In addition, Public Affairs' Banking Relations unit sponsored a range of industry outreach

programs, including workshops for bank directors, "Meet the Comptroller" sessions around the country, and programs for state associations that visit Washington. The Press Relations division produced 149 news releases during the last fiscal year, fielded calls from hundreds of reporters around the country, and

supported the agency's financial literacy program by getting important information on consumer concerns to the media. Other OCC units dealt with minority outreach (see "OCC Steps Up Efforts To Support Minority Banks" on page 29), Freedom of Information Act requests, publications, and internal communications.



# Section Four Financial Management Discussion and Analysis

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## OCC Focuses on Operational Excellence in Financial Management

### *Letter from the Chief Financial Officer*

I am pleased to present the OCC’s financial statements as an integral part of the *Fiscal Year 2008 Annual Report*. I am also glad to report that for fiscal year 2008 our independent auditors rendered an unqualified opinion with no material internal control weaknesses. The OCC’s commitment to effective financial management and a strong internal control environment continues to be my highest priority.

For the past several years, I have discussed the importance of our internal controls program. A strong internal control environment has never been more important. It serves as the foundation for accurate financial reporting as well as the safeguarding of agency assets. The OCC has diligently applied the concepts embodied in Office of Management and Budget Circular A-123, “Management’s Responsibility for Internal Control,” and where practicable, beyond. Our efforts in this

area are overseen by OCC executives and senior staff who meet at least monthly to monitor the status of the program. This year, there were no material control weaknesses identified through our testing process.

Circular A-123 presents an evolving program. In the past several years, the government charge card program and improper payments program have been incorporated into the A-123 oversight process. In the coming year, the OCC's acquisitions program will come under the A-123 process. We stand ready to devote the resources needed to ensure compliance with the spirit and intent of these enhancements to the A-123 program.

A strong internal control program also includes a constant review of processes. Several years ago, the OCC's Office of Management adopted the Lean Six Sigma methodology for improving administrative processes. Strong controls are the ultimate safety net in any process we design. However, inefficient administrative processes detract from the overall effectiveness of the agency and may decrease the hours available for staff to focus on the OCC's mission. This year, the OCC made major strides in this program. The Office of Management now can train and certify Lean Six Sigma blackbelts and greenbelts—the designations used for trained personnel who have successfully led Lean Six Sigma projects. The Office of Management has one master blackbelt, two blackbelts, and multiple greenbelts in multiple business units. An additional six blackbelts and 13 greenbelts will complete their training in fiscal year 2009, and all staff has received introductory training. In fiscal year 2008, 23 Lean Six Sigma projects were completed. Key projects in the Office of Management addressed the performance management, the contract administration, and staffing/recruitment processes. In total, our Lean Six Sigma productivity efforts allowed us to better serve our customers and generated more than \$2.3 million in savings as reported on the Office of Management "Balanced Scorecard." While this program focuses on improving overall administrative productivity, it also empowers our staff to continuously improve the processes that affect their working conditions.

Along with a strong internal control environment, the agency's financial condition remains sound. The structure of our balance sheet and annual operating budget has been influenced greatly by the influx of assets into the national banking system over the past five years. The increase in bank assets supervised has required the OCC to respond with corresponding

growth in bank examination staff, information technology infrastructure, and office space. As a non-appropriated federal agency, the OCC's primary sources of revenue are bank assessments and interest earned on investments. The majority of the agency's operating budget is allocated to personnel, travel, and rent. These three budget items accounted for almost 76 percent of the fiscal year 2008 operating budget. While the current economic situation and the impact on financial institutions are well-documented, our goal is to ensure that the agency's finances adequately support the OCC's mission.

The Budget and Finance Subcommittee, which I chair, closely monitors the OCC's overall financial condition. Meeting at least monthly, the subcommittee focuses on the agency's investment activities, office space needs, and financial reserves. The growth of our staff to meet bank supervision needs has generated a significant increase in leased office space. In the coming year, we will focus on our headquarters and data center leases. Because of the lead time needed to address leases of such magnitude, the process must begin soon to ensure uninterrupted operations for the agency. The subcommittee also reviews the performance of the agency's investment portfolio. During the past year, our portfolio has performed favorably compared against benchmarks with objectives and holdings comparable to those within the OCC's investment portfolio. Finally, the subcommittee examines the adequacy of agency reserves. Over the past several years, we have been prudent in maintaining our financial reserves at levels that allow us to provide the resources needed to supervise the national banking system, build a pipeline of future talent, and prepare for the expiration of our long-term leases.

Though fiscal year 2008 has been a year of achievement, the coming year will most likely offer new and significant challenges. To ensure we are ready to meet those challenges, we will continue to seek out the latest trends and best practices associated with financial management. To ensure we maintain the capabilities required to safeguard the OCC's assets diligently, I would like to repeat my commitment from last year—to ensure we have the finest people and resources dedicated to managing and monitoring the effective and efficient use of agency funds.



Thomas R. Bloom  
Chief Financial Officer

## ***Historical Perspective***

For the past few years, the Office of Management's Financial Management department (FM) has focused on delivering the best in customer service, stewardship of agency resources, and continuous process improvement. FM strove to promote a strong internal control environment, gain experience and expertise in continuous business process improvement, and develop a strong pipeline of present and future leaders to ensure continued progress for the department. Last year, FM began gathering benchmarking data for the department's major functional areas as an initial step toward evaluating operations against external organizations that are known for using best practices.

## ***Strategic Focus***

The cornerstone of FM's 2008 strategy is continuous improvement of business processes. FM focused heavily on staff and leadership development, and on increasing employee engagement as measured through the Gallup Q-12 Employee Engagement Survey. All department initiatives relied heavily on the voice of customers who are directly affected by FM processes, and process improvements were measured by increased quality, cost savings, and increased capacity.

## ***Strategic Goals***

FM's goal is to be an efficient organization that reflects:

- An engaged workforce committed to the business strategy of operational excellence.
- A solid understanding of customer needs and expectations.
- Efficient processes that take advantage of system capabilities.
- A focus on developing staff competencies for the evolving organization.
- Optimized costs in delivering products and services.

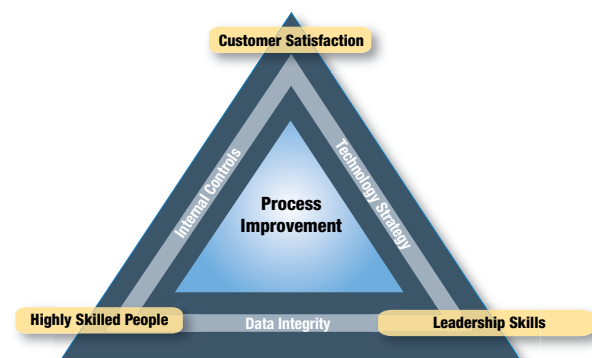
## ***Operating Strategy***

The FM operating strategy is shown in Figure 15. The strategy focuses on FM's most important business objectives, which include operating a robust process improvement program. As part of the department's efforts to improve management of financial systems, FM used Lean Six Sigma as the chosen tool for business process improvement.

Additional accomplishments include:

- Improving financial systems and their reporting capabilities.
- Refining the department's internal control and quality assurance program.
- Enhancing ongoing employee and leadership development efforts.
- Reducing FM costs as a percentage of OCC planned operating costs.

Figure 15: **FM Operating Strategy**

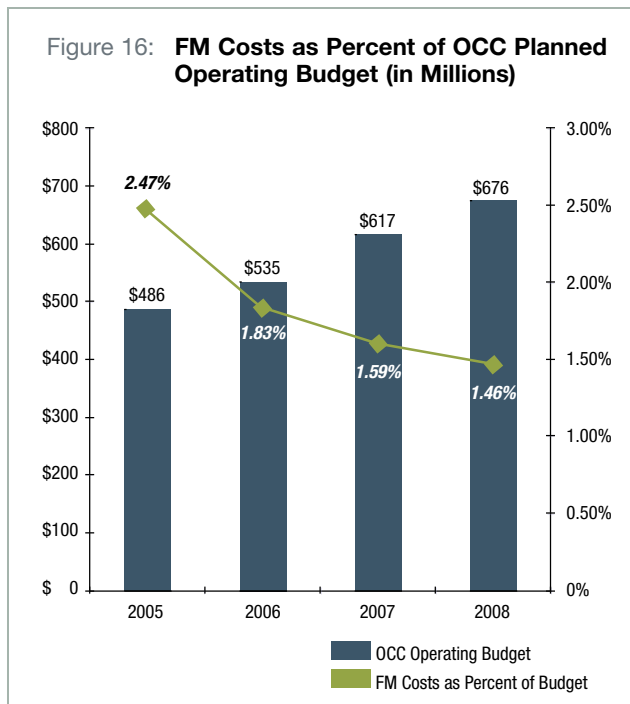


Source: OCC.

## Balanced Scorecard

The FM Balanced Scorecard contains performance measures and initiatives in four perspectives: financial, customer, internal processes, and learning and growth. The FM Balanced Scorecard is a framework that translates strategy into measurement.

The financial management perspective contains performance measures to ensure that FM is providing the best value to the OCC. In fiscal year 2008, FM continued the three-year trend of lower costs relative to the OCC planned operating costs, as reflected in Figure 16.



Source: OCC data for fiscal years 2005–2008.

The customer perspective ensures customers are identified and their needs and expectations are met. During fiscal year 2008, FM carried out a customer service action plan that used valuable input received from OCC customers through the 2007

annual customer satisfaction survey. FM engaged in ongoing dialogue with key customers and significantly improved the department's presence on the agency's intranet. FM published a series of targeted newsletters and improved coordination and review processes for communicating information to the agency with timeliness and clarity. In August 2008, FM participated again in the annual Office of Management OCC-wide customer satisfaction survey. FM management and staff will use the results of this year's survey to plan customer-focused initiatives in fiscal year 2009 and later.

The internal processes perspective ensures that FM focuses on improving processes that are most critical to achieving business goals. FM processes that had known inefficiencies, especially for customers, received the most attention and effort this year. During 2008, the department enhanced the process improvement program to incorporate the concept of continuous improvement into the FM culture.

The learning and growth perspective ensures that FM identifies the critical staff skills needed to achieve business goals and that management works with staff to ensure that those skills are fully developed. Each unit in FM continued working on Gallup Q-12 employee engagement survey action plans, and the department focused on developing the next generation of leaders. FM successfully continued augmenting staff by hiring undergraduate and graduate-level financial interns in fiscal year 2008, an effort that brings current learning in various disciplines and a fresh new perspective into the work environment. FM also continued to hire recent college graduates into the entry-level professional program, which is designed to develop the next generation of leaders in financial management.

## Looking Forward

FM will continue to focus on achieving strategic business goals and to measure progress by using the Balanced Scorecard and Lean Six Sigma. The department will continue benchmarking performance through key business metrics. Recognizing that financial management and financial reporting are much more than the mechanics of transaction processing and financial statement preparation, the department will continue to explore the latest business models including digitization and e-commerce. Finally, the department will continue to focus on modernizing internal controls and ensuring the agency is current on financial management and accounting policies.

## Financial Highlights

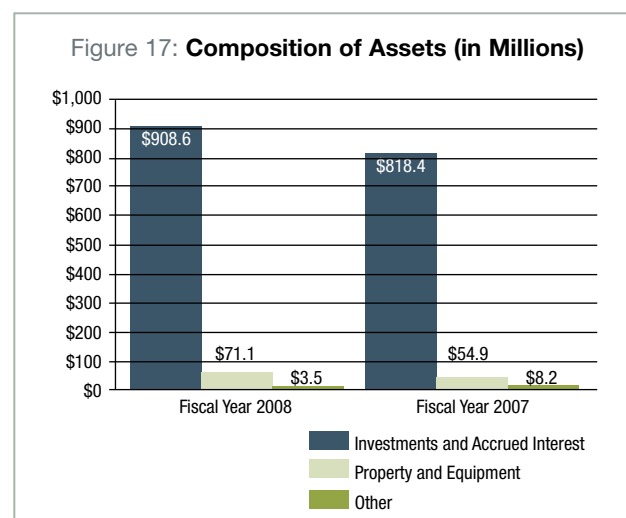
### Overview

The OCC received an unqualified opinion on our fiscal years 2008 and 2007 financial statements. The financial statements consist of Balance Sheets, Statements of Net Cost, Statements of Changes in Net Position, and Statements of Budgetary Resources. The OCC presents the financial statements and notes on a comparative basis, providing financial information for fiscal years 2008 and 2007. These financial statements were prepared from the OCC's accounting records in conformity with the generally accepted accounting principles for U.S. federal agencies (federal GAAP). The financial statements, notes, and auditor's opinion begin on page 54. A summary of the OCC's financial activities in fiscal years 2008 and 2007 follows.

## Assets

The OCC's assets include both "entity" and "non-entity" assets. The OCC uses entity assets, which belong to the agency, to fund operations. The OCC earns revenue through the collection of assessments from national banks and from other income, including interest on investments in U.S. Treasury securities. Non-entity assets are assets that the OCC holds on behalf of another federal agency or other third party. The OCC's non-entity assets are civil money penalties due the federal government through court-enforced legal actions. Once collected, the OCC transfers these amounts to the General Fund of the U.S. Treasury.

As of September 30, 2008, total assets were \$983.2 million, an increase of \$101.7 million or 11.5 percent from the level at September 30, 2007. This increase is primarily attributable to the changes in investments and accrued interest. The increase of \$90.2 million in investments and accrued interest resulted from a rise in assessment collections during fiscal year 2008. Figure 17 shows the composition of the OCC's assets.



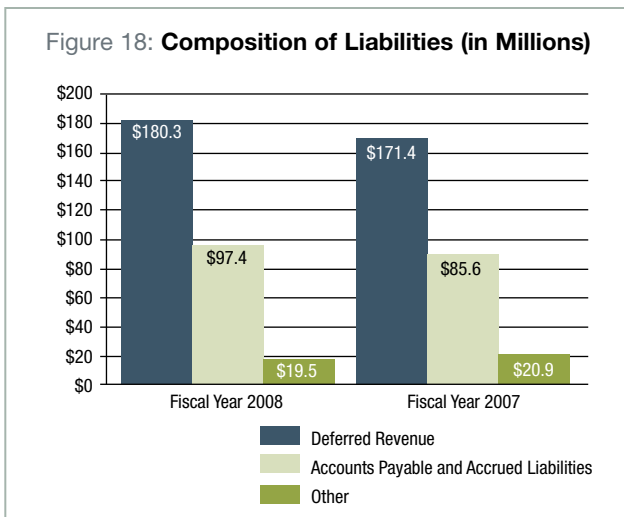
Source: OCC data for fiscal years 2008 and 2007.



## Liabilities

The OCC's liabilities represent the resources due to others or held for future recognition and are largely comprised of deferred revenue, accrued liabilities, and accounts payable. Deferred revenue represents the unearned portion of semiannual assessments that have been collected but not earned. The OCC records a custodial liability for the net amount of enforcement-related receivables. Upon collection, the OCC transfers these amounts to the General Fund of the U.S. Treasury.

As of September 30, 2008, total liabilities were \$297.2 million, an increase of a net of \$19.3 million, or 6.9 percent, over the level on September 30, 2007. The increase of \$8.9 million in deferred revenue was a result of a rise in assessment collections during fiscal year 2008. The increase of \$11.8 million in accounts payable and accrued liabilities was primarily caused by an increase in payroll and employee benefits over last year. Figure 18 illustrates the composition of the OCC's liabilities.

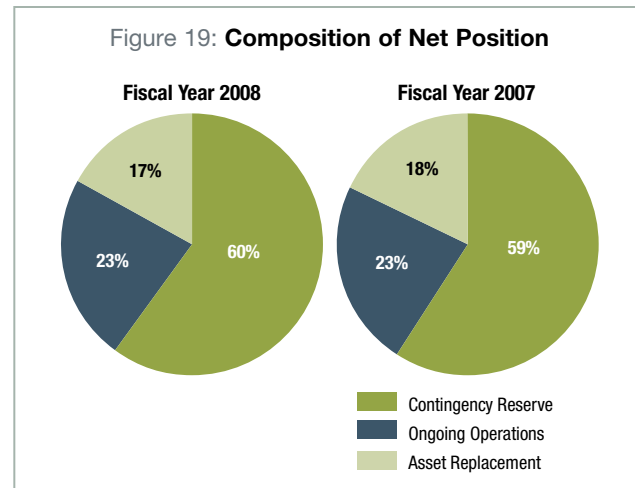


Source: OCC data for fiscal years 2008 and 2007.

## Net Position

The OCC's net position of \$686.1 million as of September 30, 2008, and \$603.6 million as of September 30, 2007, represent the cumulative net excess of the OCC's revenues over the cost of operations since inception. This represents an increase of \$82.5 million, or 13.7 percent. The majority of this increase directly relates to increases in assessment revenue over fiscal year 2007. The net position is presented on the Balance Sheets and the Statements of Changes in Net Position.

As discussed in the next section, the OCC reserves a significant portion of the net position to supplement resources made available to fund the OCC's annual budget and to cover foreseeable but rare events. The OCC also earmarks funds for ongoing operations to cover undelivered orders, the consumption of assets, and capital investments. Figure 19 shows the composition of the OCC's net position.



Source: OCC data for fiscal years 2008 and 2007.

## Reserves

The establishment of financial reserves is integral to the effective stewardship of the OCC's resources, particularly because the agency does not receive congressional appropriations. The contingency reserve, into which the OCC incorporated the funds from the special reserve during fiscal year 2008, serves to reduce the impact on the OCC's operations of revenue shortfalls resulting from foreseeable but rare events that are beyond the OCC's control, or new requirements and opportunities. Examples of such events include a major change in the national banking system or a fire, flood, or significant impairment to the OCC's information technology network that interferes with the OCC's ability to accomplish its mission. The asset replacement reserve is for the replacement of information technology equipment, leasehold improvements, and furniture replacement for future years. The OCC establishes the target level in the replacement reserve annually, based on the gross value of existing property and equipment, a growth rate factor, and other market cost adjustments.

## Revenues and Costs

The OCC does not receive appropriations. The OCC's operations are funded primarily by assessments collected from national banks and interest on investments in U.S. Treasury securities. The Comptroller, in accordance with 12 USC 482, establishes budget authority for a given fiscal year. The total budget authority available for use by the OCC in fiscal year 2008 was \$749.1 million, which represents an increase of \$77.9 million, or 11.6 percent, over the \$671.2 million budget in fiscal year 2007.

Total fiscal year 2008 revenue of \$736.1 million reflects a \$40.7 million, or 5.9 percent, increase over fiscal year 2007 revenues of \$695.4 million. The increase is primarily attributable to a rise in bank assessment revenue stemming from the overall increase in the assets of the national banking system and the growth of investment income from an expanded investment portfolio. Figure 20 depicts the components of total revenue for fiscal years 2008 and 2007.

Figure 20: **Components of Total Revenue (in Millions)**

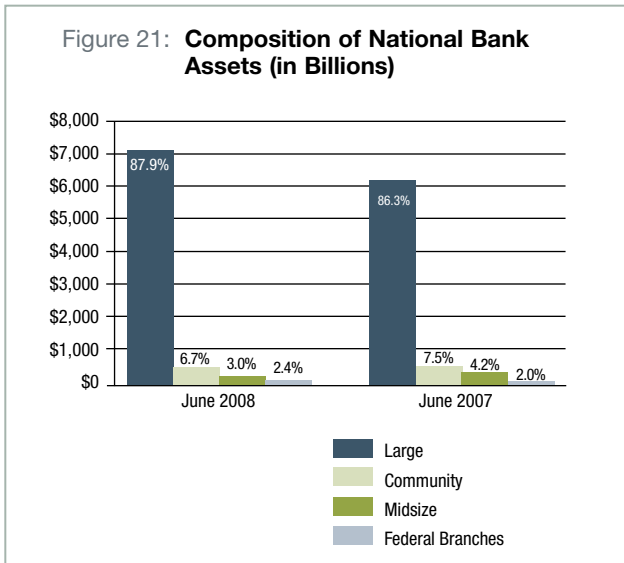
	Fiscal Year 2008	Fiscal Year 2007	Change
Assessments	\$ 707.5	\$ 666.0	\$ 41.5
Investment Income	26.1	26.6	(0.5)
Other <sup>1</sup>	2.5	2.8	(0.3)
Total Revenue	\$ 736.1	\$ 695.4	\$ 40.7

Source: OCC data for fiscal years 2008 and 2007.

<sup>1</sup> Other sources of revenue include bank licensing fees, revenue received from the sale of publications, and other miscellaneous sources.

## Bank Assets and Assessment Revenue

Total assets under OCC supervision increased during fiscal year 2008 to \$8.1 trillion from \$7.2 trillion in fiscal year 2007. For fiscal year 2008, 87.9 percent (\$7.1 trillion) is attributable to large national banks. Large banks' share of total OCC assessment revenue increased from 68.0 percent to 70.1 percent, followed by midsize and community banks decreasing to 26.7 percent, and federal branches up slightly to 3.2 percent. National bank asset growth combined with the movement of assets into the national banking system resulted in the higher total assets of national banks in fiscal year 2008. Figure 21 shows the composition of national bank assets by large banks, midsize banks, community banks, and federal branches for fiscal years 2008 and 2007.



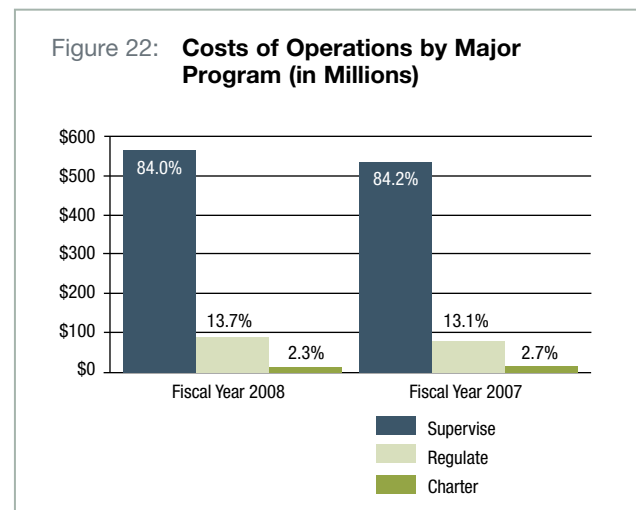
Source: OCC data as of June 30 for fiscal years 2008 and 2007.

## Investments

The book value of the OCC's portfolio on September 30, 2008, was \$904.7 million, compared with \$814.3 million a year earlier. The OCC invests available funds in non-marketable U.S. Treasury securities issued through the Department of the Treasury's Bureau of Public Debt in accordance with the provisions of 12 USC 481 and 12 USC 192. The increase in investments of \$90.4 million during the fiscal year reflects the investment of increased assessment revenue and the interest on investments held in the portfolio. The portfolio earned an annual yield for 2008 of 3.8 percent. The OCC calculates annual portfolio yield by dividing the total interest earned during the year by the average ending monthly book value of investments.

## Cost of Operations

The OCC's net cost of operations is reported on the Statements of Net Cost and the Statements of Changes in Net Position. The OCC uses an activity-based time reporting system to allocate costs among the agency's programs. Costs are further divided into those resulting from transactions between the OCC and other federal entities (intragovernmental) and those between the OCC and non-federal entities (with the public). The Statements of Net Cost present the full cost of operating the OCC's three major programs—supervise, regulate, and charter national banks—for the years ended September 30, 2008, and 2007. Figure 22 illustrates the breakdown of costs of operations for fiscal years 2008 and 2007.



Source: OCC data for fiscal years 2008 and 2007.

The full cost presented in the Statements of Net Cost includes contributions made by the Office of Personnel Management (OPM) on behalf of the OCC to cover the cost of the Federal Employees Retirement System and Civil Service Retirement System retirement plans, totaling \$25.8 million in fiscal year 2008 and \$26.4 million in fiscal year 2007. Fiscal year 2008 total program costs of \$679.5 million reflect an increase of \$42.9 million from \$636.6 million in fiscal year 2007. The increase was primarily because of pay and benefits resulting from a 2.6 percent increase to full time equivalents of 3,030.8 in fiscal year 2008 from 2,955.1 in fiscal year 2007, and additions to the benefit programs. Additional contributing factors include increases to contractual services supporting maintenance and non-capitalized information technology investments and imputed costs.

The full cost is reduced by earned revenues to arrive at net cost. Earned revenues increased by \$40.7 million because of an increase in fiscal year 2008 bank assessments that was slightly offset by minor decreases in other revenues. The increases in assessments are a direct result of bank asset growth in the national banking system, particularly the largest banks. The influx of assets into the national banking system has increased the OCC assessment revenue. Correspondingly, the costs of supervising the national banks have risen because of the increasing size and complexity of national bank assets.

### ***Budgetary Resources***

As previously discussed, the OCC receives the majority of our funding from assessment revenue earned and investment income. The Statements of Budgetary Resources, designed primarily for appropriated fund activities, present the budgetary resources available to the OCC for the year, the status of these resources at the end of the year, and the net outlay of budgetary resources at the end of the year. The OCC, which is a non-appropriated agency, executed \$672.8 million or 89.8 percent of the fiscal year 2008 budget of \$749.1 million, with the remaining funding being applied to the asset replacement and contingency reserves.

Office of the Comptroller of the Currency  
Balance Sheets

As of September 30, 2008 and 2007

	<u>Fiscal Year 2008</u>	<u>Fiscal Year 2007</u>
<b>Assets</b>		
<b>Intragovernmental:</b>		
Fund balance with Treasury	\$ 1,762,698	\$ 6,762,090
Investments and related interest (Note 2)	908,556,217	818,361,022
Advances and prepayments	64,815	82,904
<b>Total intragovernmental</b>	<b>910,383,730</b>	<b>825,206,016</b>
Cash	11,633	11,944
Accounts receivable, net	1,709,611	1,347,977
Property and equipment, net (Note 3)	71,089,891	54,882,947
Advances and prepayments	46,057	24,193
<b>Total assets</b>	<b>\$ 983,240,922</b>	<b>\$ 881,473,077</b>
<b>Liabilities</b>		
<b>Intragovernmental:</b>		
Accounts payable and other accrued liabilities	\$ 3,367,868	\$ 2,019,543
<b>Total intragovernmental</b>	<b>3,367,868</b>	<b>2,019,543</b>
Accounts payable	8,935,460	7,251,284
Accrued payroll and benefits	26,695,083	22,677,144
Accrued annual leave	32,681,026	29,996,291
Other accrued liabilities	25,763,750	23,671,832
Deferred revenue	180,283,755	171,380,008
Other actuarial liabilities (Note 5)	19,458,735	20,882,737
<b>Total liabilities</b>	<b>297,185,677</b>	<b>277,878,839</b>
<b>Net position (Note 6)</b>	<b>686,055,245</b>	<b>603,594,238</b>
<b>Total liabilities and net position</b>	<b>\$ 983,240,922</b>	<b>\$ 881,473,077</b>

The accompanying notes are an integral part of these financial statements.

**Office of the Comptroller of the Currency  
Statements of Net Cost**

*For the Years Ended September 30, 2008 and 2007*

	<b>Fiscal Year 2008</b>	<b>Fiscal Year 2007</b>
<b>Program Costs</b>		
<b>Supervise National Banks</b>		
Intragovernmental	\$ 80,246,924	\$ 74,331,808
With the Public	490,310,368	462,006,442
<b>Subtotal - Supervise National Banks</b>	<b>\$ 570,557,292</b>	<b>\$ 536,338,250</b>
<b>Regulate National Banks</b>		
Intragovernmental	\$ 13,092,698	\$ 11,790,685
With the Public	80,323,998	71,519,547
<b>Subtotal - Regulate National Banks</b>	<b>\$ 93,416,696</b>	<b>\$ 83,310,232</b>
<b>Charter National Banks</b>		
Intragovernmental	\$ 2,290,338	\$ 2,462,667
With the Public	13,189,237	14,513,285
<b>Subtotal - Charter National Banks</b>	<b>\$ 15,479,575</b>	<b>\$ 16,975,952</b>
<b>Total Program Costs</b>	<b>\$ 679,453,563</b>	<b>\$ 636,624,434</b>
Less: Earned Revenues Not Attributed to Programs	(736,142,091)	(695,443,263)
<b>Net Cost of Operations (Note 7)</b>	<b>\$ (56,688,528)</b>	<b>\$ (58,818,829)</b>

*The accompanying notes are an integral part of these financial statements.*

**Office of the Comptroller of the Currency  
Statements of Changes in Net Position**

*For the Years Ended September 30, 2008 and 2007*

	<b>Fiscal Year 2008</b>	<b>Fiscal Year 2007</b>
<b>Beginning Balances</b>	\$ 603,594,238	\$ 518,356,458
Other Financing Sources:		
Imputed financing (Note 8)	25,772,479	26,418,951
<b>Net Cost of Operations</b>	56,688,528	58,818,829
<b>Net Change</b>	82,461,007	85,237,780
<b>Ending Balances</b>	<b>\$ 686,055,245</b>	<b>\$ 603,594,238</b>

*The accompanying notes are an integral part of these financial statements.*

**Office of the Comptroller of the Currency  
Statements of Budgetary Resources**

*For the Years Ended September 30, 2008 and 2007*

	<b>Fiscal Year 2008</b>	<b>Fiscal Year 2007</b>
<b>Budgetary Resources</b>		
Unobligated balance, brought forward, October 1	\$ 667,660,982	\$ 597,772,320
Spending authority from offsetting collections		
Earned		
Collected	740,544,477	707,929,667
Receivable from Federal sources	(132,564)	392,256
Subtotal	740,411,913	708,321,923
<b>Total Budgetary Resources</b>	<b>\$ 1,408,072,895</b>	<b>\$ 1,306,094,243</b>
<b>Status of Budgetary Resources</b>		
Obligations incurred	\$ 673,715,700	\$ 638,433,261
Unobligated balance available	734,357,195	667,660,982
<b>Total Status of Budgetary Resources</b>	<b>\$ 1,408,072,895</b>	<b>\$ 1,306,094,243</b>
<b>Change in Obligated Balance</b>		
<b>Obligated balance, net, beginning of period</b>		
Unpaid obligations brought forward, October 1	\$ 151,721,328	\$ 117,900,706
Uncollected customer payments from		
Federal sources, October 1	( 4,036,718)	(3,644,462)
Total unpaid obligated balance, net	147,684,610	114,256,244
Obligations incurred	673,715,700	638,433,261
Gross outlays	(659,869,422)	(604,612,639)
Change in uncollected customer payments from		
Federal sources	132,565	(392,256)
Obligated balance, net, end of period		
Unpaid obligations	165,567,607	151,721,328
Uncollected customer payments from		
Federal sources	(3,904,154)	(4,036,718)
<b>Obligated balance, net, end of period</b>	161,663,453	147,684,610
Net outlays		
Gross outlays	\$ 659,869,422	\$ 604,612,639
Offsetting collections	(740,544,477)	(707,929,667)
<b>Net Outlays</b>	<b>\$ (80,675,055)</b>	<b>\$ 103,317,028)</b>

*The accompanying notes are an integral part of these financial statements.*



## *Notes to the Financial Statements*

### **Note 1—Significant Accounting Policies**

#### **A. Reporting Entity**

The OCC was created as a bureau within the U.S. Department of the Treasury by an act of Congress in 1863. The mission of the OCC was to establish and regulate a system of federally chartered national banks. The National Currency Act of 1863, rewritten and reenacted as the National Bank Act of 1864, authorized the OCC to supervise national banks and to regulate the lending and investment activities of federally chartered institutions.

The financial statements report on the OCC's three major programs: supervise, regulate, and charter national banks. These programs support the OCC's overall mission by ensuring the safety and soundness of the national banking system; fostering a flexible legal and regulatory framework that enables the national banking system to provide a full, competitive array of financial services; and promoting fair access to financial services and fair treatment of bank customers.

#### **B. Basis of Accounting and Presentation**

The accompanying financial statements present the operations of the OCC. The OCC's financial statements are prepared from the agency's accounting records in conformity with the generally accepted accounting principles for United States federal agencies (federal GAAP) and are presented in accordance with the form and content guidelines established by the Office of Management and Budget (OMB) in Circular A-136, "Financial Reporting Requirements."

The OCC's financial statements consist of Balance Sheets, Statements of Net Cost, Statements of Changes in Net Position, and Statements of Budgetary Resources. The OCC presents the financial statements on a comparative basis, providing information for fiscal years 2008 and 2007. In previous years, the OCC's financial statements also included the Statements of Custodial Activity. However, as the amounts for fiscal years 2008 and 2007 are immaterial, these statements have

been eliminated. Should amounts become material in the future, the Statements of Custodial Activity will be included in the OCC's financial statement presentation.

Per OMB's authority under the Statement of Federal Financial Accounting Standards (SFFAS) No. 7, "Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting," the Statement of Financing was eliminated as a basic statement effective in fiscal year 2007. The Statement of Financing data are presented in Note 9, Reconciliation of Net Cost of Operations to Budget.

The financial statements reflect both the accrual and budgetary bases of accounting. Under the accrual method, revenues are recognized when earned, and expenses are recognized when a liability is incurred, without regard to cash receipt or payment. The budgetary method recognizes the obligation of funds according to legal requirements, which in many cases is made prior to the occurrence of an accrual-based transaction. Budgetary accounting is essential for compliance with legal constraints and controls over the use of federal funds.

In accordance with federal GAAP, the preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Such estimates and assumptions could change in the future as more information becomes known, which could affect the amounts reported and disclosed herein.

Throughout these financial statements, intragovernmental assets, liabilities, earned revenues, and costs have been classified according to the entity responsible for these transactions. Intragovernmental earned revenues are collections or accruals of revenue from other federal entities, and intragovernmental costs are payments or accruals of expenditures to other federal entities.

### **C. Revenues and Other Financing Sources**

The OCC derives revenue primarily from assessments and fees paid by national banks and income on investments in U.S. Treasury securities. The OCC does not receive congressional appropriations to fund any of the agency's operations. Therefore, the OCC does not have any unexpended appropriations.

By federal statute 12 USC 481, the OCC's funds are maintained in a U.S. government trust revolving fund. The funds remain available to cover the annual costs of the OCC's operations in accordance with policies established by the Comptroller.

### **D. Earmarked Funds**

Earmarked funds are financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes, and must be accounted for separately from the government's general revenues. In accordance with Federal Accounting Standards Advisory Board SFFAS No. 27, "Identifying and Reporting Earmarked Funds," all of the OCC's revenue meets this criterion and constitutes an earmarked fund.

The federal government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. Treasury securities are an asset to the OCC and a liability to the U.S. Treasury. Because the OCC and the U.S. Treasury are both parts of the federal government, the corresponding assets and liabilities offset one another from the standpoint of the government as a whole. For this reason, they do not represent an asset or a liability in the U.S. government-wide financial statements.

Treasury securities provide the OCC with authority to draw upon the U.S. Treasury to make future payments or expenditures. When the OCC requires redemption of these securities to make expenditures, the government finances those expenditures from accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the government finances all other expenditures.

### **E. Fund Balance with Treasury**

The Department of the Treasury processes the OCC's cash receipts and disbursements. Sufficient funds are maintained in a U.S. government trust revolving fund and are available to pay current liabilities. The OCC invests available funds in non-marketable U.S. Treasury securities (Note 2). In accordance with SFFAS No. 1, "Accounting for Selected Assets and Liabilities," the OCC has the positive intent and ability to hold these securities until maturity.

The OCC's Statements of Budgetary Resources reflect the status of the Fund Balance with Treasury. It consists of the unobligated balance amount of \$734.4 million at September 30, 2008, and \$667.7 million at September 30, 2007, which is included in the OCC's net investment balance of \$894.2 million for fiscal year 2008 and \$808.6 million for fiscal year 2007, and the obligated balances not yet disbursed (e.g., undelivered orders) of \$161.7 million for fiscal year 2008 and \$147.7 million for fiscal year 2007. These balances reflect the budgetary authority remaining for disbursements against current or future obligations.

### **F. Accounts Receivable**

As presented in the OCC's Balance Sheets, accounts receivable represent monies owed, primarily due from the public, for services and goods provided that will be retained by the OCC upon collection. Also included are civil money penalty (CMP) amounts assessed against people or banks for violations of law, regulation, and orders; unsafe or unsound practices; and breaches of fiduciary duty. When collected, these CMP amounts are transferred to the Treasury General Fund. CMP collections totaled \$25.3 million at September 30, 2008, and \$12.7 million at September 30, 2007.

In accordance with SFFAS No. 1, "Accounting for Selected Assets and Liabilities," the OCC updates the allowance for loss on accounts receivable account annually or as needed to reflect the most current estimate of accounts that are likely to be uncollectible. Accounts receivable from the public are reduced by an allowance for loss on doubtful accounts.

The OCC's practice has been to reserve 50 percent of outstanding receivable balances between 180 and 365 days delinquent and 100 percent

for outstanding balances greater than 365 days delinquent. Since CMPs are not debts due the OCC, the amount outstanding does not enter into the calculation for the allowance. In addition, debts owed by other government entities and interest receivable on investments in U.S. Treasury securities are considered collectible, and therefore also do not enter into the calculation for the allowance. The balance in the OCC's allowance for loss on accounts receivable account was \$1,079 at September 30, 2008, and \$2,374 at September 30, 2007.

## **G. Advances and Prepayments**

Payments in advance for receipt of goods and services are recognized as advances or prepayments and are reported as assets on the Balance Sheets.

## **H. Property and Equipment**

Property, equipment, and internal use software (Note 3) are accounted for in accordance with SFFAS No. 6, "Accounting for Property, Plant, and Equipment," and SFFAS No. 10, "Accounting for Internal Use Software."

Property and equipment purchases and additions are stated at cost. The OCC expenses acquisitions that do not meet the capitalization criteria, such as normal repairs and maintenance, when they are received or incurred.

In addition, property and equipment are depreciated over their estimated useful lives using the straight-line method. They are removed from the OCC's asset accounts in the period of disposal, retirement, or removal from service. Any difference between the book value of the property and equipment and amounts realized is recognized as a gain or loss in the same period that the asset is removed.

## **I. Liabilities**

### *Accounts Payable*

Liabilities represent the amounts owed or accrued under contractual or other arrangements governing the transactions, including operating expenses incurred but not paid. Payments are made in a timely manner in accordance with the Prompt Payment Act. Interest penalties are paid when payments are late. Discounts are taken when cost-effective, and the invoice is paid within the discount period.

### *Accrued Annual Leave*

The OCC accounts for liabilities in accordance with SFFAS No. 5, "Accounting for Liabilities of the Federal Government." In accordance with SFFAS No. 5, annual leave is accrued and funded by the OCC as it is earned, and the accrual is reduced as leave is taken or paid. Each year, the balance in the accrued annual leave account is adjusted to reflect actual leave balances with current pay rates. Sick leave and other types of leave are expended as taken.

### *Deferred Revenue*

The OCC's activities are primarily financed by assessments on assets held by national banks and the federal branches of foreign banks. These assessments are due March 31 and September 30 of each year, based on asset balances as reflected on call reports dated December 31 and June 30, respectively. Assessments are paid in mid-cycle and are recognized as earned revenue on a straight-line basis over the six months following the call report date. The unearned portions of collected assessments are classified as deferred revenue.

### *Civil Money Penalties*

The custodial liability amount of \$1.7 million recognized represents the amount of accounts receivable that, when collected, will be deposited to the Treasury General Fund. Included in the custodial liability are amounts collected for fines, CMPs, and related interest assessments.

The SFFAS No. 12, "Recognition of Contingent Liabilities Arising from Litigation," defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss. The uncertainty will be resolved when one or more future events occur or fail to occur. The OCC recognizes contingencies as liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated. For fiscal years 2008 and 2007, the OCC neither identified nor recognized any such contingent liabilities.

## **J. Employment Benefits**

### *Retirement Plan*

OCC employees are eligible to participate in either the Civil Service Retirement System or the

Federal Employees Retirement System, depending on when they were hired by the federal government. Pursuant to the enactment of Public Law 99-335, which established the Federal Employees Retirement System, most employees hired after December 31, 1983, are automatically covered by Federal Employees Retirement System and Social Security. Employees hired prior to January 1, 1984, are covered by the Civil Service Retirement System, with the exception of those who, during the election period, joined the Federal Employees Retirement System.

#### ***Thrift Savings Plan***

OCC employees are eligible to participate in the federal Thrift Savings Plan. For those employees under the Federal Employees Retirement System, a Thrift Savings Plan account is automatically established, and the OCC contributes a mandatory 1.0 percent of base pay to this account. In addition, the OCC matches employee contributions up to an additional 4.0 percent of pay, for a maximum OCC contribution of 5.0 percent of base pay.

#### ***OCC 401(k) Plan***

In addition to the federal Thrift Savings Plan, employees can elect to contribute up to 10.0 percent of their base pay in the OCC 401(k) Plan administered by Prudential Financial Incorporated, subject to Internal Revenue Service regulations. Currently, the OCC contributes a fixed 2.0 percent of the base pay to the plan for all qualified employees, regardless of whether they contribute to the plan or not. In addition, the OCC will match an additional 1.0 percent employee contribution, for a maximum OCC contribution of 3.0 percent of base pay. In both fiscal years 2008 and 2007, the OCC funded a special lump sum contribution of \$1,000 to be deposited in the 401(k) accounts of all permanent employees. The OCC contracted with an independent public accounting firm to perform an audit of the plan and related financial statements for the year ended December 31, 2007. The financial statements for the plan received an unqualified opinion.

#### ***Federal Employees Health Benefits and Federal Employees Group Life Insurance***

Employees and retirees of the OCC are eligible to participate in Federal Employees Health Benefits

and Federal Employees Group Life Insurance plans that involve a cost sharing of bi-weekly coverage premiums by employee and employer. The Office of Personnel Management (OPM) administers both of these employee benefit plans.

#### **K. Effects of Recent Accounting Pronouncements**

The OCC's benefits program includes a Postretirement Life Insurance Plan, a defined benefit program not typically offered within the federal government and therefore not addressed by accounting standards issued by the Federal Accounting Standards Advisory Board. For this program, the OCC follows Financial Accounting Standards Board Statement of Financial Accounting Standard (SFAS) No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." As a result, the OCC implemented SFAS 158, "Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans" in fiscal year 2007. This standard requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multi-employer plan) as an asset or liability in the Statement of Financial Position and to recognize changes in that funded status in the year in which the changes occur. Implementation of this standard resulted in an increase to the OCC's liability of \$3.1 million in fiscal year 2007 for the funded portion, in accordance with the actuarial estimate.

In addition, no new accounting pronouncements issued during fiscal year 2008 affected the OCC.

#### ***Note 2—Investments and Related Interest***

The OCC invests available funds in non-marketable U.S. Treasury securities and has the positive intent and ability to hold all U.S. Treasury securities to maturity. It does not maintain any available-for-sale or trading securities. The OCC manages risk by diversifying the agency's portfolio across maturities within established parameters. Diversifying maturities of the individual securities is meant to help manage the inherent risk of interest rate fluctuations. As part of the agency's investment strategy, the OCC evaluates, at least annually, performance benchmarks with objectives and holdings comparable to those within the OCC's investment portfolio.

Investments are stated at amortized cost and the related accrued interest. Premiums and discounts are amortized over the term of the investment using the effective yield method. The fair market value of investment securities was \$922.2 million at September 30, 2008, and \$815.9 million at September 30, 2007. The total return on the OCC's portfolio, which includes income from interest and the change in the market value of the securities held

in the portfolio during the reporting period, was 7.0 percent and 6.2 percent, respectively. The overall portfolio earned an annual yield of 3.8 percent for fiscal year 2008 and 4.4 percent for fiscal year 2007.

The yield-to-maturity on the non-overnight portion of the OCC's investment portfolio ranged from 1.5 percent to 4.7 percent in fiscal year 2008, and from 2.9 percent to 4.9 percent in fiscal year 2007.

#### Investments and Related Interest

Intragovernmental Securities	Cost	Amortization Method	Amortized (Premium)/Discount	Investments, Net	Market Value Disclosure
<b>Fiscal Year 2008</b>					
Non-Marketable Market-Based	\$ 908,441,786	Effective Yield	\$ (3,724,908)	\$ 904,716,878	\$ 922,247,855
Accrued Interest	3,839,339		0	3,839,339	3,839,339
<b>Total Intragovernmental Investments</b>	<b>\$ 912,281,125</b>		<b>\$ (3,724,908)</b>	<b>\$908,556,217</b>	<b>\$ 926,087,194</b>

<b>Fiscal Year 2007</b>					
Non-Marketable Market-Based	\$ 815,967,809	Effective Yield	\$ (1,643,505)	\$ 814,324,304	\$ 815,902,463
Accrued Interest	4,036,718		0	4,036,718	4,036,718
<b>Total Intragovernmental Investments</b>	<b>\$ 820,004,527</b>		<b>\$ (1,643,505)</b>	<b>\$ 818,361,022</b>	<b>\$ 819,939,181</b>

### Note 3—Property and Equipment, Net

Property and equipment purchased at a cost greater than or equal to the noted thresholds below with useful lives of three years or more are capitalized at cost and depreciated or amortized, as applicable. Leasehold improvements are amortized on a straight-line basis over the lesser of the terms of the related leases or their estimated useful lives. All other property and equipment are depreciated

or amortized, as applicable, on a straight-line basis over their estimated useful lives.

For fiscal year 2008, per SFFAS No. 6, “Accounting for Property, Plant and Equipment,” the OCC reported \$4.9 million of fully depreciated assets removed from service and recognized a loss of \$54,057 on the disposal of other assets.

The following figure summarizes property and equipment balances as of September 30, 2008, and 2007.

#### Property and Equipment, Net

Class of Assets	Capitalization Threshold/ Useful Life		Cost	Accumulated Depreciation	Net Book Value
<b>Fiscal Year 2008</b>					
Leasehold Improvements	\$ 50,000	5-20	\$ 44,585,541	\$ (24,255,659)	\$ 20,329,882
Equipment	\$ 50,000	3-10	25,896,127	(17,731,089)	8,165,038
Internal Use Software	\$500,000	5	57,707,853	(36,410,965)	21,296,888
Internal Use Software-Dev	\$500,000	N/A	13,570,654	–	13,570,654
Leasehold Improvements-Dev	\$ 50,000	N/A	7,727,429	–	7,727,429
<b>Total</b>			<b>\$ 149,487,604</b>	<b>\$ (78,397,713)</b>	<b>\$ 71,089,891</b>
<b>Fiscal Year 2007</b>					
Leasehold Improvements	\$ 50,000	5-20	\$ 28,480,815	\$ (21,989,589)	\$ 6,491,226
Equipment	\$ 50,000	3-10	26,941,592	(18,213,271)	8,728,321
Internal Use Software	\$500,000	5	39,922,748	(27,290,315)	12,632,433
Internal Use Software-Dev	\$500,000	N/A	22,583,709	–	22,583,709
Leasehold Improvements-Dev	\$ 50,000	N/A	4,447,258	–	4,447,258
<b>Total</b>			<b>\$ 122,376,122</b>	<b>\$ (67,493,175)</b>	<b>\$ 54,882,947</b>

**Note 4—Leases**

The OCC leases office space for headquarters operations in Washington, D.C., and for district and field operations. The lease agreements expire at various dates. In fiscal year 2008, the OCC entered into five new lease occupancy agreements that ranged between 65 and 120 months in various locations throughout the continental United States

as current leases expired. These leases are treated as operating leases. All annual lease costs under the operating leases are included in the Statements of Net Cost.

Under existing commitments, the minimum yearly lease payments through fiscal year 2014 and thereafter are illustrated in the following figure:

**Future Lease Payments**

Fiscal Year 2008	
Year	Amount
2009	\$ 34,838,102
2010	33,701,893
2011	27,858,269
2012	15,579,300
2013	12,480,836
2014 and Beyond	52,613,662
<b>Total</b>	<b>\$177,072,062</b>

Fiscal Year 2007	
Year	Amount
2008	\$ 29,064,300
2009	28,735,823
2010	27,189,128
2011	21,338,482
2012	9,068,922
2013 and Beyond	18,780,610
<b>Total</b>	<b>\$134,177,265</b>

**Note 5—Other Actuarial Liabilities**

OCC’s other actuarial liabilities are reported on the Balance Sheets and include the components as shown in the following figure:

**Actuarial Liabilities Category**

Component	Fiscal Year 2008	Fiscal Year 2007
Federal Employee’s Compensation Act (FECA)	\$ 2,380,482	\$ 3,418,308
Postretirement Life Insurance Benefits	17,078,253	17,464,429
<b>Total Actuarial Liabilities</b>	<b>\$ 19,458,735</b>	<b>\$ 20,882,737</b>

## Federal Employee's Compensation Act

The FECA provides income and medical cost protection to cover federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease. Claims incurred for benefits for OCC employees covered under FECA are administered by the U.S. Department of Labor and later billed to the OCC. The fiscal year 2008 present value of these estimated outflows are calculated using a discount rate of 4.4 percent in the first year and 4.8 percent in subsequent years.

## Postretirement Life Insurance Benefits

The OCC sponsors a life insurance benefit plan for current and retired employees. This plan is a defined benefit plan. The following figure sets forth the plan's funded status reconciled with the actuarial liability.

The actuarial cost method used to determine costs for the retirement plans is the Projected Unit Credit method, a benefit valuation method, according to SFAS No. 87, "Employers Accounting for Pensions," used to determine the actuarial present value of the benefit obligation and the related

service cost. The weighted-average discount rate used in determining the accumulated postretirement benefit obligation was 6.5 percent. Gains or losses owing to changes in actuarial assumptions are amortized over the service life of the plan. Because the OCC's liability experience, including changes in assumptions, has been favorable, the accumulated SFAS 158 charge has dropped to \$1.3 million, resulting in a reduction of \$1.8 million to the funded status adjustment for fiscal year 2008. The actuarial assumptions and methods used in calculating actuarial amounts comply with the requirements for postretirement benefits other than pensions as set forth in SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," and for health benefit plans as set forth in the American Institute of Certified Public Accountants (AICPA) Statement of Position 92-6.

Net periodic postretirement benefit costs for life insurance provisions under the plan include the components as shown in the previous figure. The OCC has modified the layout of the data in the Figure from fiscal year 2007 to improve the presentation of the OCC's postretirement liabilities. The total benefit expenses are recognized as program costs in the Statements of Net Cost.

### Accrued Postretirement Benefit Liability and Net Periodic Postretirement Benefit Cost

Liability Component	Fiscal Year 2008	Fiscal Year 2007
Accumulated Postretirement Benefit Obligation, Beginning of Period	\$ 17,464,429	\$ 12,839,288
Net Periodic Benefit Cost	1,844,994	1,888,028
Expected Benefit Distribution	(402,964)	(406,190)
SFAS 158 Funded Status Adjustment	(1,828,206)	3,143,303
<b>Total Postretirement Benefit Liability</b>	<b>\$ 17,078,253</b>	<b>\$ 17,464,429</b>

Cost Component	Fiscal Year 2008	Fiscal Year 2007
Service Cost	\$ 607,651	\$ 598,961
Interest Cost	1,027,797	967,799
Amortization of Transition Obligation	172,837	172,837
Amortization of Unrecognized Loss	36,709	148,431
<b>Total Postretirement Benefit Cost</b>	<b>\$ 1,844,994</b>	<b>\$ 1,888,028</b>



**Note 6—Net Position**

Net Position represents the net result of operations since inception, and includes cumulative amounts related to investments in capitalized assets. The OCC sets aside a portion of the net position as contingency and asset replacement reserves for use at the Comptroller’s discretion. In addition, funds are set aside to cover the cost of ongoing operations.

The contingency reserve supports the OCC’s ability to accomplish the mission in the case of foreseeable but rare events. Foreseeable but rare events are beyond the control of the OCC, such as a major change in the national banking system or, for instance, a fire, flood, or significant impairment of the information technology systems. During

fiscal year 2008, the OCC incorporated into the contingency reserve the funds from the special reserve, which had originally been established to reduce the impact on the OCC’s operations of revenue shortfalls or new requirements and opportunities.

The asset replacement reserve funds the replacement of information technology equipment, leasehold improvements, and furniture replacements for future years. The target level for the replacement reserve is established annually based on the gross value of existing property and equipment plus a growth rate factor and a margin for market cost adjustments.

The figure below reflects changes for fiscal years 2008 and 2007:

**Net Position Availability**

Components	Fiscal Year 2008	Fiscal Year 2007
Contingency Reserve	\$ 409,061,610	\$ 355,256,659
Asset Replacement Reserve	116,800,000	111,200,000
Set Aside for Ongoing Operations:		
Undelivered Orders	52,742,606	50,972,975
Consumption of Assets	81,606,510	60,742,789
Capital Investments	25,844,519	25,421,815
<b>Net Position</b>	<b>\$ 686,055,245</b>	<b>\$ 603,594,238</b>

**Note 7—Net Cost of Operations**

The Net Cost of Operations represents OCC’s operating costs deducted from assessments and fees paid by national banks and investment interest income earned. The revenue earned from reimbursable services is shown as an offset against

the full cost of the program to arrive at net cost. The imputed financing sources for net cost of operations are reported on the Statements of Changes in Net Position and in Note 9, Reconciliation of Net Cost of Operations to Budget.

The figure below illustrates the OCC’s operating expenses categories for fiscal years 2008 and 2007:

**Operating Expenses**

Expense Category	Fiscal Year 2008	Fiscal Year 2007
Personnel Compensation and Benefits	\$ 452,936,124	\$ 423,596,167
Contractual Services	79,694,100	77,945,521
Travel and Transportation of Persons and Things	43,650,692	41,099,328
Rent, Communication, and Utilities	43,945,774	36,486,810
Imputed Costs	25,772,479	26,418,951
Depreciation	15,899,671	12,112,108
Other	17,554,723	18,965,549
<b>Total</b>	<b>\$ 679,453,563</b>	<b>\$ 636,624,434</b>

### **Note 8—Imputed Costs and Financing Sources**

In accordance with SFFAS No. 5, “Liabilities of the Federal Government,” federal agencies must recognize the portion of employees’ pension and other retirement benefits to be paid by the OPM trust funds. These amounts are recorded as imputed costs and imputed financing for other agencies. OPM provides federal agencies with cost factors for the computation of current year imputed costs. These cost factors are multiplied by the current year salary or number of employees, as applicable, to provide an estimate of the imputed financing that the OPM trust funds will provide for each agency.

The imputed costs categories for fiscal years 2008 and 2007 are listed in the following figure. These imputed costs are included on the Statements of Net Cost. The financing sources absorbed by OPM are reflected on the Statements of Changes in Net Position and in Note 9, Reconciliation of Net Cost of Operations to Budget.

### **Note 9—Reconciliation of Net Cost of Operations to Budget**

The reconciliation of Net Cost of Operations to Budget demonstrates the relationship between OCC’s proprietary (net cost of operations) and budgetary accounting (net obligations) information. For fiscal year 2008, the following reconciliation shows \$40.9 million in excess resources available to finance activities, a net decrease of \$2.6 million over September 30, 2007. This net decrease resulted from a \$32.1 million increase in resources available netted against the increase of \$35.3 million in resources used (obligations incurred) and the \$0.6 million decrease in imputed financing. The increase in net resources available is primarily because of increased assessments, while the increase in resources used results from various office space and information technology investments as well as salary and employee benefits.

#### **Imputed Costs Absorbed by OPM**

<b>Component</b>	<b>Fiscal Year 2008</b>	<b>Fiscal Year 2007</b>
Retirement	\$ 10,848,000	\$ 10,971,155
Federal Employees Health Benefits	14,892,660	15,417,724
Federal Employees Group Life Insurance	31,819	30,072
<b>Total Imputed Costs Covered by OPM</b>	<b>\$ 25,772,479</b>	<b>\$ 26,418,951</b>

## Reconciliation of Net Cost of Operations to Budget

	<b>Fiscal Year 2008</b>	<b>Fiscal Year 2007</b>
<b>Resources Used to Finance Activities:</b>		
Budgetary Resources Obligated		
Obligations incurred	\$ 673,715,700	\$ 638,433,261
Less: Spending authority from offsetting collections	(740,411,913)	(708,321,923)
Net obligations	(66,696,213)	(69,888,662)
Other Resources		
Imputed financing sources (Note 8)	25,772,479	26,418,951
<b>Total resources used to finance activities</b>	<b>(40,923,734)</b>	<b>(43,469,711)</b>
<b>Resources Used to Finance Items Not Part of the Net Cost of Operations</b>		
Change in budgetary resources obligated for goods, services, and benefits ordered but not yet provided	(3,835,648)	(16,455,629)
Resources that finance the acquisition of assets	(32,106,616)	(24,244,583)
Other resources or adjustments to net obligated resources that do not affect net cost of operations	91,867	(107,415)
<b>Total resources used to finance items not part of the net cost of operations</b>	<b>(35,850,397)</b>	<b>(40,807,627)</b>
<b>Total resources used to finance the net cost of operations</b>	<b>\$ (76,774,131)</b>	<b>\$ (84,277,338)</b>
<b>Components of the Net Cost of Operations that Will Not Require or Generate Resources in the Current Period:</b>		
Components Requiring or Generating Resources in Future Periods:		
Change in deferred revenue	8,903,747	11,958,547
Total components that will require or generate resources in future periods	8,903,747	11,958,547
Components Not Requiring or Generating Resources:		
Depreciation and amortization	15,845,615	12,112,109
Net (increase) decrease in bond premium	(4,717,816)	973,181
Other	54,057	414,672
Total components that will not require or generate resources	11,181,856	13,499,962
<b>Total components of net cost of operations that will not require or generate resources in the current period</b>	<b>20,085,603</b>	<b>25,458,509</b>
<b>Net Cost of Operations</b>	<b>\$ (56,688,528)</b>	<b>\$ (58,818,829)</b>

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## Independent Auditor's Report on Financial Statements

Inspector General, Department of the Treasury, and  
the Comptroller of the Currency:

We have audited the accompanying balance sheets of the Office of the Comptroller of the Currency (OCC) as of September 30, 2008 and 2007, and the related statements of net cost, changes in net position and budgetary resources for the years then ended. These financial statements are the responsibility of the management of OCC. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and applicable provisions of Office of Management and Budget Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the OCC as of September 30, 2008 and 2007, and its net costs, changes in net position, and budgetary resources for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The information in Section Four, pages 45 through 53 of OCC's fiscal year 2008 Annual Report is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information, and we express no opinion on it.

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# Independent Auditor's Report

**gka, P.C.**

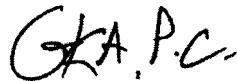
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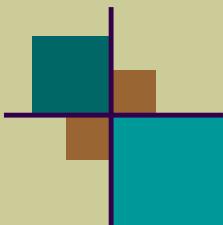
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Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The information included in Sections One, Two, and Three of OCC's fiscal year 2008 Annual Report is presented for purposes of additional analysis and is not a required part of the financial statements. We did not audit this information, and we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued reports dated October 31, 2008, on our consideration of the OCC's internal control over financial reporting, and on our tests of its compliance with certain provisions of applicable laws, regulations, and contracts. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be read in conjunction with this report in considering the results of our audits.



October 31, 2008

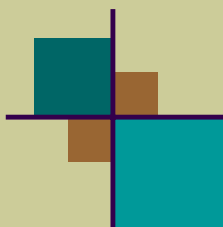


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### Independent Auditor's Report on Internal Control over Financial Reporting

Inspector General, Department of the Treasury, and  
the Comptroller of the Currency:

We have audited the balance sheet and the related statements of net cost, changes in net position, and budgetary resources, hereinafter referred to as "financial statements" of the Office of the Comptroller of the Currency (OCC) as of and for the year ended September 30, 2008, and have issued our report thereon dated October 31, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered the OCC's internal control over financial reporting by obtaining an understanding of the design effectiveness of OCC's internal control, determined whether these internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 07-04 and *Government Auditing Standards*. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*, such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide an opinion on internal control over financial reporting. Consequently, we do not provide an opinion on internal control over financial reporting.

Our consideration of the internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily disclose all deficiencies in internal control over financial reporting that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. Under standards issued by the American Institute of Certified Public Accountants, a control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course

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# Independent Auditor's Report

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of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the OCC's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles, such that there is more than a remote likelihood that a misstatement of the OCC's financial statements that is more than inconsequential will not be prevented or detected by the OCC's internal control.

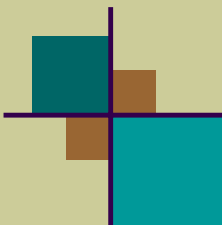
A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the OCC's internal control. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

We noted certain matters involving internal control and its operation that we reported to management of OCC in a separate letter dated October 31, 2008.

This report is intended solely for the information and use of the Management of the OCC, the Department of the Treasury Office of Inspector General, the Government Accountability Office, OMB, and the U.S. Congress, and is not intended to be, and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

*GKA, P.C.*

October 31, 2008



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## Independent Auditor's Report on Compliance with Laws and Regulations

The Inspector General, Department of the Treasury, and  
the Comptroller of the Currency:

We have audited the balance sheets and the related statements of net cost, changes in net position, and budgetary resources, hereinafter referred to as “financial statements” of the Office of the Comptroller of the Currency (OCC) as of and for the years ended September 30, 2008 and 2007, and have issued our report thereon dated October 31, 2008. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and, the applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*.

The management of the OCC is responsible for complying with laws and regulations applicable to the OCC. As part of obtaining reasonable assurance about whether the OCC's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 07-04, including certain requirements referred to in the *Federal Financial Management Improvement Act (FFMIA) of 1996*. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations and contracts applicable to the OCC. However, our objective was not to provide an opinion on overall compliance with laws, regulations and contracts. Accordingly, we do not express such an opinion.

The results of our tests of compliance with laws, regulations and contracts described in the preceding paragraph, exclusive of FFMIA, disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 07-04.

Under FFMIA, we are required to report whether the OCC's financial management systems substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA section 803(a) requirements.

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## Independent Auditor's Report

**gka, P.C.**

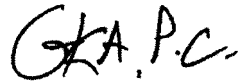
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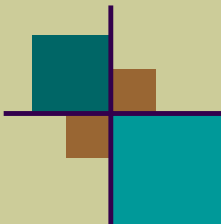
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The results of our tests disclosed no instances in which the OCC's financial management systems did not substantially comply with the three requirements discussed in the preceding paragraph.

This report is intended solely for the information and use of the Management of the OCC, the Department of the Treasury Office of Inspector General, the Government Accountability Office, OMB, and U.S. Congress and is not intended to be, and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.



October 31, 2008



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## Other Accompanying Information

### Performance Measures and Results

The OCC's fiscal year 2008 performance measures, workload indicators, customer service standards, and results are presented in Figure 23.

Figure 23: Performance Measures, Workload Indicators, Customer Service Standards, and Results

Strategic Goal	Performance Measure Workload Indicator Customer Service Standard	Fiscal Year 2005	Fiscal Year 2006	Fiscal Year 2007	Fiscal Year 2008	
					Target	Actual <sup>1</sup>
<b>I. A safe and sound national banking system</b>						
	Percentage of national banks with composite CAMELS rating of 1 or 2	94%	95%	96%	90%	<b>92%</b>
	Rehabilitated problem national banks as a percentage of the problem national banks one year ago (CAMELS 3, 4 or 5)	44%	46%	52%	40%	<b>47%</b>
	Percentage of national banks that are categorized as well capitalized	99%	99%	99%	95%	<b>99%</b>
	Percentage of critically undercapitalized banks on which responsible action is taken within 90 calendar days after they become critically undercapitalized	N/A <sup>2</sup>	N/A <sup>2</sup>	100%	100%	100%
	Average survey response that the report of examination clearly communicated examination findings, significant issues and the corrective actions management needed to take <sup>3</sup>	1.28	1.30	1.32	≤ 1.75	1.28
<b>II. Fair access to financial services and fair treatment of bank customers</b>						
	Percentage of national banks with consumer compliance rating of 1 or 2	94%	94%	97%	94%	<b>97%</b>
	Percentage of qualified intermediate small banks to which the OCC offers to provide consultation on the Community Reinvestment Act and community development opportunities	100%	100%	100%	100%	100%
	Percentage of consumer complaints closed within 60 calendar days of receipt <sup>4</sup>	N/A	36%	18%	80%	12%
	Number of consumer complaints opened/closed during the fiscal year <sup>4</sup>	N/A N/A	31,827 32,925	33,655 26,245	38,000 36,000	41,656 30,986
<b>III. A flexible legal and regulatory framework that enables the national banking system to provide a full, competitive array of financial services</b>						
	Percentage of external legal opinions issued within established time frames	86%	89%	96%	86%	92%
	Number of external legal opinions issued during the fiscal year <sup>5</sup>	119	70	81	120	73
	Percentage of licensing applications and notices filed electronically during the fiscal year	38%	36%	38%	40%	46%
	Number of licensing applications and notices filed electronically during the fiscal year	1,256	1,367	1,261	1,520	1,525
	Percentage of licensing applications and notices completed within established time frames	96%	94%	96%	95%	95%
	Number of licensing applications and notices completed during the fiscal year <sup>6</sup>	2,128	2,425	2,278	2,000	1,843
	Average survey rating of the overall licensing services provided by OCC <sup>7</sup>	1.19	1.20	1.20	≤ 1.50	1.22

Strategic Goal	Performance Measure Workload Indicator Customer Service Standard	Fiscal Year 2005	Fiscal Year 2006	Fiscal Year 2007	Fiscal Year 2008	
					Target	Actual <sup>1</sup>
IV. An expert, highly motivated, and diverse workforce that makes effective use of OCC resources						
	Total OCC costs relative to every \$100,000 in bank assets regulated	N/A	\$ 8.57	\$ 8.89	\$ 9.55	<b>\$ 8.39</b>

Source: OCC data for fiscal years 2008 and 2007.

<sup>1</sup> Fiscal year 2008 performance numbers shown in bold italics are estimates. Some performance data is obtained from quarterly call reports from banks. The September 30, 2008, call reports are not due until 30 or 45 days after the end of the period. Additionally, examinations concluded late in the fiscal year are not finalized for another 30 to 60 days. As a result, complete fiscal year data is not yet available; therefore, estimates have been reported.

<sup>2</sup> There were no critically undercapitalized national banks in fiscal years 2005 and 2006.

<sup>3</sup> The examination survey is based on a five-point scale, in which 1 indicates complete agreement and 5 indicates complete disagreement.

<sup>4</sup> In fiscal year 2006, the OCC revised reporting on the consumer complaints measure and related workload indicators to exclude inquiries and appeals at the recommendation of the Government Accountability Office. As such, prior year reporting is no longer presented because the data is not comparable and fiscal year 2006 is shown as the baseline year.

<sup>5</sup> For fiscal year 2008, the number of external legal opinions issued is below target because legal opinions are initiated externally by banks requesting interpretations from the OCC, and the OCC can only base projections on past history and anticipated activity.

<sup>6</sup> The number of total licensing filings has declined from the previous fiscal year because the number is based on actual applications received that also declined. However, the number of applications filed electronically increased for the fiscal year.

<sup>7</sup> The licensing survey is based on a five-point scale, in which 1 indicates outstanding and 5 indicates significantly deficient.

### ***Improper Payments Information Act***

The Improper Payments Information Act of 2002, as implemented by the OMB, requires federal agencies to review all program and activities annually and identify those that may be susceptible to significant erroneous payments. The OCC analyzed payments (excluding payroll) made during fiscal year 2008 and identified 38 erroneous payments requiring adjustments totaling \$31,895. Erroneous payments are identified and monitored daily to ensure prompt recovery. The underlying causes and contributing factors are identified quickly, and control measures are implemented to prevent additional erroneous payments. The OCC corrected and recovered all erroneous payments made during the year. Figure 24 summarizes the OCC's erroneous payments for fiscal years 2008 and 2007.

Figure 24: **Erroneous Payments**

	Fiscal Year 2008	Fiscal Year 2007
Number of payments	38	78
Dollar value of adjustments	\$ 31,895	\$ 272,570

Source: OCC data for fiscal years 2008 and 2007.

### ***Methodology for Identifying Improper Payments***

The OCC conducts both pre-payment reviews and post-payment audits to identify improper or erroneous payments. The OCC conducts a 100 percent pre-payment review of all supplier invoices and payment files prior to transmission to Treasury. As part of its sensitive payments program, the OCC conducts a 100 percent pre-payment review of executive and international travel vouchers and relocation payments, thereby helping to prevent erroneous payments. The OCC uses a sampling approach to audit travel vouchers and data-mining techniques to detect potential erroneous payments for post-payment audit activities. Immediately upon their identification, the OCC initiates collection activity to ensure recovery of funds. Also, the OCC is conducting a business process improvement review of the non-payroll process to bring about efficiencies and to determine the need for additional controls.

Based on the analyses, the OCC has concluded that erroneous payments do not exceed the Treasury threshold, which is both 2.5 percent of non-payroll payments and \$10 million. The OCC is compliant with the Erroneous Payments and Recovery Act of 2001 and the Improper Payments Information Act of 2002.

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## Assurance Statement

The Office of the Comptroller of the Currency (OCC) has made a conscientious effort during fiscal year (FY) 2008 to meet the internal control requirements of the Federal Managers' Financial Integrity Act (FMFIA), the Federal Financial Management Improvement Act (FFMIA), and Office of Management and Budget (OMB) Circular A-123.

OCC systems of management control are designed to ensure that:

- a) Programs achieve their intended results;
- b) Resources are used in accordance with the agency's mission;
- c) Programs and resources are protected from waste, fraud, and mismanagement;
- d) Laws and regulations are followed;
- e) Controls are sufficient to minimize improper or erroneous payments;
- f) Performance information is reliable;
- g) Systems security is in substantial compliance with relevant requirements;
- h) Continuity of operations planning in critical areas is sufficient to reduce risk to reasonable levels; and
- i) Financial management systems are in compliance with federal financial systems standards, i.e., FMFIA Section 4 and FFMIA.

I am providing reasonable assurance that the above-listed management control objectives were achieved by the OCC without material weakness during FY 2008. Specifically, this assurance is provided relative to Sections 2 and 4 of the Federal Managers' Financial Integrity Act (FMFIA).

I am also reporting substantial compliance with the requirements imposed by the Federal Financial Management Improvement Act (FFMIA).

The OCC also conducted its assessment of the effectiveness of internal control over financial reporting, which includes the safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of OMB Circular A-123. Based on the results of this evaluation, the OCC can provide reasonable assurance that its internal control over financial reporting as of June 30, 2008, was operating effectively, and no material weaknesses were found in the design or operation of the internal control over financial reporting.

### ***Other Control Deficiency***

The OCC presented results of performance measures, workload indicators, and customer service standards in the *FY 2007 Annual Report*. We reported that only 18 percent of the targeted 80 percent of FY 2007 consumer complaints were closed within 60 calendar days of receipt. Our management team conducted a process improvement project during FY 2008, and changes are being initiated. The OCC Customer Assistance Group expects substantial improvement during FY 2009 as a result of these process improvement initiatives.

### ***Analytical Basis of Assurance Statement***

OCC evaluated its management controls in accordance with the FY 2008 Secretary's Assurance Statement Guidance of July 10, 2008, and also considered the following guidance:

- OMB Circular A-123, Management's Responsibility for Internal Control;
- OMB Circular A-127, Financial Management Systems;

- OMB Circular A-130, Management of Federal Information Resources; and
  - Treasury Directive 40-04, Treasury Internal (Management) Control Program.
- Information considered in our control assessment included the following:
- FMFIA and FFMIA certifications submitted by each Executive Committee member;
  - OCC's Strategic Risk Management Plan;
  - Results of internal control testing under OMB Circular A-123, Appendix A;
  - Executive Committee descriptions of business unit quality management programs;
  - Results of internal reviews, including quality management program testing by the Enterprise Governance unit;
  - Results of control self-assessments completed by OCC managers in FY 2008;
  - Audit reports and evaluations issued by the Government Accountability Office and the Office of the Inspector General;
  - Completion of risk assessment materials related to the Improper Payments Information Act by our Deputy Chief Financial Officer, which was submitted to the Department in May 2008;
  - Completion of GAO's Core Financial System Requirements Checklist;
  - Unqualified and timely audit opinion on FY 2007 financial statements; and
  - GKA, P.C.'s status report of October 17, 2008, on the FY 2008 financial statement audit.



John C. Dugan  
Comptroller of the Currency  
November 3, 2008

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## List of Acronymns

**ACH:** Automated clearinghouse

**AICPA:** American Institute of Certified Public Accountants

**BIT:** Bank Information Technology

**BSA/AML:** Bank Secrecy Act/Anti-Money Laundering

**CAG:** Customer Assistance Group

**CDO:** Collateralized Debt Obligations

**CPA:** Certified Public Accountant

**CDFI:** Community development financial institution

**CFR:** Code of Federal Regulations

**CMP:** Civil money penalty

**CRA:** Community Reinvestment Act

**CRE:** Commercial Real Estate

**FASAB:** Federal Accounting Standards Advisory Board

**FDIC:** Federal Deposit Insurance Corporation

**FECA:** Federal Employees Compensation Act

**FFMIA:** Federal Financial Management Improvement Act

**FinCEN:** Financial Crimes Enforcement Network

**FISMA:** Federal Information Security Management Act

**FM:** Financial Management Department

**FMFIA:** Federal Managers' Financial Integrity Act

**GAAP:** Generally Accepted Accounting Principles

**GAO:** Government Accountability Office

**HSPD:** Homeland Security Presidential Directive

**IT:** Information Security

**ITS:** Information Technology Services

**OCC:** Office of the Comptroller of the Currency

**OMB:** Office of Management and Budget

**UNICEF:** United Nations Children's Fund

**OPM:** Office of Personnel Management

**OTS:** Office of Thrift Supervision

**SFAS:** Statement of Financial Accounting Standards

**SIV:** Structured Investment Vehicle

**SFFAS:** Statement of Federal Financial Accounting Standards

**USC:** United States Code

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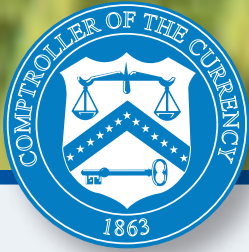
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# OCC History *and* Traditions

In February 1863, President Lincoln signed into law the National Currency Act, which created a national banking system under the supervision of a new bureau in the U.S. Department of the Treasury, headed by the Comptroller of the Currency.

The law was designed to supply the country's longstanding need for a uniform national currency and a nationwide system of banks operating under uniform rules, uniform supervision and regulation, and uniformly high standards. The law aimed to address the instability that had long beset banking in the United States.

Until 1863, as many as 20,000 different bank note varieties were in circulation at any given time—some good as gold, some worth little more than the paper they were printed on. This diverse and irregular paper fueled inflation and uncertainty and, in some cases, was a barrier to trade and economic growth. Banks themselves banded together in some parts of the country to promote monetary order and provide some assurance to depositors that, if one bank failed, others in the group would stand by it. Regulation, conducted by state banking departments, was uneven.

Under the National Currency Act and the follow-on National Bank Act of 1864, bank organizers were required to raise substantial capital. Previously, many banks had little or no real capital. The banks were required to invest a portion of that capital in U.S. government bonds, stimulating their sale at a time when the Treasury faced severe financial need. The bonds would be deposited with the Comptroller, who would deliver a proportionate quantity of bank notes of uniform design imprinted with a bank's name. The bonds served as security for the notes; if a national bank was unable to meet its obligations, the bonds were liquidated and the note holders repaid. This ingenious arrangement served the country for many years until national currency

was phased out in favor of a more elastic system of Federal Reserve notes.

The first Comptroller was Hugh McCulloch, a respected Indiana banker. McCulloch staffed the office, developed policies and procedures, promulgated standards of professional conduct for bankers and bank examiners, and worked to refine the legal framework under which national banks still operate today.

Charter number one was issued to the First National Bank of Philadelphia. The First National Bank of Davenport, the 15th charter, was first to open for business, on June 29, 1863. By 1870, more than 1,600 institutions, including hundreds of former state banks, had joined the national system, holding well over 50 percent of the country's total bank assets.

The National Bank Act offered a broad and potent grant of enumerated powers and such "incidental powers as shall be necessary to carry on the business of banking." The law required the Comptroller to report directly to Congress on needed improvements in the law. Modifications undertaken over the years have provided national banks with the flexibility to meet changing conditions in the financial marketplace.

From the beginning, professionalism and independence have been the OCC's hallmarks. The Comptroller, appointed by the President with the consent of the Senate, serves a five-year term of office. The OCC receives no appropriated funds; its revenues are derived from assessments paid by national banks.

During its 145-year history, the OCC has supervised the national banking system through many turns of the economic cycle. Its goal is to promote sound banking practices in good times and bad, ensuring that the interests of depositors, investors, communities, and taxpayers are appropriately safeguarded.

The seal depicted on the front cover dates to 1863. It was designed under the direction of the first Comptroller of the Currency, Hugh McCulloch, chosen by President Abraham Lincoln and Secretary of the Treasury Salmon P. Chase. The OCC marked its 145<sup>th</sup> anniversary in 2008.