network investment, including loop plant, switching costs, and other investments (e.g., interoffice network); (2) modeling operating and support expenses, including plant specific operating expenses, non-plant specific expenses, and treatment of joint and common costs; (3) modeling capital expenses, including rate of return on capital and debt, depreciation, and taxes; and (4) validation of the models.

The round table participants will include a broad representation of the telecommunications industry. Individuals interested in participating in one of the workshop round tables should submit their request in writing. Each request should include name, organization, address, telephone number, fax number, and a brief description of the person's expertise in this area. Such requests should be sent by no later than December 20, 1996, to Astrid Carlson, Universal Service Branch, Accounting and Audits Division, Common Carrier Bureau, FCC, 2100 M Street, Room 8607, Washington, D.C. 20554.

Federal Communications Commission.

Kathleen B. Levitz,

Deputy Bureau Chief, Common Carrier Bureau.

[FR Doc. 96–32190 Filed 12–18–96; 8:45 am]

BILLING CODE 6712–01–P

[CC Docket No. 92–237; DA 96–2086]

North American Numbering Council; Meetings

AGENCY: Federal Communications Commission.

ACTION: Notice.

SUMMARY: On December 11, 1996, the Commission released a public notice announcing the third and fourth meetings of the North American Numbering Council and the Agenda for those meetings. The intended effect of this action is to make the public aware of the NANC's third and fourth meetings and its Agenda.

FOR FURTHER INFORMATION CONTACT: Linda Simms, Administrative Assistant of the NANC, or Donna Scott Martin, both at (202) 418–2330. The address for both is: Network Services Division, Common Carrier Bureau, Federal Communications Commission, 2000 M Street, NW., Suite 235, Washington, DC 20054. The fax number for both is: (202) 418–2345. The TTY number for both is: (202) 418–0484.

SUPPLEMENTARY INFORMATION: Released: December 11, 1996. The third and fourth meetings of the North American Numbering Council (NANC) will be held on Monday, January 13, 1997, at 9:30 a.m. EST at the ANA Hotel, 2401 M Street, NW., Washington, DC and on Tuesday, January 28, 1997, at 9:30 a.m. at the Federal Communications Commission, 1919 M Street, NW., Room 856, Washington, DC, respectively. For the January 13 meeting, Council members will be billed for meeting costs (room and microphones) subsequent to the meeting.

This meeting will be open to members of the general public. The FCC will attempt to accommodate as many people as possible. Admittance, however will be limited to the seating available. The public may submit written statements to the NANC, which must be received two business days before the meeting. In addition, oral statements at the meeting by parties or entities not represented on the NANC will be permitted to the extent time permits. Such statements will be limited to five minutes in length by any one party or entity, and requests to make an oral statement must be received two business days before the meeting. Requests to make an oral statement or provide written comments to the NANC should be sent to Linda Simms or Donna Scott Martin, At the address under **FOR FURTHER INFORMATION CONTACT**, stated above.

Agenda

The planned agenda for the January 13, 1997 meeting is as follows:

1. Report of steering group activities.
2. Discussion of timing, process and deadline for selecting new North American Numbering Plan (NANP) Administrator, including specific duties of NANC, contract holder, CO code administration and cost recovery issues.
3. Reports from working groups, including discussion of non-consensus items, if any.
4. NANC Meeting Schedule.
5. Other Business.

The planned agenda for the January 28, 1997 meeting is as follows:

1. Dispute resolution. Status of proposal from Working Group.
2. Status of NANP Administrator Request for Proposal.
3. Working Group reports, including non-consensus items, if any.
4. Future of NANC.
5. Other Business.

Federal Communications Commission.

Geraldine A. Matise,

Chief, Network Services Division, Common Carrier Bureau.

[FR Doc. 96–32075 Filed 12–18–96; 8:45 am]

BILLING CODE 6712–01–M

FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

Uniform Financial Institutions Rating System

AGENCY: Federal Financial Institutions Examination Council.

ACTION: Notice.

SUMMARY: The Federal Financial Institutions Examination Council (FFIEC) is revising the Uniform Financial Institutions Rating System (UFIRS), which is commonly referred to as the CAMEL rating system. The term ''financial institutions'' refers to those insured depository institutions whose primary Federal supervisory agency is represented on the FFIEC. The agencies comprising the FFIEC are the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS). The revisions update the rating system to address changes in the financial services industry and in supervisory policies and procedures occurring since the rating system was adopted in 1979. The changes include: reformatting and clarification of component rating descriptions and component rating definitions; adding a sixth component addressing sensitivity to market risk; increasing emphasis on the quality of risk management practices in each of the rating components, particularly in the Management component; revising the composite rating definitions; and explicitly identifying the risks considered in assigning component ratings.

DATES: December 19, 1996.

FOR FURTHER INFORMATION CONTACT:

OCC: Lawrence W. (Bill) Morris, National Bank Examiner, Office of the Chief National Bank Examiner, (202) 874–5350, Office of the Comptroller of the Currency, 250 E Street SW, Washington, D.C. 20219.

FRB: Kevin Bertsch, Supervisory Financial Analyst, (202) 452–5265, or Constance Powell, Supervisory Financial Analyst, (202) 452–3506, Division of Banking Supervision and Regulation, Board of Governors of the Federal Reserve System, 20th and C Streets NW, Washington, D.C. 20551. For the hearing impaired only, Telecommunication Device for the Deaf (TDD), Dorothea Thompson, (202) 452–3544.

FDIC: Daniel M. Gautsch, Examination Specialist, (202) 898–6912, Office of Policy, Division of Supervision. For legal issues, Linda L. Stamp, Counsel, (202) 898–7310, Supervision and Legislation Branch, Federal Deposit Insurance Corporation, 550 17th Street NW, Washington, D.C. 20429.

OTS: William J. Magrini, Senior Project Manager, (202) 906–5744, Supervision Policy, Office of Thrift Supervision, 1700 G Street NW, Washington, D.C. 20552.

SUPPLEMENTARY INFORMATION:

Background Information

On July 18, 1996, the FFIEC published a notice and request for comment in the Federal Register (July Notice), 60 FR 37472, requesting comment on proposed revisions to the UFIRS. The UFIRS is an internal rating system used by the Federal supervisory agencies and State supervisory agencies for evaluating the soundness of financial institutions on a uniform basis and for identifying those institutions requiring special supervisory attention or concern. The UFIRS takes into consideration a careful evaluation of managerial, operational, financial, and compliance performance factors common to all institutions. The UFIRS is used by the supervisory agencies to monitor aggregate trends in the overall soundness of financial institutions. The UFIRS also provides a means for the supervisory agencies to monitor, for various statistical and supervisory purposes, the types and severity of problems that institutions may be experiencing, and to determine the level of supervisory concern that is warranted.

Under the UFIRS, each financial institution is assigned a composite rating based on an evaluation and rating of essential components of an institution's financial condition and operations. Under the former UFIRS, the component factors addressed the adequacy of capital, the quality of assets, the capability of the board of directors and management, the quality and level of earnings, and the adequacy of liquidity. The composite and component ratings are assigned on a 1 to 5 numerical scale. A 1 indicates the strongest performance and management practices and the lowest degree of supervisory concern. A 5 indicates the weakest performance and management practices and the highest degree of supervisory concern.

The UFIRS is an effective tool for the supervisory agencies to determine the safety and soundness of financial institutions. A number of changes, however, have occurred in the financial services industry and in supervisory policies and procedures since the rating system was adopted in 1979. As a result, the FFIEC is making certain enhancements to the rating system but is retaining its basic framework. The enhancements include: reformatting and clarifying the component rating descriptions and component rating definitions; adding a new sixth component, Sensitivity to Market Risk; increasing emphasis on the quality of risk management processes in each of the component ratings, particularly in the Management component; adding language in the composite rating definitions to parallel the changes in the component rating descriptions; and identifying the types of risk associated with each component area.

The FFIEC notes that some Federal supervisory agencies' regulations reference the institution's UFIRS or CAMEL rating in determining an institution's status under those regulations. The Federal supervisory agencies may consider amending those regulations to incorporate changes made to the UFIRS system.

Comments Received and Changes Made

The FFIEC received 55 comments regarding the proposed revisions to UFIRS. Thirty-four of the comments were from banks and thrifts, ten from state banking departments, five from trade associations, two from FRB offices, two from consultants, and two from Federal bank examiners.

Commenters generally favored the changes to the rating system regarding structure and format, reference to risk management practices, identification of risk types, and revisions to the composite and component rating definitions. However, commenters were divided regarding the new component on sensitivity to market risk.

Examiners field tested the revised rating system during 185 bank and thrift examinations conducted between July and October, 1996. The examiners provided comments regarding the revised rating system. Examiner response generally was favorable for the revised rating system, including the new sixth component. Few significant problems or rating differences were encountered between the former and the updated UFIRS.

Many commenters and examiners recommended clarifying changes to various aspects of the revised rating system. The FFIEC carefully considered each comment and examiner response and is making certain changes. The following discussion describes the comments received and changes made to the UFIRS in response to the comments. The updated UFIRS is included at the end of this Notice.

July Notice Specific Questions

In addition to requesting general comments regarding the proposed rating system, the FFIEC invited comments on two specific questions:

(1) *Does the proposed, revised rating system capture the essential aspects of a financial institution's condition, compliance with laws and regulations, and overall operating soundness? If not, what additional or different components should be considered?*

The majority of responses to this question were positive and indicated no additional or different components should be considered. Some commenters noted concerns with or the need for clarification of the new sixth component. These concerns are addressed later in this Notice.

(2) *Does the proposed management component rating adequately represent an assessment of the quality of the board of directors' and management's oversight regarding an institution's operating performance, risk management practices, and internal controls? If not, what other factors should be considered when rating management?*

The majority of responses to this question were favorable. A number of commenters recommended that the Management component make a clearer distinction between the role of the board of directors and the role of senior management.

The FFIEC added language to the Management component that recognizes the different responsibilities of these two management groups.

Structure and Format of Component Descriptions

The July Notice enhanced and clarified component rating descriptions by reformatting each component into three distinct sections: (1) An introductory paragraph discussing the areas to be considered when rating each component; (2) a bullet-style listing of the evaluation factors to be considered when assigning component ratings; and (3) a brief, qualitative description of the five rating grades that can be assigned to a particular component.

Several commenters expressed concern that component descriptions and component rating definitions need clear distinction and differentiation between rating levels.

The FFIEC acknowledges the need for clear distinction and differentiation between component rating levels. The UFIRS now reflects changed or added language to clarify that the component rating assessments consider an institution's size, the nature and complexity of its business activities, and its risk profile. Sentence structure, coupled with other minor language changes, were made to enhance parallelism and to improve differentiation between component rating levels.

Some commenters expressed concern regarding the number of evaluation factors within each component, the subjectivity associated with the evaluation factors, the order in which evaluation factors were listed, the redundancy of evaluation factors between components, and the need for clarification of some of the evaluation factors.

The FFIEC made revisions to the UFIRS to better structure and identify the factors that examiners traditionally consider as part of their assessment of a component area. This allows examiners and bankers to have a better understanding of what is being assessed under each component. Since its inception, the UFIRS has always contained elements of subjectivity and examiner judgment when assigning a rating, particularly as it relates to qualitative assessments of policies, practices, processes, and systems. Subjectivity and judgment cannot be eliminated but, as in the past, it can be reasonably applied based on the examiner's experience and knowledge, and their familiarity with the unique characteristics of the institution being examined.

The list of evaluation factors under each component is not meant to be all inclusive and appropriate language is added to the UFIRS noting that the evaluation factors are not listed in any particular order of importance. This allows examiners the flexibility of assessing factors that are most pertinent to the institution's situation and risk profile.

The FFIEC also acknowledges that there is a certain degree of redundancy between the component evaluation factors. For example, certain factors, such as the ability of management to identify, measure, monitor, and control risk, apply to each of the components and are an integral part of each component's rating. In addition, the level of classified assets will also impact the Asset Quality component and the Capital and Earnings components. This analysis should not be considered as ''double counting,'' but rather as a balanced assessment of how an evaluation factor can impact several component areas.

The FFIEC, however, has removed the evaluation factor referring to compliance with laws and regulations from all but the Management component. In addition, minor language changes are made to some of the component evaluation factors for clarification purposes.

Sensitivity to Market Risk Component

The July Notice added a sixth rating component addressing sensitivity to market risk and the degree to which changes in interest rates, foreign exchange rates, commodity prices, or equity prices can adversely affect a financial institution's earnings or economic capital.

A number of commenters noted that the sensitivity to market risk already is considered under the existing components and questioned the need for the new component.

The FFIEC acknowledges that market risk is already considered under the UFIRS; however, adding a new component provides a more precise indication of an institution's ability to monitor and manage its market risk. Since the sensitivity to market risk is already considered when assigning UFIRS ratings, the addition of the new component should not result in a change to the composite ratings being assigned.

The principal benefit of this new component is that it gives a clearer indication of supervisory concerns related to market risk than can be gained from the former UFIRS. For example, a financial institution with weak earnings and poor liquidity also might have significant and poorly managed exposures to interest rate risk. Less than satisfactory component ratings for earnings or liquidity accorded an institution under the former UFIRS would not specifically note a problem with exposure to, or the management of, market risk. Under the updated UFIRS, however, it is now possible to determine whether an institution has less than satisfactory earnings, a deficiency in its level or management of liquidity, *and* a problem with its exposure to market risks.

Other commenters objected to the new component on the grounds that it will place too much weight on a risk that is insignificant to most institutions and may result in examiners requiring elaborate market risk management systems where relatively basic management practices would suffice.

The FFIEC acknowledges that, for most institutions, market risk primarily reflects exposures to changes in interest rates.

Currently, interest rate risk is not a significant problem for the industry. In light of the level of risk embodied in this component for most institutions, the Federal supervisory agencies do not anticipate examiners overemphasizing this component when assigning a composite rating.

For the institutions that choose to take on greater market risk through holdings of complicated investments or hedging instruments or as part of significant trading activities, the exposure to, and management of, market risk is more significant to their overall risk profile. Thus, it is possible more weight will be assigned to the new component in determining the composite rating under UFIRS for institutions engaging in these activities. This is consistent with the Federal supervisory agencies' views that, when assigning a composite rating, examiners should determine the weight placed on each component based upon the particular situation of the institution, not on an arithmetic average of the components.

Thus, supervisory expectations for the management of market risk remain unchanged; the quality of management systems must be commensurate with risk exposure. Accordingly, the new component does not imply a requirement to develop enhanced management systems where market risk already is being identified, measured, monitored, and controlled in a manner appropriate to the institution's market risk exposure.

Several commenters also raised concerns about a perceived emphasis on the absolute level of market risk in the rating descriptions for the sensitivity to market risk component.

The FFIEC agrees that the evaluation of market risk must take into account the capital and earnings of an institution and the quality of its risk management practices. Accordingly, the description of the new component and its rating definitions have been revised to reflect this view.

Risk Management

The revised rating system reflects an increased emphasis on risk management processes. The Federal supervisory agencies currently consider the quality of risk management practices when applying the UFIRS, particularly in the management component. Changes in the financial services industry, however, have broadened the range of financial products offered by institutions and accelerated the pace of transactions. These trends reinforce the importance of institutions having sound risk management systems. Accordingly, the revised rating system contains explicit language in each of the components emphasizing management's ability to identify, measure, monitor, and control risks.

Several commenters expressed concern that the revised rating system would add to an institution's regulatory burden; require additional policies, processes, and highly formalized management information systems; or prevent institutions from attaining the highest ratings if they did not have formalized risk management policies and systems.

The FFIEC recognizes that management practices, particularly as they relate to risk management, vary considerably among financial institutions depending on their size and sophistication, the nature and complexity of their business activities, and their risk profile. Each institution must properly manage its risks and have appropriate policies, processes, or practices in place that management follows and uses. Activities undertaken in a less complex institution engaging in less sophisticated risk-taking activities may only need basic management and control systems compared to the detailed and formalized systems and controls needed for the broader and more complex range of activities undertaken at a larger and more complex institution.

The FFIEC added appropriate language clarifying that the UFIRS does not add to the regulatory burden of institutions, but promotes and complements efficient examination processes. The FFIEC also added language clarifying that detailed or highly formalized management systems and controls are not required for less complex institutions engaging in less sophisticated risk taking activities to receive the higher composite and component ratings.

Composite Rating Definitions

The July Notice retained the basic context of the existing composite rating definitions. The composite ratings are based on a careful evaluation of an institution's managerial, operational, financial, and compliance performance. The revised composite rating definitions contain an explicit reference to the quality of overall risk management practices.

A number of commenters recommended that the composite rating definitions contain a clearer distinction between rating levels, include a better perspective on examiner flexibility in considering the evaluation factors, and clarify other language to ensure consistent and uniform application by supervisory agencies.

The FFIEC agrees and has made certain changes in the structure and language of the composite rating definitions to address the concerns raised about examiner flexibility when assigning ratings based on an institution's particular circumstances. The principal change includes language to note explicitly that examiners consider an institution's size, complexity, and risk profile when assessing risk management practices. Other changes include sentence structure and other language changes in each of the composite rating definitions for better parallelism and readability from one definition to another and to provide clearer distinction between rating levels.

Peer Data Comparisons

Some commenters noted the lack of references to peer comparisons in component descriptions and rating definitions in the UFIRS.

The FFIEC acknowledges that it does not include peer comparison data in the updated rating system. The principal reason is to avoid over reliance on statistical comparisons to justify the component rating being assigned. Examiners are encouraged to consider all relevant factors when assigning a component rating. The rating system is designed to reflect an assessment of the individual institution. Peer data are a part of the overall assessment process, however.

Component Rating Disclosure

Several commenters noted that component ratings should be disclosed to an institution's board of directors and senior management.

The FFIEC agrees that component ratings should be disclosed to an institution's board of directors and senior management and recommended that the FDIC, FRB, OCC, and OTS begin disclosing component ratings in reports of examination no later than January 1, 1997. The FDIC began disclosing component ratings in reports of examination in process after September 30, 1996. The other Federal supervisory agencies expect to begin such disclosures on or before January 1, 1997.

The FFIEC inserted into the Overview section of the UFIRS appropriate language noting that both composite and component ratings are disclosed to an institution's board of directors and senior management.

Specialty Area Examinations

Some commenters recommended that the specialty area examinations, i.e., Bank Information Systems, Fiduciary, Consumer Compliance, CRA, etc., be integrated into the rating system.

The FFIEC acknowledges that results of such specialty examinations currently are taken into consideration when assigning an institution's composite rating or component ratings, as appropriate. Generally, the impact of specialty area examination findings are reflected in the composite and Management component ratings. However, other factors, such as reimbursable violations under Regulation Z (12 CFR Part 226), if substantial, could impact an institution's capital or earnings performance.

The FFIEC added appropriate language to the revised UFIRS noting that Foreign Branch examination and specialty examination findings (Compliance, CRA, Government Security Dealers, Information Systems, Municipal Security Dealers, Transfer Agent, and Fiduciary) and the ratings assigned to those areas are taken into consideration, as appropriate, when assigning a composite rating and component ratings under UFIRS.

Implementation Date

The FFIEC recommends that the Federal supervisory agencies implement the updated UFIRS no later than January 1, 1997. This date provides the Federal supervisory agencies flexibility to implement the updated UFIRS in conjunction with procedures for disclosing both composite and component ratings, as appropriate, to institutions' boards of directors and senior management. This date also ensures that institutions with examinations commenced in 1997 will be assessed under the updated UFIRS.

Text of the Revised Uniform Financial Institutions Rating System

Uniform Financial Institutions [1] Rating System

Introduction

The Uniform Financial Institutions Rating System (UFIRS) was adopted by the Federal Financial Institutions Examination Council (FFIEC) on November 13, 1979. Over the years, the UFIRS has proven to be an effective internal supervisory tool for evaluating

[1] For purposes of this rating system, the term ''financial institution'' refers to those insured depository institutions whose primary Federal supervisory agency is represented on the Federal Financial Institutions Examination Council (FFIEC). The agencies comprising the FFIEC are the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision. The term ''financial institution'' includes Federally supervised commercial banks, savings and loan associations, mutual savings banks, and credit unions.

the soundness of financial institutions on a uniform basis and for identifying those institutions requiring special attention or concern. A number of changes, however, have occurred in the banking industry and in the Federal supervisory agencies' policies and procedures which have prompted a review and revision of the 1979 rating system. The revisions to UFIRS include the addition of a sixth component addressing sensitivity to market risks, the explicit reference to the quality of risk management processes in the management component, and the identification of risk elements within the composite and component rating descriptions.

The revisions to UFIRS are not intended to add to the regulatory burden of institutions or require additional policies or processes. The revisions are intended to promote and complement efficient examination processes. The revisions have been made to update the rating system, while retaining the basic framework of the original rating system.

The UFIRS takes into consideration certain financial, managerial, and compliance factors that are common to all institutions. Under this system, the supervisory agencies endeavor to ensure that all financial institutions are evaluated in a comprehensive and uniform manner, and that supervisory attention is appropriately focused on the financial institutions exhibiting financial and operational weaknesses or adverse trends.

The UFIRS also serves as a useful vehicle for identifying problem or deteriorating financial institutions, as well as for categorizing institutions with deficiencies in particular component areas. Further, the rating system assists Congress in following safety and soundness trends and in assessing the aggregate strength and soundness of the financial industry. As such, the UFIRS assists the agencies in fulfilling their collective mission of maintaining stability and public confidence in the nation's financial system.

Overview

Under the UFIRS, each financial institution is assigned a composite rating based on an evaluation and rating of six essential components of an institution's financial condition and operations. These component factors address the adequacy of capital, the quality of assets, the capability of management, the quality and level of earnings, the adequacy of liquidity, and the sensitivity to market risk. Evaluations of the components take into consideration the institution's size and sophistication, the nature and complexity of its activities, and its risk profile.

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

The composite rating generally bears a close relationship to the component ratings assigned. However, the composite rating is not derived by computing an arithmetic average of the component ratings. Each component rating is based on a qualitative analysis of the factors comprising that component and its interrelationship with the other components. When assigning a composite rating, some components may be given more weight than others depending on the situation at the institution. In general, assignment of a composite rating may incorporate any factor that bears significantly on the overall condition and soundness of the financial institution. Assigned composite and component ratings are disclosed to the institution's board of directors and senior management.

The ability of management to respond to changing circumstances and to address the risks that may arise from changing business conditions, or the initiation of new activities or products, is an important factor in evaluating a financial institution's overall risk profile and the level of supervisory attention warranted. For this reason, the management component is given special consideration when assigning a composite rating.

The ability of management to identify, measure, monitor, and control the risks of its operations is also taken into account when assigning each component rating. It is recognized, however, that appropriate management practices vary considerably among financial institutions, depending on their size, complexity, and risk profile. For less complex institutions engaged solely in traditional banking activities and whose directors and senior managers, in their respective roles, are actively involved in the oversight and management of day-to-day operations, relatively basic management systems and controls may be adequate. At more complex institutions, on the other hand, detailed and formal management systems and controls are needed to address their broader range of financial activities and to provide senior managers and directors, in their respective roles, with the information they need to monitor and direct day-to-day activities. All institutions are expected to properly manage their risks. For less complex institutions engaging in less sophisticated risk taking activities, detailed or highly formalized management systems and controls are not required to receive strong or satisfactory component or composite ratings.

Foreign Branch and specialty examination findings and the ratings assigned to those areas are taken into consideration, as appropriate, when assigning component and composite ratings under UFIRS. The specialty examination areas include: Compliance, Community Reinvestment, Government Security Dealers, Information Systems, Municipal Security Dealers, Transfer Agent, and Trust.

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

Composite Ratings

Composite ratings are based on a careful evaluation of an institution's managerial, operational, financial, and compliance performance. The six key components used to assess an institution's financial condition and operations are: capital adequacy, asset quality, management capability, earnings quantity and quality, the adequacy of liquidity, and sensitivity to market risk. The rating scale ranges from 1 to 5, with a rating of 1 indicating: the strongest performance and risk management practices relative to the institution's size, complexity, and risk profile; and the level of least supervisory concern. A 5 rating indicates: the most critically deficient level of performance; inadequate risk management practices relative to the institution's size, complexity, and risk profile; and the greatest supervisory concern. The composite ratings are defined as follows:

Composite 1

Financial institutions in this group are sound in every respect and generally have components rated 1 or 2. Any weaknesses are minor and can be handled in a routine manner by the board of directors and management. These financial institutions are the most capable of withstanding the vagaries of business conditions and are resistant to outside influences such as economic instability in their trade area. These financial institutions are in substantial compliance with laws and regulations. As a result, these financial institutions exhibit the strongest performance and risk management practices relative to the institution's size, complexity, and risk profile, and give no cause for supervisory concern.

Composite 2

Financial institutions in this group are fundamentally sound. For a financial institution to receive this rating, generally no component rating should be more severe than 3. Only moderate weaknesses are present and are well within the board of directors' and management's capabilities and willingness to correct. These financial institutions are stable and are capable of withstanding business fluctuations. These financial institutions are in substantial compliance with laws and regulations. Overall risk management practices are satisfactory relative to the institution's size, complexity, and risk profile. There are no material supervisory concerns and, as a result, the supervisory response is informal and limited.

Composite 3

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

Composite 4

Financial institutions in this group generally exhibit unsafe and unsound practices or conditions. There are serious financial or managerial deficiencies that result in unsatisfactory performance. The problems range from severe to critically deficient. The weaknesses and problems are not being satisfactorily addressed or resolved by the board of directors and management. Financial institutions in this group generally are not capable of withstanding business fluctuations. There may be significant noncompliance with laws and regulations. Risk management practices are generally unacceptable relative to the institution's size, complexity, and risk profile. Close supervisory attention is required, which means, in most cases, formal enforcement action is necessary to address the problems. Institutions in this group pose a risk to the deposit insurance fund. Failure is a distinct possibility if the problems and weaknesses are not satisfactorily addressed and resolved.

Composite 5

Financial institutions in this group exhibit extremely unsafe and unsound practices or conditions; exhibit a critically deficient performance; often contain inadequate risk management practices relative to the institution's size, complexity, and risk profile; and are of the greatest supervisory concern. The volume and severity of problems are beyond management's ability or willingness to control or correct. Immediate outside financial or other assistance is needed in order for the financial institution to be viable. Ongoing supervisory attention is necessary. Institutions in this group pose a significant risk to the deposit insurance fund and failure is highly probable.

Component Ratings

Each of the component rating descriptions is divided into three sections: an introductory paragraph; a list of the principal evaluation factors that relate to that component; and a brief description of each numerical rating for that component. Some of the evaluation factors are reiterated under one or more of the other components to reinforce the interrelationship between components. The listing of evaluation factors for each component rating is in no particular order of importance.

Capital Adequacy

A financial institution is expected to maintain capital commensurate with the nature and extent of risks to the institution and the ability of management to identify, measure, monitor, and control these risks. The effect of credit, market, and other risks on the institution's financial condition should be considered when evaluating the adequacy of capital. The types and quantity of risk inherent in an institution's activities will determine the extent to which it may be necessary to maintain capital at levels above required regulatory minimums to properly reflect the potentially adverse consequences that these risks may have on the institution's capital.

The capital adequacy of an institution is rated based upon, but not limited to, an assessment of the following evaluation factors:

- The level and quality of capital and the overall financial condition of the institution.
- The ability of management to address emerging needs for additional capital.
- The nature, trend, and volume of problem assets, and the adequacy of allowances for loan and lease losses and other valuation reserves.
- Balance sheet composition, including the nature and amount of intangible assets, market risk, concentration risk, and risks associated with nontraditional activities.
- Risk exposure represented by off-balance sheet activities.
- The quality and strength of earnings, and the reasonableness of dividends.
- Prospects and plans for growth, as well as past experience in managing growth.
- Access to capital markets and other sources of capital, including support provided by a parent holding company.

Ratings

1 A rating of 1 indicates a strong capital level relative to the institution's risk profile.

2 A rating of 2 indicates a satisfactory capital level relative to the financial institution's risk profile.

3 A rating of 3 indicates a less than satisfactory level of capital that does not fully support the institution's risk profile. The rating indicates a need for improvement, even if the institution's capital level exceeds minimum regulatory and statutory requirements.

4 A rating of 4 indicates a deficient level of capital. In light of the institution's risk profile, viability of the institution may be threatened. Assistance from shareholders or other external sources of financial support may be required.

5 A rating of 5 indicates a critically deficient level of capital such that the institution's viability is threatened. Immediate assistance from shareholders or other external sources of financial support is required.

Asset Quality

The asset quality rating reflects the quantity of existing and potential credit risk associated with the loan and investment portfolios, other real estate owned, and other assets, as well as off-balance sheet transactions. The ability of management to identify, measure, monitor, and control credit risk is also reflected here. The evaluation of asset quality should consider the adequacy of the allowance for loan and lease losses and weigh the exposure to counterparty, issuer, or borrower default under actual or implied contractual agreements. All other risks that may affect the value or marketability of an institution's assets, including, but not limited to, operating, market, reputation, strategic, or compliance risks, should also be considered.

The asset quality of a financial institution is rated based upon, but not limited to, an assessment of the following evaluation factors:

- The adequacy of underwriting standards, soundness of credit administration practices, and appropriateness of risk identification practices.
- The level, distribution, severity, and trend of problem, classified, nonaccrual, restructured, delinquent, and nonperforming assets for both on- and off-balance sheet transactions.
- The adequacy of the allowance for loan and lease losses and other asset valuation reserves.
- The credit risk arising from or reduced by off-balance sheet transactions, such as unfunded commitments, credit derivatives, commercial and standby letters of credit, and lines of credit.
- The diversification and quality of the loan and investment portfolios.
- The extent of securities underwriting activities and exposure to counterparties in trading activities.
- The existence of asset concentrations.
- The adequacy of loan and investment policies, procedures, and practices.
- The ability of management to properly administer its assets, including the timely identification and collection of problem assets.
- The adequacy of internal controls and management information systems.
- The volume and nature of credit documentation exceptions.

Ratings

1 A rating of 1 indicates strong asset quality and credit administration practices. Identified weaknesses are minor in nature and risk exposure is modest in relation to capital protection and management's abilities. Asset quality in such institutions is of minimal supervisory concern.

2 A rating of 2 indicates satisfactory asset quality and credit administration practices. The level and severity of classifications and other weaknesses warrant a limited level of supervisory attention. Risk exposure is commensurate with capital protection and management's abilities.

3 A rating of 3 is assigned when asset quality or credit administration practices are less than satisfactory. Trends may be stable or indicate deterioration in asset quality or an increase in risk exposure. The level and severity of classified assets, other weaknesses, and risks require an elevated level of supervisory concern. There is generally a need to improve credit administration and risk management practices.

4 A rating of 4 is assigned to financial institutions with deficient asset quality or credit administration practices. The levels of risk and problem assets are significant, inadequately controlled, and subject the financial institution to potential losses that, if left unchecked, may threaten its viability.

5 A rating of 5 represents critically deficient asset quality or credit administration practices that present an imminent threat to the institution's viability.

Management

The capability of the board of directors and management, in their respective roles, to identify, measure, monitor, and control the risks of an institution's activities and to ensure a financial institution's safe, sound, and efficient operation in compliance with applicable laws and regulations is reflected in this rating. Generally, directors need not be actively involved in day-to-day operations; however, they must provide clear guidance regarding acceptable risk exposure levels and ensure that appropriate policies, procedures, and practices have been established. Senior management is responsible for developing and implementing policies, procedures, and practices that translate the board's goals, objectives, and risk limits into prudent operating standards.

Depending on the nature and scope of an institution's activities, management practices may need to address some or all of the following risks: credit, market, operating or transaction, reputation, strategic, compliance, legal, liquidity, and other risks. Sound management practices are demonstrated by: active oversight by the board of directors and management; competent personnel; adequate policies, processes, and controls taking into consideration the size and sophistication of the institution; maintenance of an appropriate audit program and internal control environment; and effective risk monitoring and management information systems. This rating should reflect the board's and management's ability as it applies to all aspects of banking operations as well as other financial service activities in which the institution is involved.

The capability and performance of management and the board of directors is rated based upon, but not limited to, an assessment of the following evaluation factors:

- The level and quality of oversight and support of all institution activities by the board of directors and management.
- The ability of the board of directors and management, in their respective roles, to plan for, and respond to, risks that may arise from changing business conditions or the initiation of new activities or products.
- The adequacy of, and conformance with, appropriate internal policies and controls addressing the operations and risks of significant activities.
- The accuracy, timeliness, and effectiveness of management information and risk monitoring systems appropriate for the institution's size, complexity, and risk profile.
- The adequacy of audits and internal controls to: promote effective operations and reliable financial and regulatory reporting; safeguard assets; and ensure compliance with laws, regulations, and internal policies.
- Compliance with laws and regulations.
- Responsiveness to recommendations from auditors and supervisory authorities.
- Management depth and succession.
- The extent that the board of directors and management is affected by, or susceptible to, dominant influence or concentration of authority.
- Reasonableness of compensation policies and avoidance of self-dealing.
- Demonstrated willingness to serve the legitimate banking needs of the community.
- The overall performance of the institution and its risk profile.

Ratings

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

Management and the board have demonstrated the ability to promptly and successfully address existing and potential problems and risks.

2 A rating of 2 indicates satisfactory management and board performance and risk management practices relative to the institution's size, complexity, and risk profile. Minor weaknesses may exist, but are not material to the safety and soundness of the institution and are being addressed. In general, significant risks and problems are effectively identified, measured, monitored, and controlled.

3 A rating of 3 indicates management and board performance that need improvement or risk management practices that are less than satisfactory given the nature of the institution's activities. The capabilities of management or the board of directors may be insufficient for the type, size, or condition of the institution. Problems and significant risks may be inadequately identified, measured, monitored, or controlled.

4 A rating of 4 indicates deficient management and board performance or risk management practices that are inadequate considering the nature of an institution's activities. The level of problems and risk exposure is excessive. Problems and significant risks are inadequately identified, measured, monitored, or controlled and require immediate action by the board and management to preserve the soundness of the institution. Replacing or strengthening management or the board may be necessary.

5 A rating of 5 indicates critically deficient management and board performance or risk management practices. Management and the board of directors have not demonstrated the ability to correct problems and implement appropriate risk management practices. Problems and significant risks are inadequately identified, measured, monitored, or controlled and now threaten the continued viability of the institution. Replacing or strengthening management or the board of directors is necessary.

Earnings

This rating reflects not only the quantity and trend of earnings, but also factors that may affect the sustainability or quality of earnings. The quantity as well as the quality of earnings can be affected by excessive or inadequately managed credit risk that may result in loan losses and require additions to the allowance for loan and lease losses, or by high levels of market risk that may unduly expose an institution's earnings to volatility in interest rates. The quality of earnings may also be diminished by undue reliance on extraordinary gains, nonrecurring events, or favorable tax effects. Future earnings may be adversely affected by an inability to forecast or control funding and operating expenses, improperly executed or ill-advised business strategies, or poorly managed or uncontrolled exposure to other risks.

The rating of an institution's earnings is based upon, but not limited to, an assessment of the following evaluation factors:

• The level of earnings, including trends and stability.

• The ability to provide for adequate capital through retained earnings.

• The quality and sources of earnings.

• The level of expenses in relation to operations.

• The adequacy of the budgeting systems, forecasting processes, and management information systems in general.

• The adequacy of provisions to maintain the allowance for loan and lease losses and other valuation allowance accounts.

• The earnings exposure to market risk such as interest rate, foreign exchange, and price risks.

Ratings

1 A rating of 1 indicates earnings that are strong. Earnings are more than sufficient to support operations and maintain adequate capital and allowance levels after consideration is given to asset quality, growth, and other factors affecting the quality, quantity, and trend of earnings.

2 A rating of 2 indicates earnings that are satisfactory. Earnings are sufficient to support operations and maintain adequate capital and allowance levels after consideration is given to asset quality, growth, and other factors affecting the quality, quantity, and trend of earnings. Earnings that are relatively static, or even experiencing a slight decline, may receive a 2 rating provided the institution's level of earnings is adequate in view of the assessment factors listed above.

3 A rating of 3 indicates earnings that need to be improved. Earnings may not fully support operations and provide for the accretion of capital and allowance levels in relation to the institution's overall condition, growth, and other factors affecting the quality, quantity, and trend of earnings.

4 A rating of 4 indicates earnings that are deficient. Earnings are insufficient to support operations and maintain appropriate capital and allowance levels. Institutions so rated may be characterized by erratic fluctuations in net income or net interest margin, the development of significant negative trends, nominal or unsustainable earnings, intermittent losses, or a substantive drop in earnings from the previous years.

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

Liquidity

In evaluating the adequacy of a financial institution's liquidity position, consideration should be given to the current level and prospective sources of liquidity compared to funding needs, as well as to the adequacy of funds management practices relative to the institution's size, complexity, and risk profile. In general, funds management practices should ensure that an institution is able to maintain a level of liquidity sufficient to meet its financial obligations in a timely manner and to fulfill the legitimate banking needs of its community. Practices should reflect the ability of the institution to manage unplanned changes in funding sources, as well as react to changes in market conditions that affect the ability to quickly liquidate assets with minimal loss. In addition, funds management practices should ensure that liquidity is not maintained at a high cost, or through undue reliance on funding sources that may not be available in times of financial stress or adverse changes in market conditions.

Liquidity is rated based upon, but not limited to, an assessment of the following evaluation factors:

• The adequacy of liquidity sources compared to present and future needs and the ability of the institution to meet liquidity needs without adversely affecting its operations or condition.

• The availability of assets readily convertible to cash without undue loss.

• Access to money markets and other sources of funding.

• The level of diversification of funding sources, both on- and off-balance sheet.

• The degree of reliance on short-term, volatile sources of funds, including borrowings and brokered deposits, to fund longer term assets.

• The trend and stability of deposits.

• The ability to securitize and sell certain pools of assets.

• The capability of management to properly identify, measure, monitor, and control the institution's liquidity position, including the effectiveness of funds management strategies, liquidity policies, management information systems, and contingency funding plans.

Ratings

1 A rating of 1 indicates strong liquidity levels and well-developed funds management practices. The institution has reliable access to sufficient sources of funds on favorable terms to meet present and anticipated liquidity needs.
2 A rating of 2 indicates satisfactory liquidity levels and funds management practices. The institution has access to sufficient sources of funds on acceptable terms to meet present and anticipated liquidity needs. Modest weaknesses may be evident in funds management practices.
3 A rating of 3 indicates liquidity levels or funds management practices in need of improvement. Institutions rated 3 may lack ready access to funds on reasonable terms or may evidence significant weaknesses in funds management practices.
4 A rating of 4 indicates deficient liquidity levels or inadequate funds management practices. Institutions rated 4 may not have or be able to obtain a sufficient volume of funds on reasonable terms to meet liquidity needs.
5 A rating of 5 indicates liquidity levels or funds management practices so critically deficient that the continued viability of the institution is threatened. Institutions rated 5 require immediate external financial assistance to meet maturing obligations or other liquidity needs.

Sensitivity to Market Risk

The sensitivity to market risk component reflects the degree to which changes in interest rates, foreign exchange rates, commodity prices, or equity prices can adversely affect a financial institution's earnings or economic capital. When evaluating this component, consideration should be given to: management's ability to identify, measure, monitor, and control market risk; the institution's size; the nature and complexity of its activities; and the adequacy of its capital and earnings in relation to its level of market risk exposure.

For many institutions, the primary source of market risk arises from nontrading positions and their sensitivity to changes in interest rates. In some larger institutions, foreign operations can be a significant source of market risk. For some institutions, trading activities are a major source of market risk.

Market risk is rated based upon, but not limited to, an assessment of the following evaluation factors:

• The sensitivity of the financial institution's earnings or the economic value of its capital to adverse changes in interest rates, foreign exchanges rates, commodity prices, or equity prices.

• The ability of management to identify, measure, monitor, and control exposure to market risk given the institution's size, complexity, and risk profile.

• The nature and complexity of interest rate risk exposure arising from nontrading positions.

• Where appropriate, the nature and complexity of market risk exposure arising from trading and foreign operations.

Ratings

1 A rating of 1 indicates that market risk sensitivity is well controlled and that there is minimal potential that the earnings performance or capital position will be adversely affected. Risk management practices are strong for the size, sophistication, and market risk accepted by the institution. The level of earnings and capital provide substantial support for the degree of market risk taken by the institution.
2 A rating of 2 indicates that market risk sensitivity is adequately controlled and that there is only moderate potential that the earnings performance or capital position will be adversely affected. Risk management practices are satisfactory for the size, sophistication, and market risk accepted by the institution. The level of earnings and capital provide adequate support for the degree of market risk taken by the institution.
3 A rating of 3 indicates that control of market risk sensitivity needs improvement or that there is significant potential that the earnings performance or capital position will be adversely affected. Risk management practices need to be improved given the size, sophistication, and level of market risk accepted by the institution. The level of earnings and capital may not adequately support the degree of market risk taken by the institution.
4 A rating of 4 indicates that control of market risk sensitivity is unacceptable or that there is high potential that the earnings performance or capital position will be adversely affected. Risk management practices are deficient for the size, sophistication, and level of market risk accepted by the institution. The level of earnings and capital provide inadequate support for the degree of market risk taken by the institution.
5 A rating of 5 indicates that control of market risk sensitivity is unacceptable or that the level of market risk taken by the institution is an imminent threat to its viability. Risk management practices are wholly inadequate for the size, sophistication, and level of market risk accepted by the institution.

End of Proposed Text of Uniform Financial Institutions Rating System

Dated: December 13, 1996.

Keith J. Todd,

Assistant Executive Secretary, Federal Financial Institutions Examination Council.

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BILLING CODE 4810–33–P; 6210–01–P; 6710–01–P; 6720–01–P

FEDERAL MARITIME COMMISSION

Ocean Freight Forwarder License Applicants

Notice is hereby given that the following applicants have filed with the Federal Maritime Commission applications for licenses as ocean freight forwarders pursuant to section 19 of the Shipping Act of 1984 (46 U.S.C. app. 1718 and 46 CFR 510).

Persons knowing of any reason why any of the following applicants should not receive a license are requested to contact the Office of Freight Forwarders, Federal Maritime Commission, Washington, D.C. 20573.

Satt International Forwarding Inc., 147–35 Farmers Blvd., Jamaica, NY 11434, Officers: Agnes Tang, President, Flora Chen, Vice President

Latin American Brokers, Inc., 9581 Fontainebleau Blvd., #606, Miami, FL 33172, Officer: Alex Sklavounos, President

Diversified Transport Services, Ltd., 53 Nelson Blvd., Brewster, NY 10509, Officers: Andrew J. Quinn, Jr., President, Andrew J. Quinn, Sr., Vice President

Pegasus Transair, Inc., 1100 E. Dallas Road, Suite 310, Grapevine, TX 76051, Officer: Kenneth C. Beam, President

Dated: December 16, 1996.

Joseph C. Polking,

Secretary.

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