

# [OCC Logo]

Comptroller of the Currency  
Administrator of National Banks

Washington, DC 20219

Date: August 21, 2003

## OCC Significant Deviation Policy

### Enforceable 12 USC § 1818 Condition

The following condition is used for all new Bank Charters, applicable Mergers and Conversions, and Other Filings:

*The Bank: (i) shall give the [insert the appropriate OCC supervisory office] at least sixty (60) days prior written notice of the Bank's intent to significantly deviate or change from its business plan or operations<sup>1</sup> and (ii) shall obtain the OCC's written determination of no objection before the Bank engages in any significant deviation or change from its business plan or operations. [For Insured Charters Only insert: "For the first three years of operation, the Bank must also provide a copy of such notice to the FDIC's [insert the appropriate regional FDIC supervisory office."]*

### Definition

**A significant deviation or change ("significant deviation") for the purpose of this enforceable condition is defined as "a material variance from the bank's business plan or operations that occurs after the proposed transaction has been consummated (such as with a new bank charter, conversion, or merger)."**

### Purpose

Generally, the OCC uses this significant deviation condition to address heightened supervisory risk that exists during the first several years of a new bank charter's operations, or that exists in unusual cases after a conversion, merger, or other filing.

### *Applicability for Charters*

This condition is a standard condition required for all new bank charter approvals. New banks are particularly vulnerable to internal and external risks until they achieve a certain level of stability and profitability, clearly justifying the imposition of the significant deviation condition. The condition provides the OCC with the opportunity to evaluate any enhanced risks presented before the bank initiates a significant change to its business plan or operations.

<sup>1</sup> If such deviation is the subject of an application filed with the OCC, the OCC does not require any further notice to the supervisory office.

### *Applicability for Conversions*

The OCC considers the imposition of a significant deviation condition for conversion applications on a case-by-case basis. The condition of the converting institution, and whether the institution or sponsor plans to change its business plan or operations, are key considerations in assessing risks of institutions converting to national bank charters. If the converting institution has financial weaknesses (for example, weaknesses in capital, asset quality, earnings, or liquidity), or if the sponsor plans to make significant changes in the business plan or operations of the financial institution, or if the OCC believes that the institution is vulnerable to a potentially significant adverse change in the short- or intermediate-term, the OCC may impose the significant deviation condition.

Even though an applicant may disclose its plan to change the bank's operations in the application, the heightened supervisory risk resulting from the change may nonetheless warrant imposing this condition because the bank may subsequently fail to accomplish the original plan's objectives or the bank may subsequently deviate from the plan. The condition also may be appropriate if the applicant discloses future plans to offer a new product, service, or enter a new market, but no formal plans exist at the time that application is filed, and implementation of these plans will occur after OCC approval.

### *Applicability for Mergers*

The OCC will consider applying a significant deviation condition for merger applications on a case-by-case basis. The OCC is most likely to impose this condition for mergers if the sponsor plans a significant deviation in the operations of an existing national bank, or if the OCC believes the institution is vulnerable to a potential significant change in the short- or intermediate-term, or if the sponsor plans entry into the national banking system (for example, a merger of an existing entity with an interim national bank).

The OCC also may use the significant deviation condition for mergers and acquisitions where the financial condition of the target is less than satisfactory, the size of the acquisition target is large relative to the applicant, or the applicant's financial projections rely heavily on unproven efficiencies and strategies that may result in a subsequent deviation from the original plan.

### *Applicability for Other Filings*

The OCC generally will not impose a significant deviation condition on other filings. However, this safeguard potentially is available for any application where the OCC considers the supervisory risk warrants such a condition.

## Identifying Significant Deviations

A significant deviation from the bank's business plan or operations may include, but is not limited to, a material deviation or material change in the bank's:

- Projected growth, such as planning significant growth in a product or service.
- Strategy or philosophy, such as significantly reducing the emphasis of its targeted niche (for example, small business lending) in favor of significant expansion of another area (for example, funding large commercial real estate projects).
- Lines of business, such as initiating a new program for subprime lending.
- Funding sources, such as shifting from core deposits to brokered deposits.
- Scope of activities, such as establishing transactional Internet banking or entering new, untested markets.
- Stock benefit plans for de novo banks,<sup>2</sup> including the introduction of plans that were not previously reviewed during the chartering process with no objection by the OCC.
- Relationships with a parent company or affiliate, such as a shift to significant reliance on a parent or affiliate as a funding source or provider of back office support.

Changes in bank control or management are not considered significant deviations for purposes of this condition because existing law and regulation<sup>3</sup> provide other means for prior notification and an opportunity for OCC objection.

**Deviations in financial performance alone are not significant deviations under this condition.** However, the OCC still may consider the underlying reason(s) for the deviation in financial performance a significant deviation. For example, a bank could deviate from its pro forma balance sheet or budget because of significant growth caused by a new product that was not disclosed in the business plan or initial plan of operations. This is an example of a significant change that requires prior written notification to, and a written determination of no objection from, the supervisory office. On the other hand, if the bank's strategies are consistent with the business plan, but the bank simply experiences significantly more growth than planned, that growth, by itself, does not qualify as a significant deviation for this condition. Nevertheless, examiners will evaluate the supervisory risk that deviations from projected financial performance may pose to the bank, and what, if any, supervisory response is appropriate under the circumstances. For example, an examiner could determine that the bank's risk management systems are no longer adequate given the magnitude of the unplanned growth, and that deficient systems are a Matter Requiring Board Attention.

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<sup>2</sup> A de novo bank is defined as a newly chartered bank open less than three years.

<sup>3</sup> The Change in Bank Control Act in 12 USC 1817(j) and the OCC's implementing regulation in 12 CFR 5.50 generally require prior notification of a change in bank control. As a condition of the charter approval, the OCC retains the right to object to and preclude the hiring of any officer, or the appointment or election of any director, for a two-year period from the date the bank commences business (12 CFR 5.20(g)(2)).

## **Evaluating Significant Deviations**

Upon receipt of a prior notice, the supervisory office will evaluate whether the proposed deviation significantly elevates supervisory risk. The OCC assesses risk by its potential impact on a bank's earnings and capital. The OCC recognizes that some deviations are necessary or prudent. For example, a deviation from the business plan may be necessary to meet changes in local market conditions.

Examiners will determine if the risks that a bank is undertaking, or proposes to undertake, are properly managed. Generally, risks are not considered imprudent if they are understandable, measurable, controllable, and within the bank's capacity to readily withstand any financially adverse results. If examiners determine that risks are unwarranted or uncontrolled, the examiners will communicate to the bank's management and directors that a need exists to mitigate or eliminate the excessive risks. Appropriate actions may include reducing exposures, increasing capital, or strengthening risk management processes. Refer to the "Bank Supervision Process" booklet of the *Comptroller's Handbook* for more detailed discussions of risks and risk management systems. However, the bank's directors and management remain ultimately responsible for ensuring that the bank appropriately addresses risk.

## **Supervisory Actions and Communications**

If the evaluation of a proposed significant deviation results in little or no supervisory concern, the supervisory office should send a "no objection" letter to the bank. If the evaluation discloses supervisory concerns with a proposed deviation, the supervisory office will send an "objection" letter detailing the reasons for this determination.

If, despite the issuance of an objection letter, a bank subsequently engages in actions that reflect a significant deviation to, or change from, its business plan, additional supervisory or enforcement action will be considered consistent with the OCC's Enforcement Policy (PPM 5310-3 Revised).

If a significant deviation from the bank's business plan is disclosed during a supervisory activity (examination or periodic monitoring), and the bank has failed to obtain a prior written determination of no objection, the resulting supervisory action will reflect the degree of supervisory concern with the deviation. At a minimum, a violation of the Regulatory Condition Imposed in Writing (RCIW) will be cited. A violation of the RCIW can provide the basis for the assessment of Civil Money Penalties (CMPs) or other enforcement actions. All supervisory actions will be communicated to the bank in writing.

Please direct any questions or comments about this new policy to your local OCC supervisory or licensing office. Alternatively, you may contact Licensing Policy and Systems at 202-874-5060 located in Washington, DC.