

Nondeposit Investment Products

Examiners should evaluate the above-captioned function against the following control and performance standards. The Standards represent control and performance objectives that should be implemented to help ensure the bank operates in a safe and sound manner, and that the entity's objectives are carried out. Associated Risks represent potential threats to the bank if the standards are not achieved and maintained. The Standards are intended to assist examiners in analyzing important functions that may warrant additional review. All of the following Standards may NOT need to be considered at every bank. Conversely, these do NOT represent all of the control and performance standards needed for every bank. Examiners should continue to use their judgement when assessing risk.

Standards	Associated Risks
MANAGEMENT AND CONTROL	
The board establishes and approves goals and guidelines for an effective NDIP program. Management develops and implements effective policies, procedures, and controls.	An ineffective program may lead to inadequate control and supervision of NDIP activities.
NDIP personnel meet minimum qualifications and training standards as outlined in the Interagency Statement. Compensation practices comply with the Interagency Statement's guidelines.	The NDIP program may not operate properly without qualified employees. Improperly structured compensation programs may lead to unsuitable investment recommendations and inappropriate customer account activity.
NDIP disclosures are complete and accurate.	Incomplete or inaccurate disclosures may cause customer confusion between insured deposits and uninsured NDIP, leading to increased legal and reputational risk
Management takes reasonable precautions to eliminate customer confusion between the NDIP and retail deposit settings and operations.	Poorly designed sales settings and contact procedures can create customer confusion and expose the bank to risk.
Sales representatives offer suitable investment recommendations.	Sales representatives may recommend unsuitable investments given a specific customer's investment objectives and constraints. Inappropriate recommendations may lead to liability and increase reputation risk.
Proprietary products are controlled by comprehensive policies, appropriate internal controls, and direct board oversight.	Poor management may expose the bank to increased legal, reputation, liquidity, operational, and capital risk.
The board has established an independent review program that is commensurate with the scope and complexity of the NDIP activities. Independent reviews ensure that the NDIP program complies with all laws, regulations, the Interagency Policy Statement, and internal policies and procedures.	Management and the board may not be aware of inadequate operations of NDIP activities. Noncompliance with laws, regulations, policy statement, and internal policies increases the risk of loss and the possibility of litigation.

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Core Analysis Decision Factors

Examiners should evaluate Core Analysis in this section for significance and to determine if an Expanded Analysis is necessary. Negative responses to Core Analysis Decision Factors may not require proceeding to the Expanded Analysis. Conversely, positive responses to Core Analysis Decision factors do not preclude examiners from proceeding to the Expanded Analysis if deemed appropriate.

Do Core Analysis and Decision Factors indicate that risks are adequately identified, measured, monitored and controlled?

Core Answer: General Comment:(If any)

Core Analysis Decision Factors

- C.1. Are policies, procedures, and risk limits adequate?
- C.2. Are internal controls adequate?
- C.3. Are the audit or independent review functions adequate?
- C.4. Are information and communication systems adequate and accurate?
- C.5. Are personnel and compensation policies, procedures, and controls adequate?
- C.6. Do proprietary products have adequate oversight, disclosures, and reviews?
- C.7. Do the board and senior management effectively supervise NDIP activities?

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Expanded Analysis Decision Factors

This section evaluates the significance and materiality of deficiencies or other specific concerns identified in the Core and Expanded Analyses.

Do Expanded Analysis and Decision Factors indicate that risks are adequately identified, measured, monitored, and controlled?

Expanded Answer: General Comment:(If any)

Expanded Analysis Decision Factors

E.1. Are management deficiencies immaterial to the supervision of the NDIP function?

E.2. Are performance deficiencies immaterial to the institution's overall condition?

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Consider the following procedures at each examination. Examiners are encouraged to exclude items deemed unnecessary. This procedural analysis does not represent every possible action to be taken during an examination. The references are not intended to be all-inclusive and additional guidance may exist. Many of these procedures will address more than one of the Standards and Associated Risks. For the examination process to be successful, examiners must maintain open communication with bank management and discuss relevant concerns as they arise.

PRELIMINARY REVIEW

- 1 Review prior examination reports, prior examination work papers, pre-examination memoranda, and file correspondence for an overview of activities.
- 2 Review interim internal and external audit reports, and assess the adequacy of the audit scope.
- 3 Review remedial actions taken by management to correct audit and examination deficiencies.
- 4 Discuss with management any planned changes to NDIP activities. Determine if current and planned NDIP activities are consistent with the overall strategic plan.
- 5 Analyze data used by management to supervise NDIP activities. This data may include:
 - 5 A Policies and procedures.
 - 5 B Agreements with third parties.
 - 5 C NDIP activity and financial reports.
 - 5 D Available promotional materials.
 - 5 E Customer complaints and resolutions.
 - 5 F Customer disclosure forms.
 - 5 G Training programs materials and records.
 - 5 H Qualifications of all NDIP program personnel.
 - 5 I Proprietary product management reports.
- 6 When necessary, examiners can obtain the examination findings and work papers from the most recent NASD examinations of bank-affiliated brokers or dealers (Note: FDIC Regional Offices and Federal Reserve District Banks are responsible for contacting the appropriate NASD regional office and establishing information sharing procedures. NASD information should be requested prior to beginning pre-examination planning to ensure that it is available for offsite review.)
- 7 Determine if the institution offers IRA and Keogh accounts outside of a Trust Department. If so, include these accounts in the NDIP review

POLICIES AND PROCEDURES

- 8 Determine if policies and procedures are adequate for the NDIP activities. Policies and procedures should:
 - 8 A Ensure compliance with applicable laws, regulations, and the Interagency Statement.

- 8 B Designate a senior manager responsible for supervising NDIP activity.
 - 8 C Address product suitability for customers.
 - 8 D Designate employees authorized to recommend and sell NDIPs.
 - 8 E Establish separation of duties between NDIP sales, management, and accounting.
 - 8 F Delineate procedures and criteria for selecting and reviewing the NDIPs offered.
 - 8 G Establish guidelines for customer information usage.
 - 8 H Establish NDIP referral procedures.
 - 8 I Detail employee qualification, training, and compensation practices.
 - 8 J Ensure that bank's blanket bond covers NDIP activities.
 - 8 K Establish a process to document and resolve customer complaints.
 - 8 L Provide for an independent review of NDIP activities
- 9 Determine if disclosure procedures address the following:
- 9 A Disclosure training for NDIP personnel.
 - 9 B Minimum disclosures during NDIP sales presentations.
 - 9 C Minimum disclosures for all NDIP advertising and promotions.
 - 9 D Require customers to sign a statement that acknowledges receipt and understanding of all disclosures before the account is opened.

INTERNAL CONTROLS

- 10 Determine if the internal control program, at a minimum, includes the following elements:
- 10 A Official lines of authority, including authorization requirements.
 - 10 B Separation of duties between sales, supervision and accounting functions.
- 11 Verify that disclosures contain at least the minimum required content. Evaluate the NDIP program's standard materials, including the following items:
- 11 A Customer account disclosures.
 - 11 B Sales confirmations.
 - 11 C NDIP account statements.
 - 11 D Advertising and promotion materials.
- 12 Determine if the NDIP sales areas are clearly distinct, to the extent practicable, from retail deposit areas. In banks with multiple NDIP sites, evaluate a small sample of the NDIP sales locations.

13 Evaluate controls concerning product suitability. Determine if controls

13 A Require representatives to evaluate sufficient customer information before offering investment recommendations.

13 B Require representatives to clearly explain all recommendations to customers.

14 Verify that NDIP names are not identical to the bank's name.

15 Review customer complaints in the NDIP program's files and the FDIC or Federal Reserve Bank files. Determine if the complaints suggest a pattern of inadequate disclosures or customer confusion regarding the sales setting.

AUDIT OR INDEPENDENT REVIEW

16 Determine if the independent review process addresses the following:

16 A Identifies potential conflicts of interest.

16 B Monitors customer complaints and resolutions.

16 C Ensures the sales setting is physically separate, to the extent practicable, from the area where insured deposits are accepted.

16 D Verifies that third-party sales adhere to the agreement with the bank, applicable laws and regulations, and the Interagency Statement.

16 E Ensures that disclosure policies, procedures, and content comply with applicable laws, regulations, and the Interagency Statement.

16 F Samples customer files to verify that signed disclosure statements are obtained.

16 G Reviews all advertising and promotions for compliance with applicable laws, regulations, and the Interagency Statement.

16 H Scrutinizes the suitability process and samples customer account files.

16 I Evaluates proprietary product operations.

16 J Reports directly to the board or designated committee.

16 K Personnel qualifications and compensation policies and procedures.

INFORMATION AND COMMUNICATION SYSTEMS

17 Determine if managerial reports provide sufficient information relative to the size and risk profile of the NDIP activities. Reports may include the following types of information

17 A Types of products offered.

17 B Sales volume of each type of product.

17 C Amount of compensation received by each sales representative.

17 D Amount of compensation received by each employee for referrals.

17 E Overall return to the bank.

PERSONNEL AND COMPENSATION PROCEDURES

18 Determine if NDIP representatives and management are qualified to conduct their authorized duties.

19 Determine if the NDIP training program provides adequate continuing education.

20 Determine if compensation and referral policies and procedures comply with applicable laws, regulations, and the Interagency Statement.

PROPRIETARY PRODUCT RISK

21 Evaluate policies, procedures, board oversight, and management supervision relating to proprietary products.

22 Review other regulatory reports (from sources such as the National Association of Securities Dealers, the SEC or state insurance commissioners) for findings regarding proprietary products that may affect the bank's safety and soundness.

23 Verify that policies and procedures require sales representatives to clearly disclose proprietary products' risks, fees, and commissions.

24 Determine if proprietary products present excessive risk to the institution.

MANAGERIAL EFFECTIVENESS

25 Determine compliance with board policies.

26 Determine compliance with applicable laws, regulations, Nondeposit Investment Product examination guidance (FIL-48-97), and the Interagency Statement (FIL-9-94).

27 Determine if board records document appropriate oversight of NDIP activities.

28 If the bank has a networking arrangement with a third-party vendor, determine if the arrangement encompasses the following:

28 A Coverage by a written agreement.

28 B Approved by the board.

28 C Complies with all laws, regulations, and the Interagency Statement.

28 D Indemnifies the bank from the third party's NDIP activities.

28 E Provides for bank oversight, including the authority to remove sales representatives from bank premises.

28 F Establishes sales representative requirements.

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Generally, procedures used in the Expanded Analysis should target concerns identified in the Core Analysis and Decision Factors. Expanded procedures associated with Core Analysis and Decision Factors of no concern need not be used. The flexible guidelines specified for the Core Analysis also apply here.

POLICIES AND PROCEDURES

- 1 Investigate why NDIP policy or procedure deficiencies identified in the Core Analysis exist. Discuss recommendations with management. Possible reasons for policy deficiencies may include the following:
 - 1 A Management overlooked these issues.
 - 1 B Management is unfamiliar with guidelines and procedures for NDIP activities.
 - 1 C Management is unwilling to create or enhance policies and procedures.
- 2 If poor compliance with policies and procedures exist, determine the reasons. Possible reasons are detailed below:
 - 2 A Poor internal communication of policy and procedures or subsequent revisions.
 - 2 B Lack of awareness of policy existence.
 - 2 C Disregard for established policies.
 - 2 D Misunderstanding of policy and procedures.
- 3 Determine if management commits to and supports proper controls and monitoring to ensure policy guidelines are followed in the future. Determine if proposed controls, if any, are reasonable.

INTERNAL CONTROLS

- 4 Visit additional NDIP sales locations, and evaluate the NDIP promotional materials and sample customer information. Also determine if the NDIP sales setting is physically distinct, to the extent practicable from the retail deposit area.
- 5 Interview sales representatives and gauge their knowledge of and commitment to adequate disclosure.
- 6 Assess the extent of suitability problems and potential risk exposures, but do not judge the appropriateness of individual recommendations to customers or suggest alternatives. Contact your Senior Regional Capital Markets Securities Specialist (SRCMSS) (FDIC), Regional Capital Markets Securities Specialist (RCMSS), or Capital Markets Coordinator (FRB) for guidance.
- 7 Review a sample of customer files and determine if the file contains the following items:
 - 7 A Signed disclosure forms.
 - 7 B Evidence of representative's review of adequate customer information before offering investment recommendations.
 - 7 C Current customer data.

- 7 D Evidence that representatives provide complete information to customers regarding risks.
- 7 E Recommendations that consider the customer goals.
- 8 Analyze sales reports and promotions to determine if the following situations exist:
 - 8 A Questionable practices, such as account churning.
 - 8 B Unsuitable recommendation practices. For example, high volumes of volatile instruments or dramatic increases in a particular product's sales may indicate suitability concerns.

AUDIT OR INDEPENDENT REVIEW

- 9 Investigate why audit or independent review deficiencies identified in the Core Analysis exist.
- 10 Sample customer account files and determine if the independent review identifies documentation deficiencies.
- 11 Determine if the independent review tracks customer complaints and reports findings to the board.
- 12 Verify the accuracy of the independent review's reports to the board.
- 13 Interview NDIP staff and assess the independent review's oversight presence.

INFORMATION AND COMMUNICATION

- 14 Research the deficiencies in management reports to determine the underlying cause.

PERSONNEL AND COMPENSATION POLICIES AND PROCEDURES

- 15 Review sales representatives' files and assess their backgrounds and regulatory histories. If management does not maintain this information, they should obtain it for the examination and for internal review.
- 16 Sample compensation practices to determine if management adheres to all applicable laws, regulations, the Interagency Statement, and board policy.
- 17 Interview various branch employees, including tellers and receptionists, and determine if proper NDIP referral procedures are followed.
- 18 Review sales records and determine if only specifically designated personnel sell NDIPs.
- 19 Determine if referral practices are appropriate and determine if management adheres to applicable laws, regulations, the Interagency Statement, and board policy.

PROPRIETARY PRODUCTS

- 20 Evaluate management's policies, procedures, and ability relative to potential cash injections or liquidity problems.
- 21 Sample customer account files and verify that proper disclosures are included.

MANAGERIAL EFFECTIVENESS

Expanded Analysis

22 Determine the cause of the violations or contraventions to Statements of Policy and responsible party or parties. Consider the following:

22 A Lack of familiarity with laws, regulations, or policy statements.

22 B Negligence

22 C Misinterpretation

22 D Willful disregard and noncompliance.

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Impact Analysis reviews the impact that deficiencies identified in the Core and Expanded Analysis and Decision Factors have on the bank's overall condition. Impact Analysis also directs the examiner to consider possible supervisory options.

1 Determine if NDIP activities create current or potential contingent liabilities that can negatively affect earnings or capital. Consider the following issues:

1 A Settled, pending, and planned litigation.

1 B Regulatory investigations and sanctions.

1 C Failure to document minimum disclosures.

1 D Inappropriate product suitability or investment recommendation practices.

2 Determine if NDIP activities are eroding customers or the market place confidence in the institution. Assess the impact on reputation risk.

3 Evaluate the effect that current and planned NDIP activities may have on capital, earnings, and liquidity.

4 Gauge management's willingness and ability to correct deficiencies.

5 Determine the need for administrative and enforcement actions, formulate specific recommendations, and advise appropriate supervisory officials.