Federal Deposit Insurance Corporation
Division of Risk Management Supervision
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October 28, 2022

Board of Directors
b4,b8

Subject: April 4, 2022 Report of Examination (Report)

Members of the Board:

Enclosed is a copy of the subject Report prepared by the Federal Deposit Insurance Corporation (FDIC). The Report includes the findings of concurrent Information Technology (IT) and Bank Secrecy Act/Anti-Money Laundering examinations. Please thoroughly review the Report and document such review in the board minutes.

The overall condition of the bank remains satisfactory. Asset quality remains satisfactory with total adversely classified assets b4,b8 accounting for b4,b8 of Tier 1 Capital plus the ALLL. While overall underwriting and credit administration practices are generally adequate, Board decisions pertaining to digital asset-related lending exhibit an elevated risk appetite. Digital asset lending is a specialized area and the Board needs to develop comprehensive lending guidelines, portfolio limits, and accounting considerations to ensure credits are appropriate underwritten and administered.

The Report notes certain due diligence activities conducted for the b4,b8 loans extended to digital asset-related technology firms, yet it also highlights areas to improve underwriting and administration of these loans. In addition, the loan to b4,b8 is secured by Bitcoin and aspects of the collateral control and its ongoing perfection present uncertainties. Collateral safekeeping is facilitated by an affiliate of the borrower, highlighting an inherent conflict of interest and the nature of cryptoassets means that the recovery of the property following an improper transfer is difficult or impossible. The questionability in collateral control and its perfection, along with concerns noted within the Report, present weaknesses that warrant management's attention. Any future renewals should:

- clearly identify and assess the primary repayment source with a comprehensive financial analysis of the borrower itself;
- obtain documentation to establish the true ownership of the collateral; and
- arrange for independent and bankruptcy-remote collateral safekeeping.

If left uncorrected, these potential weaknesses may result in the deterioration of the institution's credit position at some future date.

Capital protection remains satisfactory for the risk profile. However, b4,b8 are noted related to temporary capital injections at the end of the third and fourth quarters of 2021. While the temporary capital injections were intended to offset the timing of temporary large deposits, a robust capital planning framework provides for capital at sufficient levels to manage growth and address emerging needs. Recommendations to formalize minimum capital levels and dividend practices are provided on the *Examination Conclusions and Comments* pages of the Report, and the Board is reminded that capital that is temporary in nature does not qualify for regulatory capital.

Board and management oversight is adequate. Management continues to pursue growth opportunities by incorporating digital asset-related activities. Consistent with Financial Institution Letter 16-2022, *Notification of Engaging in Crypto-Related Activities,* please provide this office with information necessary to allow a comprehensive assessment of the safety and soundness, consumer protection, and financial stability implications of the digital asset-related activities the bank engages in or is planning to engage in.

Bank Secrecy Act and Anti-Money Laundering compliance is satisfactory; however, management failed to file eight currency transaction reports, b4,b8 b4,b8 Additionally, a recommendation to strengthen management's ongoing customer due diligence monitoring procedures is noted. IT operations are satisfactory. One recommendation is detailed within the *Information Technology and Operations Risk Assessment* section of the Report to improve audit tracking procedures.

Following your review of the Report, please provide a written response to the above address or the FDIC Secure Email portal at ChiMailroom@fdic.gov within 45 days after the date of this letter as to the actions taken or planned with respect to the matters discussed above and within the Report.

Enclosed is an invitation to participate in the FDIC's post-examination survey process. Please refer to the invitation for details and instructions.

This letter and its contents (including attachments) are confidential and intended only for the bank's internal use. The disclosure of such confidential supervisory information is governed by Part 309 of the FDIC Rules and Regulations.

Please contact Case Manager b8 at b6,b8 or b8, if you have any questions or comments regarding the Report or this correspondence.

Sincerely,
Michelle Ogren
Acting Deputy Regional Director

Enclosures: Report of Examination
Post-Examination Survey Letter

cc: b8
Federal Reserve Bank of Chicago