① Language from 2014 SBNA Roll up Exam
② Response
③ update 12/31/14
④ Closure = ERM Exam

Matters Requiring Attention

MRAs are concerns that warrant Board and senior management's attention and require corrective action. These concerns include practices that deviate from sound governance, internal control, and risk management principles, which may adversely impact the bank's earnings and capital, risk profile, or reputation if not addressed, or that result in substantive noncompliance with:

- laws and regulations,
- internal policies, controls or processes,
- OCC supervisory guidance, or
- supervisory conditions imposed in interpretive letters or licensing approvals.

New Matters Requiring Attention

Issue: New Product Approval Processes

The initiation of SBNA's consumer auto leasing relationship with its affiliate, Santander Consumer USA (SCUSA), represented a transformational shift into a new product with a complex risk profile. The approval of this high growth strategy involving a new product without a comprehensive risk assessment or demonstrated ability to identify, measure, monitor, and control residual risk is a cause for supervisory concern. While management has subsequently expanded its review of this product, obtained residual value insurance to mitigate risk, and reduced its growth expectations, the necessary up-front analysis to determine whether this new product offered the appropriate risk-versus-return profile was not completed timely.

The nature of certain new products and services, or modifications to existing ones, can pose an elevated risk meriting a higher level of due diligence and scrutiny based on their potential impact to the bank's risk profile. Such initiatives would also warrant a higher level of approval outside of the original deliberating body. In our review of this roll out, we noted that there were no risk-based triggers subjecting new product proposals approved by management's Bank Activities Committee (BAC) to prior review and scrutiny of the Board or a designated committee thereof.

Required Corrective Action: The Board and management must ensure the bank's new product approval policies reflect the supervisory guidance included in *OCC Bulletin 2004-20 Risk Management of New, Expanded, or Modified Products and Services.* Management has engaged an external consultant to review SBNA's new product review policies and procedures. With the Board's advice and consent, management must revise these policies to incorporate a more comprehensive assessment of product risk, complexity, the need for risk systems commensurate with identified risks, and the potential impact of volatility in the product's performance in normal and stressed conditions on the bank's earnings and capital. To strengthen Board oversight, new product approval policies must incorporate risk and complexity triggers to require additional approvals of the Board or a designated committee thereof when appropriate.

10/20/14 Response to 2014 ROE

Required Corrective Action:

The Board and Management must ensure the bank's new product approval policies reflect the supervisory guidance included in OCC Bulletin *2004-20 Risk Management of New, Expanded, or Modified Products and Services.* Management has engaged an external consultant to review SBNA's new product review policies and procedures. With the Board's advice and consent, management must revise these policies to incorporate a more comprehensive assessment of product risk, complexity, the need for risk systems commensurate with identified risks, and the potential impact of volatility in the product's performance in normal and stressed conditions on the bank's earnings and capital. To strengthen Board oversight, new product approval policies must incorporate risk and complexity triggers to require additional approvals of the Board or a designated committee there of when appropriate.

Response:

An update to the SBNA's Enterprise Product Commercialization Policy (the "Policy") and related procedures is underway in which the tenets will be in alignment with the OCC's guidance as set forth in OCC Bulletin 2004-20. This Policy will establish an effective new product/business activities process in which SBNA: performs appropriate due diligence prior to introduction of the product; develops and implements controls and processes to ensure risks are properly measured, monitored, and controlled; develops and implements appropriate post-launch performance monitoring and review systems; and considers the potential impact of performance volatility on earnings and capital under both normal and stressed conditions.

The Policy, which will mandate the creation of risk profile thresholds triggering Board level review, will be reviewed by the Bank's New Products/Business Activities Committee and Executive Management Committee, prior to the review for approval by the SBNA Board of Directors.

The key enhancements of the Policy and process will include following:

- Adoption of a revised definition of new products, which includes new, expanded, or modified products, services, business initiatives or significant transactions (collectively "New Products/Business Activities or "NPBAs");
- Establishment of a governance and approval process that requires involvement at all levels of the organization;
- The assignment of responsibilities to the lines of business, control and oversight functions, and internal audit in accordance with the three lines of defense model;
- The establishment of a review and approval process that includes protocols, systems, and internal controls for identifying, evaluating, and managing NPBAs in accordance with sound risk management practices throughout each phase of the product lifecycle, from proposal through due diligence, risk assessment, approval, and post-launch monitoring and reporting.

In addition, with the Board's oversight and approval, management has substantially enhanced, and continues to enhance, the Policy and processes to ensure that proper new product identification methods are in place and that all NPBAs undergo a documented diligence analysis that considers, among other factors, the business case for the NPBA, risks associated with offering the NPBA, and available exit strategies. The diligence analysis helps to evaluate the risk profile of the product and whether there is a need to implement expanded risk systems and controls. Moreover, it includes detailed business line analysis and overview of the product and requires corporate functions such as Accounting, Compliance, Legal, Finance, Human Resources, Risk Management, Technology, and Operations, among others, to opine about the implementation of the product.

Through the product risk assessment, SBNA will assess the risks associated with the introduction of proposed new products, evaluate mitigating controls, and assign residual risk ratings. The risk assessment will provides a holistic view of the risks associated with the new product, inform the need for Action Plans for remediation of any identified control weaknesses that include detailed tasks owners and dates, and help shape the duration and scale of pilot programs (if applicable). Action Plans will be required for all High or Elevated residual risks as well as for all controls rated as "Weak" or "Needs Improvement". The risk assessment and underlying analysis will also dictate the scope and the frequency of post-launch monitoring and reporting. This risk assessment also will result in a residual risk rating for the NPBA. While the risk ratings eventually may be used to trigger approval levels within the SBNA, the SBNA Board will approve all NPBAs, subject to eventual approval by the Santander Holdings USA Board. Risk Management and Compliance will have veto power throughout this process.

The Board will receive periodic monitoring and reporting from the New Product/Business Activities Committee.

Specific milestones:

a. Finalize draft Policy. *To be completed 11/20/2014.*
b. Finalize draft Procedures, including risk assessment process and due diligence standards. *To be completed 11/20/2014.*
c. Finalize Implementation Plan, including training, testing and monitoring steps. *To be completed 11/20/2014.*
d. Review of Policy and Procedures and the Implementation Plan by the Executive Management Committee. *To be completed 11/30/2014.*
e. Review and approval of Policy and Procedures and the Implementation Plan by SBNA Board of Directors. *To be completed by 12/31/2014.*

Accountable parties for the above: **Christopher Pfirrman, General Counsel**
Steven Lucier, Legal Counsel

December 31, 2014

Mr. Jonathan D. Doherty
Examiner-In-Charge
Office of the Comptroller of the Currency
National Bank Examiners
75 State Street
MA1-SST-03-06
Boston, MA 02109

Dear Mr. Doherty:

Enclosed please find an update to a Matter Requiring Attention ("MRA") contained in the 2014 Report of Examination for SBNA related to the New Product Approval Process.

We appreciate your guidance and attention throughout this process.

As always, please let me know if you have any questions or concerns.

Sincerely,

Roman Blanco
Chief Executive Officer
On behalf of the Board of Directors

cc: Ronald Pasch, Deputy Comptroller, Office of the Comptroller of the Currency
SBNA Board of Directors
Marcelo Brutti, Chief Risk Officer
Maria Calero, US Chief Compliance Officer
Eduardo Gomez, Chief Internal Auditor
Christopher Pfirrman, US Chief Legal Counsel

Enclosures

Matter Requiring Attention

1) Issue: New Product Approval Processes

The initiation of SBNA's consumer auto leasing relationship with its affiliate, Santander Consumer USA (SCUSA), represented a transformational shift into a new product with a complex risk profile. The approval of this high growth strategy involving a new product without a comprehensive risk assessment or demonstrated ability to identify, measure, monitor, and control residual risk is a cause for supervisory concern. While management has subsequently expanded its review of this product, obtained residual value insurance to mitigate risk, and reduced its growth expectations, the necessary up-front analysis to determine whether this new product offered the appropriate risk-versus-return profile was not completed timely.

The nature of certain new products and services, or modifications to existing ones, can pose an elevated risk meriting a higher level of due diligence and scrutiny based on their potential impact to the bank's risk profile. Such initiatives would also warrant a higher level of approval outside of the original deliberating body. In our review of this roll out, we noted that there were no risk-based triggers subjecting new product proposals approved by management's Bank Activities Committee (BAC) to prior review and scrutiny of the Board or a designated committee thereof.

Required Corrective Action:

The Board and Management must ensure the bank's new product approval policies reflect the supervisory guidance included in OCC Bulletin *2004-20 Risk Management of New, Expanded, or Modified Products and Services.* Management has engaged an external consultant to review SBNA's new product review policies and procedures. With the Board's advice and consent, management must revise these policies to incorporate a more comprehensive assessment of product risk, complexity, the need for risk systems commensurate with identified risks, and the potential impact of volatility in the product's performance in normal and stressed conditions on the bank's earnings and capital. To strengthen Board oversight, new product approval policies must incorporate risk and complexity triggers to require additional approvals of the Board or a designated committee there of when appropriate.

Original Response from October 20, 2014:

An update to the SBNA's Enterprise Product Commercialization Policy (the "Policy") and related procedures is underway in which the tenets will be in alignment with the OCC's guidance as set forth in OCC Bulletin 2004-20. This Policy will establish an effective new product/business activities process in which SBNA: performs appropriate due diligence prior to introduction of the product; develops and implements controls and processes to ensure risks are properly measured, monitored, and controlled; develops and implements appropriate post-launch performance monitoring and review systems; and considers the potential impact of performance volatility on earnings and capital under both normal and stressed conditions.

The Policy, which will mandate the creation of risk profile thresholds triggering Board level review, will be reviewed by the Bank's New Products/Business Activities Committee and

Executive Management Committee, prior to the review for approval by the SBNA Board of Directors.

The key enhancements of the Policy and process will include following:

- Adoption of a revised definition of new products, which includes new, expanded, or modified products, services, business initiatives or significant transactions (collectively "New Products/Business Activities or "NPBAs");
- Establishment of a governance and approval process that requires involvement at all levels of the organization;
- The assignment of responsibilities to the lines of business, control and oversight functions, and internal audit in accordance with the three lines of defense model;
- The establishment of a review and approval process that includes protocols, systems, and internal controls for identifying, evaluating, and managing NPBAs in accordance with sound risk management practices throughout each phase of the product lifecycle, from proposal through due diligence, risk assessment, approval, and post-launch monitoring and reporting.

In addition, with the Board's oversight and approval, management has substantially enhanced, and continues to enhance, the Policy and processes to ensure that proper new product identification methods are in place and that all NPBAs undergo a documented diligence analysis that considers, among other factors, the business case for the NPBA, risks associated with offering the NPBA, and available exit strategies. The diligence analysis helps to evaluate the risk profile of the product and whether there is a need to implement expanded risk systems and controls. Moreover, it includes detailed business line analysis and overview of the product and requires corporate functions such as Accounting, Compliance, Legal, Finance, Human Resources, Risk Management, Technology, and Operations, among others, to opine about the implementation of the product.

Through the product risk assessment, SBNA will assess the risks associated with the introduction of proposed new products, evaluate mitigating controls, and assign residual risk ratings. The risk assessment will provides a holistic view of the risks associated with the new product, inform the need for Action Plans for remediation of any identified control weaknesses that include detailed tasks owners and dates, and help shape the duration and scale of pilot programs (if applicable). Action Plans will be required for all High or Elevated residual risks as well as for all controls rated as "Weak" or "Needs Improvement". The risk assessment and underlying analysis will also dictate the scope and the frequency of post-launch monitoring and reporting. This risk assessment also will result in a residual risk rating for the NPBA. While the risk ratings eventually may be used to trigger approval levels within the SBNA, the SBNA Board will approve all NPBAs, subject to eventual approval by the Santander Holdings USA Board. Risk Management and Compliance will have veto power throughout this process.

The Board will receive periodic monitoring and reporting from the New Product/Business Activities Committee.

Specific milestones:

a. Finalize draft Policy. *To be completed 11/20/2014.*
b. Finalize draft Procedures, including risk assessment process and due diligence standards. *To be completed 11/20/2014.*
c. Finalize Implementation Plan, including training, testing and monitoring steps. *To be completed 11/20/2014.*

d. Review of Policy and Procedures and the Implementation Plan by the Executive Management Committee. *To be completed 11/30/2014.*
e. Review and approval of Policy and Procedures and the Implementation Plan by SBNA Board of Directors. *To be completed by 12/31/2014.*

Accountable parties for the above: **Christopher Pfirrman, General Counsel**
Steven Lucier, Legal Counsel

Update:

SBNA has addressed this MRA and has completed the above referenced milestones as follows:

(i) SBNA's NPBA policy (Exhibit A) was reviewed by the Executive Management Committee and subsequently approved by the SBNA Board of Directors on December 11, 2014, which policy includes (a) a revised definition of new products to include new, expanded, or modified products, services, business initiatives or significant transactions, (b) a governance and approval process that requires involvement at all levels of the organization, (c) assignment of responsibilities to the business lines, control and oversight function and internal audit in accordance with the three lines of defense model, (d) a review and approval process that includes protocols, systems and internal controls for identifying, evaluating, and managing NPBAs in accordance with sound risk management practices throughout each phase of the product lifecycle, from proposal through due diligence, risk assessment, approval, and post launch monitoring and reporting, and (e) the SBNA Board of Directors will review proposed NPBAs for recommendation to the SHUSA Board of Directors;

(ii) SBNA's NPBA procedures (Exhibit B) were reviewed by the Executive Management Committee and approved by the NPBA Committee and the SBNA Board of Directors; and

(iii) the implementation plan (Exhibit C) (which includes training, testing and monitoring) was approved by the SBNA Board of Directors and is currently being executed.

SBNA respectfully requests closure of this MRA.

out of FLU risk management. However, a presentation to the BERC was planned after our exam fieldwork ended.

2. 2014 Report of Examination - New Product Approval Process - Closed

Issue: The initiation of SBNA's consumer auto leasing relationship with its affiliate, Santander Consumer USA (SCUSA), represented a transformational shift into a new product with a complex risk profile. The approval of this high growth strategy involving a new product without a comprehensive risk assessment or demonstrated ability to identify, measure, monitor, and control residual risk is a cause for supervisory concern. While management has subsequently expanded its review of this product, obtained residual value insurance to mitigate risk, and reduced its growth expectations, the necessary up-front analysis to determine whether this new product offered the appropriate risk-versus-return profile was not completed in a timely manner.

The nature of certain new products and services, or modifications to existing ones, can pose an elevated risk meriting a higher level of due diligence and scrutiny based on their potential impact to the bank's risk profile. Such initiatives would also warrant a higher level of approval outside of the original deliberating body. In our review of this roll out, we noted that there were no risk based triggers subjecting new product proposals approved by management's Bank Activities Committee (BAC) to prior review and scrutiny of the Board or a designated committee thereof.

Required Corrective Action: The Board and Management must ensure the bank's new product approval policies reflect the supervisory guidance included in OCC Bulletin 2004-20, "Risk Management of New, Expanded, or Modified Products and Services". Management has engaged an external consultant to review SBNA's new product review policies and procedures. With the Board's advice and consent, management must revise these policies to incorporate a more comprehensive assessment of product risk, complexity, the need for risk systems commensurate with identified risks, and the potential impact of volatility in the product's performance in normal and stressed conditions on the bank's earnings and capital. To strengthen Board oversight, new product approval policies must incorporate risk and complexity triggers to require additional approvals of the Board or a designated committee thereof when appropriate.

Status Update: We have closed this MRA in our records. The bank's policy and procedures for new product approvals are consistent with OCC Bulletin 2004-20, "Risk Management of New, Expanded, or Modified Bank Products and Services." The Board reviewed SBNA's New Products and Business Activities (NPBA) policy on December 11, 2014. The policy and procedures included a revised definition of new products, which includes new, expanded, or modified products, services, business initiatives, or significant transactions. The Executive Management Committee reviewed the NPBA procedures, and the NPBA Committee and SBNA Board approved them. The Board approved an implementation plan, which management is currently executing, that includes training, testing, and monitoring.

3. SL SBNA-2014-02 – Oversight of the ERM and HE (now HS) Projects - Closed

Issue: Oversight of the ERM and HE (now HS) projects requires improvement.

Office of the
Comptroller of the Currency
U.S. Department of the Treasury [http://occ.gov/index.html]

OCC BULLETIN 2004-20

Subject: Risk Management of New, Expanded, or Modified Bank Products and Services
Date: May 10, 2004

To: Chief Executive Officers, Directors, and Compliance Officers of National Banks, Department and Division Heads, Compliance Officers, and All Examining Personnel

Description: Risk Management Process

Purpose

This guidance reminds national banks of the process they should follow to prudently manage the risks associated with new, expanded, or modified bank products and services. Specifically, it outlines the expectations of the Office of the Comptroller of the Currency (OCC) for banks' management and boards to implement an effective risk management process.

The risk management principles outlined in this bulletin apply to the introduction of traditional and non-traditional bank products and services, as well as modifications to existing products and services. Modifications include changes in the terms or nature of an existing product or service that significantly alter the underlying risk characteristics of the product or service (e.g., significant changes in underwriting standards, geographic or industry focus).

Background

During periods of reduced net interest margins, stagnant growth in traditional business lines, and increased competition, bank management and directors face many challenges in seeking to improve the bank's financial performance. Engaging in new, expanded, or modified bank products or services is often considered a solution. However, if management and the board are overly focused on expected returns, do not have a good understanding of the inherent risks, or have poor governance practices, the bank's ability to effectively measure, monitor, and control the risks inherent in such products or services may be compromised.

Recently, the OCC has seen banks that have not performed the necessary up-front analysis to determine whether a potential new, expanded, or modified product or service offers the appropriate risk-versus-return profile and is consistent with the bank's strategic direction. Additionally, some banks have failed to implement appropriate risk management controls and processes. In some cases, these oversight failures have resulted in costly errors, unwarranted risk exposures, and deviations from the bank's business plan. Some historically well-managed banks have found themselves faced with problems because bank management underestimated its need to manage, monitor, and control the development and implementation of a product or service. Instead of boosting net income, the product or service caused systems and control problems, resulting in credit losses, compliance issues, litigation exposure, unfavorable returns, and diminished reputation in the marketplace.

Risk Management Process

The OCC expects bank management and the board to oversee all new, expanded, or modified products and services through an effective risk management process. Failure to provide an effective risk management process is an unsafe and unsound banking practice. An effective risk management process includes (1) performing adequate due diligence prior to introducing the product, (2) developing and implementing controls and processes to ensure risks are properly measured, monitored, and controlled, and (3) developing and implementing appropriate performance monitoring and review systems. The formality of the bank's risk management process should reflect the size of the bank and the complexity of the product or service offered. Depending on these factors, it may be appropriate for the bank to establish an executive management committee to oversee development and implementation of bank products and services.

Due Diligence

Before deciding to introduce a significant new, expanded, or modified product or service to bank customers, management and the board should conduct due diligence to ensure they have a realistic understanding of the risks and rewards of the product or service being considered. Management and the board should clearly understand the rationale for offering the product or service.[1]

The due diligence process should include:

- Assessing how the risks associated with the new, expanded, or modified product or service fits with the bank's business strategy and risk profile.
- Consulting with relevant functional areas, such as credit, compliance, accounting, audit, risk management, legal, operations, information technology, and marketing, as well as the Treasury/Asset Liability Committee (ALCO), to determine risks, concerns, and necessary controls.
- Determining requirements for complying with laws, regulations, and regulatory guidance.
- Determining the expertise needed to effectively manage the product or service, including the possible need to acquire additional expertise.
- Researching the background, experience, and reliability of relevant third parties.
- Developing a business and financial plan for the product or service that assesses the bank's competitive position and establishes objectives and strategies for how the product or service will be brought to market.
- Developing viable alternatives, including an exit strategy in the event the product or service fails to perform as expected.

Although the board may delegate performance of managerial duties to others, it has the ultimate responsibility for ensuring that the bank is run in a safe and sound manner. In fulfilling its responsibilities, the board or its designee must ensure that a new, expanded, or modified bank product or service is consistent with the bank's strategic goals.

Risk Management Controls and Processes

Once the bank decides to introduce a new, expanded, or modified product or service and develops a business plan, the board and management should develop and implement adequate risk management processes to effectively control the risks of the activity. This should include:

- Expanding and amending bank policies and procedures, as appropriate, to ensure that they adequately address the product or service. Policies and procedures should establish accountability and provide for exception monitoring.
- Developing and implementing the information and reporting systems (MIS) necessary to monitor adherence to established objectives and to properly supervise the product or service. MIS reports should contain key indicators to allow the board and management to effectively identify, measure, monitor, and control risk.
- Incorporating the product or service into the bank's audit and compliance processes to ensure adherence with bank policies and procedures and customer safeguards.

Performance Monitoring

Management and the board should have appropriate performance and monitoring systems in place to allow them to assess whether the product or service is meeting operational and strategic expectations. Such systems should:

- Include limits on the size of acceptable risk exposure that management and the board are willing to assume.
- Identify specific objectives and performance criteria to evaluate success of the product or service. The performance criteria should include quantitative benchmarks that will serve as a means to evaluate success of the product or service.
- Reflect a process that periodically compares actual results with projections and qualitative benchmarks, to detect and address adverse trends or concerns in a timely manner.
- Trigger changes in the business plan, when appropriate, based on the performance of the product or service. Such changes may include exiting the activity should actual results fail to achieve projections.

Risk Management of Third Parties

Unique risks are involved when a bank obtains new, expanded, or modified products and services through third-party vendors. Inferior performance or service on the part of a vendor may result in unexpected risks, including legal costs or loss of business to the bank. Although most vendors are reputable, their products may be unproven, or the risks associated with the product or service may conflict with bank safety and soundness standards or compliance requirements. In addition, the vendor's services may not be appropriate for the bank's unique market, personnel, or operating environment. These risks can be exacerbated by so-called "turn-key" arrangements that are designed to provide the bank with only minimal involvement in the administration and oversight of the product or service.

Bank management must ensure that it understands the risks associated with the activity and conducts adequate due diligence of the vendor, including assessing the proposed vendor's reputation, products, and financial condition. Management must also implement an ongoing oversight program over the vendor's activities and develop a contingency plan in the event the vendor cannot perform as expected. Management should not overly rely on the vendor's assertions, representations, or warranties, but should do its own analysis to ensure the vendor and its products are a good fit for the bank.

OCC Bulletin 2001-47, Third Party Relationships: Risk Management Principles, dated November 1, 2001, provides additional guidance to national banks on managing the risks associated with third-party vendors. This bulletin is available through the OCC Web site at http://www.occ.gov.

ASSOCIATED RISKS

Poor planning, oversight, or control may lead to an incomplete assessment and understanding of the risks involved with new, expanded, or modified bank products and services. This section highlights the primary risks that arise in their development and introduction.

Strategic Risk: The risk to earnings or capital arising from adverse business decisions or improper implementation of those decisions.

Strategic risk arises when a bank offers products and services that are not compatible with the bank's strategic goals or that do not provide an adequate return on investment. This kind of risk increases when management introduces new, expanded, or modified products or services without performing adequate due diligence reviews or without implementing an appropriate risk management infrastructure to oversee the activity. Strategic risk also increases when management does not have adequate expertise and experience to properly oversee these products or services.

Reputation Risk: The risk to earnings or capital arising from negative public opinion.

Reputation risk occurs when a bank offers new, expanded, or modified products or services without fully understanding its customers' business objectives or the economic purposes of the transaction. Reputation risk also arises when a bank stretches for income by offering products or services that involve practices or techniques that differ from the bank's standards. Reputation risk increases with poor service, inappropriate sales recommendations, or violations of consumer law, any of which may result in litigation, adverse publicity, and loss of business.

Using third parties to offer products or services, or expanding the use of existing third parties, may also expose the bank to reputation risk. This risk increases when bank management fails to closely monitor the quality and appropriateness of the provider's products or services. In cases where third-party employees interact directly with bank customers, reputation risk increases if interactions are inconsistent with the bank's policies, practices, and standards.

Credit Risk: The risk to earnings or capital arising from an obligor's failure to meet the terms of any contract with the bank or otherwise fail to perform as agreed.

Credit risk arises any time bank funds are extended, committed, invested, or otherwise exposed through actual or implied contractual agreements, whether reflected on or off the balance sheet. Since credit risk is found in all activities where success depends on counter-party, issuer, or borrower performance, it is often a key risk in new, expanded, or modified bank products and services.

Transaction Risk: The risk to earnings or capital arising from problems with service or product delivery.

A bank is exposed to transaction risk when products, services, or delivery channels do not fit with the bank's operational capacity, customer demands, or strategic objectives. Transaction risk can increase with the implementation of new information technology to support a new, expanded, or modified product or service. Failed or flawed technology, either from error, inadequate capacity, or fraud, may result in the inability to deliver products or services.

Compliance Risk: The risk to earnings or capital arising from violations of laws, rules, or regulations, or from nonconformance with internal policies and procedures or ethical standards.

Compliance risk arises when new, expanded, or modified bank products or services are not properly monitored for compliance with law, ethical standards, or the bank's policies and procedures. The potential for serious or frequent violations or noncompliance increases when a bank's oversight program does not include appropriate audit and control features. Compliance risk increases when the privacy of customer records is not protected, when conflicts of interest between a bank and affiliated third parties are not appropriately managed, and when a bank or its service providers have not implemented appropriate information security programs. Compliance risk also increases from inadequate accounting practices.

Other Potential Risks:

Depending on the product or service, a bank may be subject to increased liquidity, interest rate, price, or even foreign currency translation risk. Such risks will increase if bank management does not have a solid understanding of all risks involved and does not take all appropriate steps to control risks prior to introducing the product or service.

Supervisory Monitoring

The OCC's primary supervisory objective is to ensure that a bank does not assume more risk than it can effectively manage.

As part of ongoing supervision, OCC examiners will review significant new, expanded, or modified bank products and services, consistent with the OCC's supervision-by-risk framework. In particular, examiners will consider a product or service's impact on the bank's risk profile, and the effectiveness of a bank's product risk management program, including due diligence and oversight monitoring efforts. Examiners will be critical of banks that have not established appropriate risk management processes.

Bank management should discuss their plans with their OCC examiner-in-charge or supervisory office before developing and implementing new, expanded, or modified products or services, particularly if the new activity constitutes a significant deviation from the bank's existing business plan.[2]

Responsible Office

Questions concerning this guidance should be directed to Operational Risk at (202) 649-6550, or to Risk Evaluation at (202) 649-6360.

Mark L. O'Dell
Deputy Comptroller, Operational Risk

Kathryn E. Dick
Deputy Comptroller, Risk Evaluation

---

[1] A topical list of regulatory guidance addressing new or expanded bank products and services is attached. These reference materials are available through the OCC Web site at http://www.occ.gov.

[2] As part of its current practice, the OCC conditions approvals of certain licensing applications (charters, conversions, and other applications, where appropriate) upon the national bank giving the OCC's supervisory office prior notice of any significant deviation to the bank's operating plan.

Subject	Issuance	Date	Description
ACH Transactions	OCC Bulletin 2002-2	January 2002	Provides guidance on ACH transactions involving the Internet
Accounts Receivable and Inventory Financing	Comptroller's Handbook	March 2000	Describes selected risks associated with accounts receivable and inventory financing
Business Continuity Planning	FFIEC IT Examination Handbook	March 2003	Includes guidance on business continuity planning
Community Reinvestment Act Examination Procedures	Comptroller's Handbook	May 1999	Provides guidance on CRA exam process and evaluation.
Commercial Real Estate and Construction Lending	Comptroller's Handbook	November 1995	Describes selected risks associated with commercial real estate and construction lending
Community Bank Supervision	Comptroller's Handbook	July 2003	Includes discussion of strategic and reputation risk in community banks
Credit Card Lending	Comptroller's Handbook	October 1996	Describes specific aspects of credit card lending

Credit Card Lending: Account Management and Loss Allowance Guidance	OCC Bulletin 2003-1	January 2003	Communicates FFIEC expectations for prudent account management, risk management, and loan loss practices in the area of credit card lending.
Custody Services	Comptroller's Handbook	January 2002	Addresses the fundamentals of securities custody and related services.
Floor Plan Loans	Comptroller's Handbook	March 1990	Describes specific aspects of floor plan loans
Information Security	FFIEC IT Examination Handbook	December 2002	Provides guidance on information security
Insurance Activities	Comptroller's Handbook	June 2002	Describes specific aspects of insurance activities
Internet Banking	Comptroller's Handbook	October 1999	Describes selected risks associated with Internet banking
Investment Management Services	Comptroller's Handbook (Asset Management)	August 2001	Includes information on investment management services
Investment Portfolio Credit Risks: Safekeeping Arrangements	OCC Bulletin 2002-39	September 2002	Alerts banks to the potentially significant credit risks they incur when safekeeping investment portfolio assets with third parties
Lease Financing	Comptroller's Handbook	January 1998	Describes specific aspects of lease financing
Merchant Processing	Comptroller's Handbook	December 2001	Describes specific aspects of merchant processing
Mortgage Banking	Comptroller's Handbook	March 1996	Describes specific aspects of mortgage banking
Payment Systems and Funds Transfer Activities	Comptroller's Handbook	March 1990	Describes specific aspects of payment systems and funds transfer activities
Personal Fiduciary Services	Comptroller's Handbook (Asset Management)	August 2002	Includes relevant information on personal fiduciary services
Predatory and Abusive Lending Practices	OCC Advisory Letter 2003-2	February 2003	Provides guidelines to guard against predatory and abusive lending practices
Predatory and Abusive Lending Practices	OCC Advisory Letter 2003-3	February 2003	Provides discussion on avoidance of predatory and abusive lending practices in brokered and purchased loans
Purchases of Loans In Whole or In Part – Participations	OCC Banking Circular 181	August 1984	Describes appropriate practices for the purchase of loans and loan participations
Retail Nondeposit Investment Sales	Comptroller's Handbook	February 1994	Describes specific aspects of retail nondeposit investment sales
Risk Management of Outsourcing Technology	OCC Advisory Letter 2000-12	November 2000	Transmits FFIEC guidance on risk management practices when outsourcing technology services, including information and transaction processing and Internet banking activities
Subprime Lending	OCC Bulletin 1999-10	March 1999	Provides interagency guidance on risk management of higher risk retail credit products.
Subprime Lending	OCC Bulletin 1999-15	April 1999	Provides additional guidance on risk management of higher risk retail credit products.
Subprime Lending	OCC Bulletin 2001-6	January 2001	Supplements interagency guidance issued in March 1999 on subprime lending.
Third-Party Relationships: Risk Management Principles	OCC Bulletin 2001-47	November 2001	Provides detailed guidance on managing risks from business relationships with third parties
Third-Party Risk	OCC Advisory Letter 2000-9	August 2000	Alerts banks to potential credit risks arising from arrangements with third parties and emphasizes the importance of thorough due diligence and control over such risks
Third-Party Service Providers	OCC Bulletin 2002-16	May 2002	Provides guidance on risk management for foreign-based third-party service providers

Unfair or Deceptive Acts or Practices	OCC Advisory Letter 2002-3	March 2002	Provides guidance on unfair or deceptive acts or practices
Unsafe and Unsound Investment Portfolio Practices	OCC 2002-19	May 2002	Provides guidance on investment portfolio practices