



United States  
General Accounting Office  
Washington, D.C. 20548

General Government Division

B-259980

August 17, 1995

Mr. Joe M. Cleaver  
Executive Secretary  
Federal Financial Institutions  
Examination Council

Dear Mr. Cleaver:

This letter provides our observations on federal financial regulators' practices for screening applicants for director and senior bank executive positions under section 32 of the Federal Deposit Insurance Act. In implementing the law, federal bank and thrift regulators are to screen applicants' qualifications, background, and experience prior to their appointment or employment by insured depository institutions and holding companies falling into certain specified categories, such as newly formed or troubled institutions. We self-initiated work on this issue because of continued congressional interest in (1) the safety and soundness of financial institutions and (2) the fostering of uniform regulatory principles and supervision.

Overall, we observed that the four regulators follow somewhat different requirements and practices when processing the section 32 notices that certain banks, thrifts, and holding companies must submit to regulators prior to appointing or employing senior bank officials. Specifically, we noted differences in the extent of information that regulators require for assessing applicants' qualifications for director and senior executive positions. We also noted that regulators follow different practices when required background checks take longer than the statutorily prescribed 30-day processing period.

Section 303(a)(2) of the 1994 Riegle Community Development and Regulatory Improvement Act (P.L. 103-325) seeks to promote uniform supervisory policies among depository institution regulators. The differences we identified in regulatory practices could result in the uneven treatment of the institutions and of applicants seeking to be confirmed as key officers.

GAO/GGD-95-181R Differences in Screening Bank Executives

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BACKGROUND

Section 32 of the Federal Deposit Insurance Act requires certain insured depository institutions and holding companies to give 30-day notice to the appropriate regulator of pending employment actions involving the hiring or appointment of a bank director or senior executive officer. Institutions subject to this requirement include banks, thrifts, and depository-institution holding companies that (1) have been chartered for less than 2 years, (2) have undergone a change in control within the preceding 2 years, (3) are not in compliance with minimum capital requirements, or (4) are otherwise in a troubled condition.

Four federal regulators are responsible for screening applicants: (1) the Office of the Comptroller of the Currency (OCC), (2) the Federal Deposit Insurance Corporation (FDIC), (3) the Federal Reserve Board (FRB), and (4) the Office of Thrift Supervision (OTS). All four regulators have a 30-day window to process section 32 notices. This process involves conducting background checks and screening the applicant's work history--as well as assessing the applicant's competence, experience, character, and integrity--to determine whether the applicant's employment or association with the institution is in the best interest of depositors and the public. If an application is not disapproved within the 30 days, the applicant may begin work for the financial institution.

During the screening process, the regulators' procedures call for the gathering of biographical profiles and other personal references and information on applicants from various agencies and other regulators. As part of this process, the regulators submit requests for background checks to outside agencies, such as the Federal Bureau of Investigation, the Drug Enforcement Administration, or Customs. The screening process also involves the solicitation of information from examiners and other regulators who may have knowledge of the applicant's work experiences. When regulators receive negative information, they customarily conduct follow-up investigations to determine how the information affects the applicant's suitability for the position being sought. If no adverse information is received, regulators ordinarily notify applicants that they have no objection to the pending employment.

For fiscal years 1990-1994, financial institutions submitted a total of 18,176 section 32 notices to the four regulators. The peak year for filings over the 5-year period was 1992, when 4,297 notices were filed.

The objective of our preliminary work was to determine whether the four regulators were uniform in processing section 32 notices. To identify any differences in the processes regulators used for

assessing the qualifications of applicants, we reviewed the types and amount of information required by the four regulators, and we examined a judgmental sample of notices, ranging from 5 to 10 for each regulator. We picked these notices to obtain a mix of those which had been approved, denied, or suspended. In addition, we discussed regulatory policies and procedures with field office and headquarters officials. The work was conducted in the western regions or districts of OCC, FDIC, FRB, and OTS from November 1994 through May 1995. We selected western regions or districts because they were among the most active in processing appointment and employment notices.

INFORMATION FOR ASSESSING APPLICANTS  
DIFFERS AMONG REGULATORS

Our work indicated that the extent of information required by regulators to assess applicants' qualifications for director and senior executive positions differs widely. For instance, FRB requires applicants to fill out a 3-page questionnaire, while OCC requires that applicants and bank officials submit a detailed 15-page biographical profile. Similarly, while three of the four regulators require applicants to submit fingerprints for background checks, FRB does not require them. We likewise found that OCC and OTS are to routinely request information on an applicant's professional certification, but that the other two regulators do not require this information.

We also noted wide variations in the amount of detailed information regulators are to gather on applicants' financial affairs and previous employment. In comparison with FRB and OCC, which request information only on past bankruptcies, FDIC and OTS request full, detailed disclosures of sources of income, assets, and obligations. We noted that only OTS requires federal income tax returns from previous years. Requests concerning information on past employment range from OTS's requirement that applicants furnish employment data for the previous 5 years, to FDIC's requirement that information be provided on all past and present employment.

In addition, we noted differences in the regulators' customary procedures for requesting background checks from other federal agencies and for soliciting comments on applicants from other regulators. OCC procedures provide for the collection of background information from IRS as part of the agency's standard background check, while the three other regulators do not request an IRS background check. Another difference is that, while OCC, FDIC, and FRB procedures call for soliciting comments from other regulators, OTS makes only the FDIC inquiry mandatory. Likewise, OCC, FDIC, and FRB procedures call for routinely requesting background checks from

the FBI, the Drug Enforcement Administration, and Customs, while OTS requires only an FBI background check.

These procedural differences at least partly result from the individual regulator's past experiences. For example, FRB considers the cost to the agency and the applicant in determining how much information to collect. However, an OTS official told us that the agency collects a greater amount of information on applicants' qualifications because of concerns that originally arose in the 1980s about unqualified applicants entering the thrift industry. Similarly, regulatory officials told us that their procedures for processing section 32 notices are, for the most part, patterned after earlier procedures used for other chartering activities, such as new bank applications.

Processing of Notices With Incomplete  
Background Checks Differs

The regulators follow different processes when, at the end of the 30-day period, background checks are incomplete because of delays in the receipt of information requested from federal agencies or other sources. In such instances, some regulators' policies call for section 32 notices to be processed without waiting for the completion of background checks. Other regulators either request that the institution or holding company delay employing or appointing the applicant until background checks have been completed, or consider the application incomplete until the background check is finished.

OCC and FDIC process notices at the end of the 30-day period without waiting for information from federal agencies or other sources needed to complete background checks. OCC and FDIC officials told us that, unless they have other compelling reasons to delay their decisions, they do not hold up processing of the notices. They explained that if adverse information were to be received after their decision, they could always initiate proceedings under other statutes to remove applicants. OCC includes a qualifier in its letters to banks and applicants indicating that action may be taken if background checks should later disclose adverse information. FDIC does not see a need to qualify its consent statement since it views any removal action it takes as within its own authority.

Conversely, FRB and OTS ordinarily do not process notices until all background checks have been completed. These two regulators may make exceptions to this policy if an applicant's prior work history in the banking industry is known to them. In such instances, these regulators may choose to proceed with the processing of notices in the absence of a background check, according to FRB and OTS officials. However, when background checks have not been completed

as the end of the 30-day period approaches, the two regulators more typically seek an extension of the processing period or ask the banking institution to certify that applicants will not begin work until background checks have cleared review. An FRB applications analyst told us that FRB typically seeks an extension whenever it lacks prior knowledge of the applicant. An OTS analyst said that OTS is more likely to ask for certification in such instances.

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The differences in regulatory practices for gathering and processing applicant information could result in the uneven treatment of banks and of applicants seeking to be confirmed as key bank officers. We believe that the Council, in pursuing its mandate to foster uniform regulatory principles and standards among federal financial regulators, should find the information in this letter useful in assessing differences in regulatory practices and their impact on the banking industry.

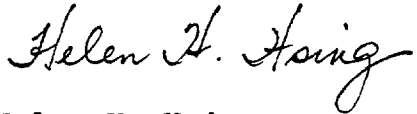
When we shared our preliminary results with you, you mentioned that the Council would likely pursue this issue as part of the Council's review of regulatory differences among the regulators. You noted that a working group composed of the regulatory agencies has begun to identify other differences and that the differences we identified would be incorporated into the working group's review. We view the Council's interest in coordinating such an assessment as a positive step towards reducing regulatory differences. In helping the regulators to assess these differences, the Council may wish to focus the working group's efforts on determining whether there are justifiable reasons for the differences and identifying the best regulatory practices and employing them consistently among regulators. We plan to do no further work on section 32 requirements; however, we remain interested in the Council's efforts and look forward to hearing from the Council about the results of the joint regulatory study and any actions taken by the regulators to more closely harmonize their practices for screening applicants.

It is our understanding that you will send copies of this letter to the federal financial regulators. We are providing copies of this letter to the Chairman and Ranking Minority Member of the Senate Committee on Banking, Housing, and Urban Affairs; and the Chairman and Ranking Minority Member of the House Committee on Banking and

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Financial Services. If you have questions, please contact Kane Wong at (415) 904-2150 or me at (202) 512-8678.

Sincerely yours,

A handwritten signature in cursive script that reads "Helen H. Hsing".

Helen H. Hsing  
Associate Director, Financial  
Institutions and Markets Issues

(233439)

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