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State of North Dakota
DEPARTMENT of FINANCIAL INSTITUTIONS

A MESSAGE FROM COMMISSIONER ENTRINGER

It has been quite an interesting year so far with now two Revised State Revenue Forecasts, an allotment for General Fund agencies, the Governor's release of the Budget Guidelines for the 2017-2019 session and now a special legislative session to deal with the revenue shortfall. Our staff has been busy preparing the Department budget for the upcoming biennium which is due to be submitted this month.

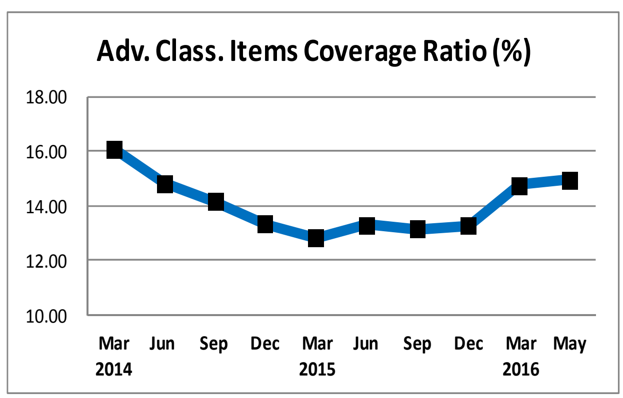
The one thing I would like to highlight is the seminar we hosted in Bismarck on May 11th, the Executive Leadership of Cybersecurity (ELOC). We had about 75 attendees from banks and credit unions across the state. I would really like to thank all of you that attended or sent people to the seminar. I have not seen the results of the survey thus far but the people I spoke with indicated the seminar provided good information. The afternoon was sort of the highlight for me when Lise Kruse, Tom Metelmann and Karla Hammer from the FDIC did a tabletop exercise with all the participants and then closed out the afternoon with highlights from the Cybersecurity Assessment Tool or "CAT". I am also grateful that Phillip Hinkley from the Texas Department of Banking participated as a presenter; I thought he did an excellent job! After his presentation I had the opportunity to visit with him and one of the suggestions he gave me is really where I am heading with this article. I would like to encourage all of you to consider participating in the FS-ISAC 2016 Cyber-Attack Against Payment Systems or CAPS. CAPS is a simulated tabletop exercise responding to a cyber-attack scenario related to payment systems. The link for a description of the exercise can be found at https://www.fsisac.com/2016-caps-exercises-us-canada And how timely is this? The FFIEC released a statement on June 7, 2016, regarding Cybersecurity of Interbank Messaging and Wholesale Payment Networks! The CAPS exercise is open to all regulated financial institutions in the U.S. and Canada and you can choose from two different dates in September to participate.

Thanks again to all of you that attended our ELOC Seminar. I hope the remainder of your summer is enjoyable and uneventful!

FACTS & FIGURES

As of June 30, 2016:

- Average Adversely Classified Items Coverage Ratio: 14.85%
- Average Adversely Classified Assets/Total Assets: 1.49%
- Average Adversely Classified Loans/Total Loans: 1.92%
- Average Past Due & Nonaccrual Loans/Total Loans: 1.30%



New information technology examination program

The FDIC has recently released an updated IT program for examiners to use when conducting IT examinations. The new program is known as InTREx (Information Technology Risk Examination) and will provide for a more efficient, risk-focused approach. Beginning July 11, 2016, FDIC and DFI examiners will use the new program for IT examinations. Notable changes for banks include, but are not limited to, the following:

- All Uniform Rating System for Information Technology (URSIT) components and composite ratings will be assessed and assigned at each IT examination (Audit, Management, Development & Acquisition, and Support & Delivery);
- The IT Officer's Questionnaire has been replaced by the IT Profile. The IT Profile contains fewer questions and is intended to help examiners focus resources.
- Before a scheduled IT examination, the bank will receive the IT Profile to be completed and returned to examiners.
- Banks may also notice a change in the items requested in the IT Request Letter as the new InTREx Program includes more specific transaction testing than the prior IT program.

More information, along with the full InTREx Program that will be used by examiners, can be found here.

BSA update

Final Rule on Customer Due Diligence Requirements: On May 5, 2016, the Financial Crimes Enforcement Network (FinCEN) released its final rule on beneficial ownership with respect to Customer Due Diligence (CDD) requirements. The final rule is focused on the second element of CDD – identifying and verifying the beneficial owners of a legal entity. The final rule contains two major provisions: (1) a new Beneficial Ownership requirement, and (2) the establishment of a so-called "fifth pillar" of the Anti-Money Laundering program requirements. The rule applies to "covered financial institutions" which includes depository institutions. Covered financial institutions will be required to comply with the final rule by May 11, 2018. To learn more and to read the final rule, click here for FinCEN's Frequently Asked Questions regarding the final rule.

Real estate evaluations

Supervisory Expectations for Real Estate Evaluations: Apparent violations related to real estate appraisals and internal evaluations continue to be frequently cited in our Reports. Some recent examples include:

- Lack of certified appraisals on certain transaction;
- Unsupported internally prepared evaluations; and
- Lack of independence on internally prepared evaluations.

Recently, the Federal banking agencies released an advisory on supervisory expectations when using an evaluation for certain real estate-related transactions. The advisory addresses transactions that permit an evaluation, preparation of an evaluation, and contents of an evaluation report. The Interagency Advisory can be found here.

Reporting unused loan commitments

Recent examinations reveal that many of our banks continue to struggle with proper reporting of unused loan commitments. Banks are reminded that *all* unused loan commitments are to be reported on Schedule RC-R of the Report of Condition and Income. The following summary of the requirements may be helpful:

- Commitments that are *unconditionally cancelable* are reported at a zero percent credit conversion rate. (Part 324.33(b)1 & RC-R Part II line 19)
- Commitments with an original maturity of less than one year and not unconditionally cancelable are reported at a 20 percent credit conversion rate. (Part 324.33(b)2 & RC-R Part II line 18a)
- Commitments with an original maturity of more than one year and not unconditionally cancelable are reported at a 50 percent credit conversion rate. (Part 324.33(b)3 & RC-R Part II line 18c)
- *Unconditionally cancelable* means with respect to a commitment, that an FDIC-supervised institution may, at any time, with or without cause, refuse to extend credit under the commitment (to the extent permitted under applicable law). (Part 324.32)
- A demand clause, by itself, is not sufficient to satisfy the unconditionally cancelable language. (Federal regulatory FAQ March 31, 2015, page 13)
- To be unconditionally cancelable, the agreement between the bank and borrower must contain language that permits the bank, at any time and without cause, to refuse to extend further advances on the line of credit.

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