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The ABCs of Banking Law: Supervision, Examination & Enforcement

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Overview



What is the purpose of supervision?

How is supervision conducted?

What results from an examination?

Is supervisory information confidential?

What happens if an examination uncovers violations of law or unsafe and unsound practices?

Have there been recent changes in how the agencies approach supervision and examination?



Supervision, Examination & Enforcement



While laws set out the rules of the road for the financial industry, supervision is a continuous process for overseeing a bank's condition and risk profile and its compliance with the laws that are applicable to its business.

Supervision is cradle to grave – from chartering to resolution – and is tailored in areas to address the risk profile and complexity of individual institutions.

Agencies use their supervisory tools to evaluate the types of risks present at an institution, the amount of risk, how well the institution is managing the risks, and, directionally, where risk is trending.

These supervisory assessments are communicated to the institution's board and senior management and set out supervisory views of the overall condition of the institution and whether there are financial or risk management weaknesses that require correction.

If the agencies have identified weaknesses, they may seek to address them through either the supervisory process or through enforcement actions.



Supervisory Framework



Focus of Federal financial services regulators:

- Office of the Comptroller of the Currency (OCC): financial and nonfinancial risks of national banks and federal savings banks;
- Board of Governors of the Federal Reserve System (FRB): financial and nonfinancial risks of bank holding companies and state member banks;
- Federal Deposit Insurance Corporation (FDIC): financial and nonfinancial risks of state nonmember banks; protection of the deposit insurance fund;
- Consumer Financial Protection Bureau (CFPB): compliance with Federal consumer protection legislation and regulations;
- Securities and Exchange Commission (SEC): effective functioning of the securities markets and investor protection, and
- Commodity Futures Trading Commission (CFTC): effective functioning of the futures and options markets and protections related to the sale of commodities and financial futures and options.



How is Supervision Conducted?



Access to books and records; speaking with management.

12 USC § 481: “The Comptroller of the Currency, with the approval of the Secretary of the Treasury, shall appoint examiners who shall examine every national bank as often as the Comptroller of the Currency shall deem necessary. The examiner making the examination of any national bank shall have power to make a thorough examination of all the affairs of the bank and in doing so he shall have power to administer oaths and to examine any of the officers and agents thereof under oath and shall make a full and detailed report of the condition of said bank to the Comptroller of the Currency....”

Full scope examinations are periodically required, and targeted examinations may focus on a product, an organizational function, a type of risk, or a specialty area.

Supervision is also conducted through:

- Horizontal exams (examinations across a range of institutions focused on a particular issue or matter).
- Periodic reporting requirements (e.g, bank call reports).
- Corporate applications or notices for expansionary activities (mergers, branching, new products and services, etc.).
- Systemic risk evaluations (CCAR, stress testing, recovery and resolution planning).



How are Examinations Conducted, and What Results from Them?



How are examinations conducted:

- Examination letters (setting out the scope of the exam, information needed, timing);
- Entrance meetings (discussing the exam scope, role of the exam team, and how it will be conducted; confirming availability of institution's personnel);
- Periodic check-ins (discussing any key issues identified or challenges in the examination), and
- Exit meetings (preliminary findings/conclusions, seeking commitments to any needed corrective actions, discussing needed follow-up supervisory activities).

What Results from Examinations:

- Supervisory Letters (supervisory observations, matters requiring attention, violations of law);
- Examination/Inspection Reports, and
- Potentially, Enforcement Actions.



Have there been recent changes to the supervisory approach?



The OCC and FDIC have announced proposed reforms governing when MRAs may be issued. Under the proposal,

- MRAs would only be issued when a practice (or failure to act) is an unsafe or unsound practice or it is an actual violation of law.
- a practice (or failure to act) would be unsafe or unsound if it is contrary to generally accepted standards of prudent banking and, if continued, is likely either to materially harm the financial condition of the bank or cause a material risk of loss to the Deposit Insurance Fund or has already materially harmed the institution; and
- examiners could issue “supervisory observations,” but these would be non-binding (the institution would not be required to remediate the observation).

While the FRB did not join in issuing the proposal, it has separately signaled shifting to similar principles, issuing “Supervisory Operating Principles” in November 2025 that announced “sharpening” its examinations and ratings to material financial risks, reducing duplication of examination efforts among supervisors, and streamlining remediation of supervisory matters.

More generally, the agencies have been working to tailor regulations and examinations to account for differences in institutional size, complexity, and risk profile and to remove reputational risk considerations from examination materials and regulations.



Supervisory Ratings



Supervisory Ratings

- CAMELS ratings for depository institutions (OCC, FDIC, FRB): Capital adequacy, Asset quality, Management, Earnings, Liquidity, Sensitivity to risk.
- Consumer compliance ratings (CFPB): Evaluates the board and management, the compliance program, and violations of law and consumer harm.
- LFI and RFI/C(D) ratings for bank holding companies (Federal Reserve):
 - Large Financial Institution ratings for BHCs \geq \$100 Billion of total consolidated with ratings (broadly meets expectations, conditionally meets expectations, Deficient-1 and Deficient-2) across 3 rated categories: capital planning and positions; liquidity risk management and positions; and governance and controls.
 - In November, the FRB finalized revisions to the LFI ratings, removing a prior automatic enforcement action presumption for any Deficient-1 category and allowing for the institution to be considered “well-managed” provided it has no more than 1 Deficient-1 component rating.
 - Risk management, Financial condition, Impact on depository institution subsidiaries, Composite and Depository institution subsidiary ratings for BHCs $<$ \$100 Billion of total consolidated assets.

Why do ratings matter?



Confidential Supervisory Information is ... Confidential



Non-public / confidential supervisory information extends to all information related to an agency's supervision, licensing, regulation, and examination of an institution and is considered the confidential information of the agency – not the subject institution.

Unless permitted by the agency's regulations or unless expressly authorized by the agency in writing, disclosure of its CSI is prohibited [12 CFR Part 261 (FRB); 12 CFR Part 4 (OCC); 12 CFR Part 309 (FDIC); 12 CFR Part 1070 (CFPB)].

The agencies have made efforts to harmonize their disclosure rules, but differences exist, and requirements for disclosure vary based on the recipient:

- to officers, employees or directors of the subject institution;
- to parent companies or to affiliates;
- to external auditors;
- to outside counsel;
- to consultants, and
- to other agencies with supervisory authority over the institution .

Institutions and individuals that violate the disclosure rules may be subject to enforcement actions.



Enforcement Actions



Violations of law or unsafe or unsound conditions or practices may result in an enforcement action.

When do agencies use enforcement actions vs. continuing to use the supervisory process?

Agencies utilize discretion, considering: examination ratings; risk profile; severity of matter; extent of unsafe/unsound practices; ability of board and management to correct deficiencies in a timely manner; potential adverse impact to customers, the deposit insurance fund, or the public generally; the existence, nature and extent of prior uncorrected deficiencies; and progress in achieving compliance with existing enforcement actions.

If an enforcement action is merited, the action may either be informal or formal.

Agencies consider the severity of the matter, supervisory ratings, and level of risk at the institution, with informal actions generally used when the institution's condition is sound but the deficiencies either have not been timely corrected or the nature of the deficiency warrants escalation beyond citation of a violation of law or documentation of a concern in a supervisory letter.

There are different types of informal and formal enforcement actions used to achieve different supervisory objectives that may be taken alone or in conjunction with one another and against the institution and/or its affiliated parties (directors, officers, employees, certain stockholders, consultants, etc.).



Enforcement Actions



Examples of informal actions include:

- Commitment letters;
- Memorandums of Understanding, and
- Notices of Deficiency (OCC Part 30).

Examples of formal actions include:

- Written Agreements/Consent Orders;
- Cease & Desist Orders;
- Temporary C&D Orders;
- Civil Monetary Penalties;
- Restitution Orders;
- Removal and Prohibition Orders;
- Prompt Corrective Action Orders, and
- Safety & Soundness Orders.



Civil Monetary Penalties (CMPs)



The general authority to issue CMPs against insured banks and IAPs derives from 12 USC 1818(i), which classifies CMPs into three tiers based on the severity of the conduct and level of culpability:

- Tier 1: violations of law or regulation, final or temporary orders, conditions imposed in writing, or written agreements;
- Tier 2: Tier 1 criteria as well as reckless engagement in unsafe and unsound practices or breach of fiduciary duty that is either part of a pattern of conduct, or that causes, or is likely to cause, more than minimal loss, or that resulted in pecuniary gain, and
- Tier 3: Tier 2 criteria that knowingly or recklessly caused substantial loss or resulted in substantial pecuniary gain.

1818(i) requires that agencies consider the following in setting the amount of the CMP: size of the financial resources and good faith; the gravity of the violation; history of prior violations; and other factors that justice may require.



Civil Monetary Penalties (CMPs)



To assess the statutory considerations, the agencies will take into account the following relevant factors:

evidence that the violation was intentional; the duration and frequency of the violation or practice; whether the violation or practice was continued after notification; failure to cooperate; efforts to conceal the violation or practice; actual or threatened loss or harm to the institution; financial gain or benefit; evidence of restitution; history of prior violations; prior criticism for similar actions; state of compliance program; tendency to engage in violations, and the existence of enforcement agreements.

Agencies utilize a weighted matrix for scoring the level of severity of each relevant factor, which results in a suggested (non-binding) amount.

Utilization of the matrix may result in no suggested CMP, and agencies may instead issue a supervisory letter or letter of reprimand if the matrix results in a small suggested CMP, the misconduct was technical in nature, and there is no prior history of misconduct or intent.



Civil Monetary Penalties (CMPs)



Supervision consults with agency legal and enforcement teams for application of the matrix and prior notice is generally provided before a CMP is assessed or a reprimand letter issued.

The recipient is provided an opportunity to respond.

If the agency elects to proceed with a CMP, the recipient receives a letter outlining the assessed CMP and a proposed consent order.

If the recipient does not accept the order, the agency files a notice of assessment (presumptively made public) and commences an administrative hearing.

If the agency elects not to proceed with a CMP, it is not barred from deciding later to act, and the election does not serve to waive other agency rights.

