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When Bank Examiners Get it Wrong: Financial Institution Appeals of Material Supervisory Determinations

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When Bank Examiners Get It Wrong: Financial Institution Appeals of Material Supervisory Determinations[†]

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Banks and credit unions sometimes complain that the examination process regulators use to police banking practices is oppressive. These financial institutions complain that regulators reach unduly negative examination conclusions known as "material supervisory determinations." Institutions are wary because negative determinations can subject an institution to further regulatory scrutiny or enforcement actions.

To guard against erroneous determinations, Congress, in 1994, enacted a statute requiring federal financial institution regulators to provide an appeals process. Each of the four regulators (the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Reserve, and the National Credit Union Administration) adopted a unique material supervisory determination appeals process.

Using data (some collected through Freedom of Information Act requests) about material supervisory decision appeals since 1994 and interviews with top regulators, this Article provides the first in-depth analysis of the appeals processes. It shows that the appeals processes are sometimes dysfunctional and seldom used.

To improve the appeals processes, the Article recommends three changes. First, once a regulator issues a material supervisory determination, financial institutions should have direct access to a dedicated appellate authority outside of the examination function. Second, the appellate authority should engage in a robust review; it should consider a broad scope of appealable matters and employ a clear and rigorous standard of review. Third, regulators should release detailed information about each decision reached by the appellate authority.

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INTRODUCTION

Financial institutions[1] are among the most heavily regulated businesses in the United States. To ensure that institutions comply with the complex web of laws, regulators conduct regular examinations. During an on-site examination, regulators comb the institution's books, records, policies, and practices looking for evidence of legal infractions and financial stress. Examiners then make a number of "material supervisory determinations" ("MSDs") about the institution's financial health and

[1] As used in this article, the terms "financial institution" and "institution" refer to federally insured banks, credit unions, bank holding companies, and financial holding companies. In some circumstances, I distinguish between "banks" (which are insured by the Federal Deposit Insurance Corporation) and "credit unions" (which are insured by the National Credit Union Share Insurance Fund).

compliance with the law.[2] The examiners prepare an examination report detailing these findings. In between on-site examinations, regulators collect and review institutions' financial information looking for potential issues. This review can also lead to MSDs.

MSDs become the building blocks of regulatory enforcement. In cases where MSDs suggest a financial institution needs to improve, regulators employ formal or informal enforcement mechanisms to ensure that the institution corrects any problems. For example, a regulator might issue a cease-and-desist order instructing the institution to stop certain lending activities.[3] In more extreme cases, regulators might close the institution.[4] MSDs are often the initial findings that set the regulatory enforcement mechanism in motion.

In the aftermath of the September 2008 financial market meltdown, some financial institutions complain that regulators' are trending toward overly aggressive examination practices.[5] At its root, dissatisfaction with the examination process often indicates that institutions disagree with examiners about MSDs. Some institutions believe that regulators do not consistently apply existing law, claiming that "examiners tended to focus too much on their own view of best practices rather than on legal and regulatory requirements."[6] Institutions also complain that regulators change examination standards without warning. They claim that "[w]hat was once A-OK is no longer A-OK, but no one knows that until after the

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2 MSDs include "determinations relating to . . . (i) examination ratings; (ii) the adequacy of loan loss reserve provisions; and (iii) loan classifications on loans that are significant to an institution . . . ." 12 U.S.C. § 4806(f)(1)(A).

3 *Id*. §§ 1818(b), 1785-86.

4 *Id*. §§ 191, 1464(d), 1787.

5 *See, e.g.*, *The Financial Institutions Examination Fairness and Reform Act: Hearing on H.R. 3461 Before the Fin. Insts. & Consumer Credit Subcomm. of the H. Fin Servcs. Comm.*, 112th Cong. 164 (2012) [hereinafter *Hearing on H.R. 3461*] (written statement of Noah Wilcox, President and CEO, Grand Rapids State Bank) ("There is an unmistakable trend toward arbitrary, micromanaged, and unreasonably harsh examinations.").

6 *Hearing on H.R. 3461*, *supra* note 5, at 150 (statement of Ken Watts, President and CEO of the West Virginia Credit Union League).

examination."[7] Some reports even claim that examiners act with bias or malice.[8]

To guard against erroneous MSDs, financial institution regulators are statutorily required to provide an "independent intra-agency appellate process . . . to review material supervisory determinations made at insured depository institutions."[9] The Office of the Comptroller of the Currency ("OCC"), the Federal Deposit Insurance Corporation ("FDIC"), the Board of Governors of the Federal Reserve System ("Federal Reserve"), and the National Credit Union Administration ("NCUA") have each implemented a different procedure for handling these appeals.[10]

Since regulators implemented the MSD appeals processes in 1995, little has been done to analyze their effectiveness. Part of the reason for the lack of scrutiny is that regulators keep much of the information about appeals, including some decisions, secret. In addition, regulators themselves have failed to conduct any serious study of the appeals processes.[11] Using data from MSD appeals (some of which I collected through

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[7] Bryan McKenzie, *Small Banks Struggle with New Regulations*, THE DAILY PROGRESS (CHARLOTTESVILLE, VA), Sept. 4, 2010, *available at* 2010 WLNR 17668535 (quoting Patricia G. Satterfield, President and CEO of the Virginia Association of Community Banks). *See also* Steve Cocheo, *Tough Times on the Exam Front*, ABA BANKING J., Nov. 2009, at 6 ("Management that was brilliant two years ago running a CAMELS 1-rated bank now appears to be a bunch of idiots running a 4- or 5-rated bank.") (quoting banking attorney Jeffrey Gerrish).

[8] *See* George Waldon, *Bank's Tiff With OCC Takes a Twist*, ARK. BUS. & ECON. REV., Oct. 8, 2012, at 24 (reporting on an Arkansas bank's claim that it received a cease-and-desist order due to a "prejudicial bias [that] flowed from something akin to personal animosity"); Heather Anderson, *OIG Dismisses Ohio Exam Claims*, CREDIT UNION TIMES MAG., Oct. 17, 2012, at 1 (reporting on a credit union complaint that an examiner had introduced himself as "The Liquidator," harassed credit union staff, and retaliated when the credit union appealed the exam rating).

[9] 12 U.S.C. § 4806(a) (2012).

[10] *See* FDIC Intra-Agency Appeals Process, 77 Fed. Reg. 17,055 (2012); Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470 (1995); OCC Bulletin 2013-15 (June 7, 2013); NCUA Interpretive Ruling and Policy Statement 12-1, 77 Fed. Reg. 322,004-06 (2012).

[11] In 2012, the Inspector General of each federal financial institution regulator reviewed its agency's MSD appeals process. The reports generated from these reviews were far from scrutinizing. After recounting the appeals process, the reports all noted that few institutions chose to appeal. None of the reports offered extensive suggestions for improvement or compared the effectiveness of the appeals processes across regulators. *See* BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM OFFICE OF INSPECTOR GENERAL, AUDIT OF THE SMALL COMMUNITY BANK EXAMINATION PROCESS (Aug. 2012), *available at* http://www.federalreserve.gov/oig/files/Audit_SCB_Exam_Process_August2012.pdf [hereinafter FEDERAL RESERVE OIG REPORT]; DEPARTMENT OF THE TREASURY OFFICE OF INSPECTOR GENERAL, SAFETY AND SOUNDNESS: REVIEW OF OCC COMMUNITY BANK EXAMINATION AND APPEALS PROCESSES, OIG-12-070 (Aug. 31, 2010) *available at* http://www.treasury.gov/about/organizational-structure/ig/Audit%20Reports%20and%20Testimonies/OIG12070.pdf [hereinafter OCC OIG

Freedom of Information Act ("FOIA") requests) and my interviews with top-level regulators,[12] this Article provides the previously untold story of these appeals.

The story is that of a dysfunctional and seldom used system. Regulators vary significantly in the reviews they provide through the MSD appeals processes. They do not agree on which examiner determinations are appealable or on the applicable standard of review. Even considering the state of the regulators' appeals policies, the rate of appeals is astonishingly low. Thousands of financial institutions have been examined every year since regulators adopted their appeals processes in 1995. Yet the OCC Ombudsman has issued only 157 decisions, the Federal Reserve has decided just 25 appeals (although data from 1995-2000 are unavailable for the Federal Reserve), the FDIC's Supervision Appeals Review Committee has issued only 63 decisions, and the NCUA's Supervisory Review Committee has issued 6 decisions.[13] When institutions do appeal, they seldom win. Most shockingly, the NCUA's Supervisory Review Committee has overturned only one MSD – the denial of a $5,000 grant reimbursement from the Office of Small Credit Union Initiatives.[14]

In light of the limited usefulness of the current MSD appeals processes, I recommend three changes. First, all financial institution regulators should adopt a consistent and broad scope of appealable matters. All examination ratings should be appealable. Moreover, institutions should be able to appeal MSDs that underlie enforcement actions if the financial institution consented to the enforcement action. Second, all financial in-

REPORT]; FDIC OFFICE OF INSPECTOR GENERAL, THE FDIC EXAMINATION PROCESS FOR SMALL COMMUNITY BANKS, AUDIT REP. 12-011 (Aug. 2012), *available at* http://www.fdicoig.gov/reports12/12-011AUD.pdf [hereinafter FDIC OIG REPORT]; NCUA OFFICE OF INSPECTOR GENERAL, REVIEW OF NCUA'S EXAMINATION AND COMPLAINT PROCESSES FOR SMALL CREDIT UNIONS, REPORT NO. OIG-12-10 (Aug. 31, 2012), *available at* http://www.ncua.gov/about/Leadership/CO/OIG/Documents/OIG-12-10ReviewExamProcess.pdf [hereinafter NCUA OIG REPORT].

12 Interview with Samuel P. Golden, Managing Director, Alvarez & Marsal, former Ombudsman, Office of the Comptroller of the Currency, in Houston, Tex. (Nov. 9, 2012) [hereinafter Golden Interview]; Telephone Interview with Larry L. Hattix, Senior Deputy Comptroller for Enterprise Governance and Ombudsman, Office of the Comptroller of the Currency (June 14. 2013) [hereinafter Hattix Interview]; Telephone Interview with Joy K. Lee, Supervisory Review Committee Chair & Ombudsman, National Credit Union Administration (Apr. 4, 2012) [hereinafter Lee Interview]; Telephone Interview with Hattie M. Ulan, Senior Ethics Counsel, former member Supervisory Review Committee, National Credit Union Administration (June 18, 2013) [hereinafter Ulan Interview].

13 The MSD appeals data in this article end in 2012.

14 *See infra* text accompany notes 332-334.

stitution regulators should adopt a consistent and robust standard of review for evaluating appeals of MSDs. I favor a *de novo* standard of review. Third, all financial institution regulators should release decisions from appeals of MSDs. Although the decisions should be redacted sufficiently to protect the anonymity of the appealing financial institution and its customers, the released information should be complete enough to allow institutions, regulators, and the public to learn how the agency reads and applies relevant statutes and regulations. Although the reforms I propose do not go as far as proposals that would create a single super-Ombudsman to hear appeals from all financial institutions,[15] my reforms target observable weaknesses in the current processes.

This Article proceeds in four parts. Part I provides a brief overview of financial institution examinations. It then describes the creation of the MSD appeals processes. Part II provides a description of the MSD appeals process as implemented by each federal regulator. It details not only the appeals processes, but also institutions' usage of the processes. Part III discusses shortcomings of the current appeals processes, and Part IV discusses recommendations for improvement.

I. REGULATORY STRUCTURE

Financial institutions are subject to a detailed and complex regulatory structure. Reams of safety and soundness laws aim to keep institutions solvent, while additional regulations seek to ensure that institutions deal fairly with consumers. Regulators ensure that institutions comply with laws by employing examination and enforcement powers.

This section describes the financial institution examination and enforcement system. It explains the role of MSDs in this system. It then describes the statutory requirement for financial institution regulators to provide an "independent intra-agency appellate process"[16] to review MSDs.

A. Examination and Enforcement

Examinations are the cornerstone of a regulatory system designed to keep financial institutions safe and sound. Regulators typically conduct a yearly "full-scope, on site examination" at each financial institution.[17] During an examination, regulators visit a financial institution to

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15 *See infra* Part IV.D.

16 12 U.S.C. § 4806(a) (2012).

17 12 U.S.C. § 1820(d). There are a few exceptions to this general rule. State chartered banks may be examined by their federal regulator every other year if the state regulator conducts an

review the institution's policies, procedures, and records. Examiners then rate the institution using the Uniform Financial Institutions Rating System.[18] Under the System, regulators evaluate the safety and soundness of institutions using the "CAMEL" or "CAMELS" factors: capital, assets, management, earnings, liquidity, and susceptibility to market risk.[19] Regulators rate each item on a 1 to 5 scale, with a 1 rating being the highest possible score. Examiners also award each institution a composite rating meant to assess the overall condition of the institution. The composite score is not simply an average of the component ratings. Rather, in issuing a composite rating the regulator considers the components and "may incorporate any factor that bears significantly on the [institution's] overall condition."[20]

To arrive at the component rating and overall ratings, examiners must make a number of additional conclusions about the institution. For example, examiners will review loan documentation to determine whether the institution has appropriately classified the institution's risky loans and whether the institution has adequately reserved for those loans. If the examiners find a large amount of adversely classified loans when compared with the institution's overall loan portfolio, the examiners may rate the institution's assets as a 3, 4, or 5. The examiners might also downgrade the institution's management rating and composite rating based on the troubled loans.

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adequate examination during the year that the federal regulator does not. *Id*. § 1820(d)(2). In addition, regulators may examine certain small, healthy, and well-managed banks on an 18-month cycle. *Id*. § 1820(d)(4). Federal regulators examine federally chartered credit unions on a 12-month cycle. *See Examining the Health of the Credit Union Industry as We Emerge from the Financial Crisis and Recover and Grow Our Economy: Hearing Before the S. Comm. on Banking, Hous., & Urban Affairs*, 111th Cong. 6, 8, 25 (2010) (statement of Deborah Matz, Chairman, NCUA). However, for federally-insured state-chartered credit unions, the federal regulator "[t]o the maximum extent feasible, . . . utilize[s] examinations conducted by state regulatory agencies." 12 C.F.R. § 741.1 (2012). The federal credit union regulator schedules examinations of state-chartered credit unions "based on risk factors of individual credit unions." NCUA, EXAMINER' GUIDE 26.4 (2013), *available at* http://www.ncua.gov/Legal/GuidesEtc/Pages/Examiners-Guide.aspx. State credit unions that are large, have received a previous poor examination rating, or pose other unique risks are more likely to received a federal examination. *Id.*

18 Federal Financial Institutions Examination Council, Uniform Financial Institutions Rating System, 61 Fed. Reg. 67,021 (Dec. 19, 1996).

19 *Id*. "Federally insured credit unions are evaluated using the 'CAMEL' rating system, which is substantially similar to the 'CAMELS' system without the 'S' component for rating Sensitivity to market risk." OCC, FDIC, OTS, NCUA, Interagency Policy Statement on Funding and Liquidity Risk Management, 75 Fed. Reg. 13,656, 13,665 n.19 (Mar. 22, 2010).

20 Federal Financial Institutions Examination Council, Uniform Financial Institutions Rating System, 61 Fed. Reg. 67,021.

Although regulators do not publicly release safety and soundness examination ratings,[21] the ratings are serious business for financial institutions. Institutions that receive a 3, 4, or 5 rating have at least "some degree of supervisory concern."[22] Regulators commonly pursue formal enforcement actions, such as written agreements, consent orders, cease-and-desist orders, capital directives, and prompt corrective action directives against institutions with these less-than-satisfactory ratings.[23] Formal enforcement actions can require an institution to undertake costly remedial measures.[24] The CAMELS ratings are also used to determine the price banks pay for deposit insurance.[25] As a result of a poor composite examination rating, regulators may choose to downgrade an institution's capital classification.[26] This can, among other things, prevent a bank from accepting brokered deposits[27] and restrict an institution's ability to grow.[28] Finally, institutions that receive poor examination ratings may face restrictions on the appointment of senior executive officers and directors.[29]

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[21] *See* RICHARD SCOTT CARNELL, JONATHAN R. MACEY, & GEOFFREY P. MILLER, THE LAW OF FINANCIAL INSTITUTIONS 442 (5th ed. 2013).

[22] Federal Financial Institutions Examination Council, Uniform Financial Institutions Rating System, 61 Fed. Reg. 67,021 (Dec. 19, 1996).

[23] *See* Jim Rives, *A Perspective on Regulatory Risk: Enforcement Actions and CAMELS*, RMA J., Mar. 1, 2011, at 20. *See also*12 U.S.C. § 1818(b)(8) (authorizing formal enforcement actions); Julie Andersen Hill, *Bank Capital Regulation by Enforcement: An Empirical Study*, 87 IND. L.J. 645, 658-62 (2012) (providing a more fulsome description of enforcement actions).

[24] *See What An Enforcement Order Will Cost Your Bank*, BANK SAFETY & SOUNDNESS ADVISOR, Nov. 22, 2010, at 1. Such an action can cost a "$100 million community bank . . . between $750,000 and $1 million in additional expenses, including hiring outside consultants, regulatory counsel and increased FDIC insurance premiums." *Id*. For larger institutions, enforcement actions are probably even more costly. *Id*. (noting that a $348.6 million community bank spent between $1 million and $2 million on a cease-and-desist order).

[25] FDIC, Financial Institution Letter, FIL-8-2011 (Feb. 9, 2011). Credit unions, however, pay share insurance premiums that are based on the institution's number of insured shares outstanding without regard to the CAMEL rating. 12 U.S.C. § 1781(c)(2).

[26] *See* 12 U.S.C. § 1831o(g) (2012); 12 C.F.R. § 325.103(d) (FDIC); 12 U.S.C. § 208.43(c) (Federal Reserve); 12 C.F.R. § 702.102(b) (NCUA); 12 C.F.R. § 6.4(d) (OCC).

[27] *See* 12 U.S.C. § 1831f(a); 12 C.F.R. § 337.6(b)(3)(i). Credit unions tend to "rely less on brokered sources of funds than banks." Letter from Dennis Dollar, Acting Chairman, NCUA to Federally Insured Credit Unions (July 2001), *available at* http://www.ncua.gov/Resources/Documents/LCU2001-08.pdf. Thus, credit union regulations do not contain similar restrictions on brokered share accounts.

[28] *See id*. § 1831o(e)(3)-(4); 12 C.F.R. § 702.202(a)(3)-(4).

[29] *See, e.g.*, 12 C.F.R. § 5.51 (requiring that a bank that is not adequately capitalized provide 90 days notice to the OCC before making changes to the board of directors or senior manage-

In addition to the basic safety and soundness examination, regulators conduct specialized examinations to assess trust department operations,[30] information technology controls,[31] compliance with consumer protection laws,[32] performance under the Community Reinvestment Act,[33] and compliance with Bank Secrecy Act and other anti-money laundering laws.[34] Like the safety and soundness examination, the specialized examinations involve regulators making MSDs. Adverse findings can lead to enforcement actions or other negative consequences for the institution.[35]

In the event that a regulator issues an erroneous MSD, it is important for the receiving institution to get that determination corrected quickly. As regulators ramp up their enforcement efforts to correct a perceived problem, an institution may have little opportunity for redress. Regulators can issue some enforcement actions, such as capital directives

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ment); 12 C.F.R. § 701.14 (requiring that a federally-insured credit union that receives a 4 or 5 composite rating provide 30 days notice before makings changes to the board of directors or senior management). Banks may also face restrictions on golden parachutes—payments made to employees as a condition of terminating their employment. *See* 12 C.F.R. §§ 359.0-.7.

30 *See generally* Federal Reserve, Commercial Bank Examination Manual §§ 4200.1, 6010.1 (Oct. 2012); FDIC, Trust Examination Manual (2005); OCC, Bank Supervision Process: Comptroller's Handbook 12, 72-89 (Sept. 2012). The NCUA does not use the Uniform Interagency Trust Rating System. *See* Uniform Interagency Trust Rating Systems, 65 Fed. Reg. 54,704 (Oct. 13, 1998).

31 *See generally* FIFIEC, IT Examination HandBook InfoBase, http://ithandbook.ffiec.gov/it-booklets.aspx (last visited Feb. 11, 2013).

32 In a compliance examination, regulators visit the institution to assess conformity with fair lending laws, consumer disclosure laws, unfair or abusive practice laws, and privacy laws. *See generally* FEDERAL RESERVE, CONSUMER COMPLIANCE HANDBOOK (June 2012); FDIC COMPLIANCE EXAMINATION MANUAL (2012); NCUA, EXAMINERS GUIDE 19-1 to 19T-16 (June 2002); OCC, BANK SUPERVISION PROCESS: COMPTROLLER'S HANDBOOK 12, 90-93 (Sept. 2012).

33 *See generally* Federal Reserve, CONSUMER COMPLIANCE HANDBOOK, at CRA 1-99 (2012); FDIC Compliance Examination Manual XI-1.1 to XI-11.1 (2012); OCC, BANK SUPERVISION PROCESS: COMPTROLLER'S HANDBOOK 12, 94-105 (Sept. 2012). Credit unions are not included within the scope of the Community Reinvestment Act and are not subject to Community Reinvestment Act examinations. *See* 12 U.S.C. §§ 1813(c)(2), 2902-03.

34 In a Bank Secrecy Act / anti-money laundering examination, regulators assess an institution's compliance with laws designed to help law enforcement officials "identify the source, volume, and movement of currency and other monetary instruments." FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL, BANK SECRECY ACT/ANTI-MONEY LAUNDERING EXAMINATION MANUAL 7 (2010).

35 For example, although the Community Reinvestment Act does not generally allow regulators to bring enforcement actions against banks that do not adequately serve the credit needs of the community, the examiner's report is publicly released. *See* CARNELL, MACEY & MILLER, *supra* note 21, at 361. Thus, any adverse finding may damage the institution's reputation.

(actions that order an institution to improve its capital ratios), without providing the institution a pre-order hearing.[36] Even in circumstances where the law allows for a pre-order hearing, institutions often elect to forego the hearing on the theory that a hearing is of little use because regulators are granted broad discretion.[37] When institutions do go to the trouble of contesting an order at a hearing, appealing to an administrative law judge, and then appealing to a federal district court, courts' limited power to review these cases ensures that regulators almost always win.[38] The prospects are even grimmer for institutions that are closed by their regulators. If an institution waits until it is closed to raise regulatory concerns, it will likely be impossible to obtain adequate redress.[39]

In some administrative settings, elected officials, the media, and the court of public opinion serve as additional safety valves for regulated entities that are unhappy with the administrative process. Financial institutions, however, are constrained in their ability to raise institution-specific concerns with anyone other than their attorneys, accountants, and regulators. Examination reports remain the property of the regulator even after they have been issued to the bank.[40] The institution cannot disclose nonpublic examination information without risking administrative and criminal sanctions.[41]

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36 *See* FDIC v. Bank of Coushatta, 930 F.2d 1122, 1126 (5th Cir. 1991).

37 *See* Joseph T. Lynyak III, *Responding to Capital Directives and Related Enforcement Actions*, 129 BANKING L.J. 387, 390 (2012).

38 *See, e.g.*, Frontier State Bank v. FDIC, 702 F.3d 588, 597 (10th Cir. 2012) (holding that a regulator's decision to set an individual bank minimum capital requirement in a cease-and-desist order was not subject to judicial review because Congress granted complete discretion to bank regulators); Greene County Bank v. FDIC, 92 F.3d 633, 636 (8th Cir. 1996) (holding that a regulator's conclusion that a bank had not complied with a memorandum of understanding was supported by substantial evidence).

39 *Can You Sue to Reverse a Receivership*, BANK SAFETY & SOUNDNESS ADVISOR, Apr. 4. 2011, at 1 (explaining that regulators have broad power to close any financial institution with an "unsafe or unsound condition" and even if the regulator acts improperly the financial institution's assets will likely have been sold to others before the legal challenge concludes). *See also* Lynyak, *supra* note 37, at 397 ("Although there are instances in which the closing of a bank may be viewed by stakeholders as unfair or perhaps illegal, there are no modern instances in which a bank closing has been reversed or enjoined.").

40 *See* 12 C.F.R. §§ 4.32(b)(2), 4.36 (2012) (OCC); 12 C.F.R. §§ 309.5(g)(8), 309.6(a), 350.9 (FDIC); 12 C.F.R. §§ 261.2(c)(1), 261.20(g), 261.22(e) (Federal Reserve); 12 C.F.R. § 792.30 (NCUA).

41 *See* Interagency Advisory on the Confidentiality of Nonpublic Supervisory Information, SR 05-04 (Feb. 28, 2005), *available at* http://www.fdic.gov/news/news/press/2005/pr1805a.html#foot2 (citing the criminal penalties associated with 18 U.S.C. § 641); Appeal of CAMELS component ratings for asset quality, management,

For their part, regulators should also have an interest in correcting erroneous MSDs. Pursuing unnecessary enforcement actions diverts regulatory attention from pressing problems. If a financial institution expends significant time and effort addressing an erroneous determination, it may prevent the institution from addressing other important matters. Moreover, allowing erroneous MSDs to persist undermines the credibility of the supervisory process.

B. Appealing Material Supervisory Determinations

Although both regulators and financial institutions have an interest in correcting erroneous MSDs, regulators were slow to allow appeals. The OCC was the first. In 1993, Comptroller Eugene A. Ludwig created the Office of the Ombudsman to handle MSD appeals.[42] He appointed Samuel P. Golden, an OCC examiner, as the first Ombudsman.[43] At the time, financial institutions and their regulators were still trying to recover from the banking crises of the 1980s.[44] Some banks that had weathered the crises began to complain about the fairness of the bank examination process. They asked newly elected President Bill Clinton and Comptrol-

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liquidity, and sensitivity to market risk, SARC-99-07, http://www.fdic.gov/regulations/laws/sarc/sarcappeals/sarc9907.html (Dec. 10, 1999) (upholding an examiner determination that a bank had violated "Section 309.6 of FDIC Rules and Regulations, which prohibits disclosure of confidential supervisory information, without the prior approval of the FDIC" when the bank "copied individual members of Congress and the General Accounting Office on its appeal of" an examination rating); *On Deadline*, CREDIT UNION J., Apr. 2, 2012, at 1 (reporting that the NCUA had banned a credit union director from associating with any credit union because he publicly disclosed a credit union CAMEL rating).

42 Eugene A. Ludwig, *Column: After Dodd-Frank, More Ombudsmen*, AM. BANKER, Sept. 16, 2010, at 9. Technically, the FDIC announced an informal policy for reviewing supervisory decisions in early 1992, but the policy was short on details and only provided that the Division of Supervision Director would "make a good faith effort to evaluate and resolve" written complaints from banks. FDIC Financial Institution Letter 11-92 (Feb. 7, 1992) (Procedures for Requesting Review of Supervisory Decisions).

43 Stephen Goldstein, *Metropolitan Money Movers & Shakers*, WASH. TIMES (D.C.), Aug. 15, 2013, at B5.

44 *See generally*, FDIC, HISTORY OF THE BANKING CRISES OF THE 1980S AND EARLY 1990S (1997) (explaining that a collapse of energy prices, real estate downturns, and an agricultural recession all combined to stress the banking industry).

ler Ludwig for an independent avenue for appealing MSDs.[45] Comptroller Ludwig obliged.[46]

The OCC's new Ombudsman operated outside of the OCC's supervisory function, instead reporting directly to the Comptroller.[47] The appeals process itself looked like binding arbitration.[48] A bank would submit a written appeal describing what it believed was an erroneous determination. The Ombudsman would then contact the OCC examination staff for its written response and the relevant OCC documents.[49] In most cases, Ombudsman Golden or his staff[50] would visit the appealing bank to make an independent assessment.[51] The Ombudsman would then issue a new and binding decision—a decision that could be more severe or more lenient than the decision reached by the examination staff.[52]

According to Ombudsman Golden, his office was initially "inundated" with appeals.[53] Banks were complimentary of the new appeals process and sometimes even more complimentary of Ombudsman Golden. After a northern California bank successfully appealed a "needs to improve" rating under the Community Reinvestment Act, the bank's

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45 Golden Interview, *supra* note 12 ("On [President Clinton's] transition team . . . there were several key bankers from some of the largest banks in the country who said, 'You need something to provide an avenue that when we disagree with the bank examiners that you don't go to the fox in the henhouse . . . .'").

46 OCC Banking Circular No. 272 (June 11, 1993).

47 *Appeals Process*, 13 OCC QUARTERLY J. 61 (Mar. 1994); Steve Cocheo, *OCC's First Ombudsman Hangs Out His Shingle*, ABA BANKING J., Oct. 1993, at 6. The office was initially located in Houston, Texas in part to create an appearance of objectivity. Barbara A. Rehm, *Former Examiner Ready for Job as OCC's Complaint Department*, AM. BANKER, Sept. 9, 1993, at 18.

48 Golden Interview, *supra* note 12 ("[T]he [appeals] process is binding arbitration because you listen to both sides, you go through, and you make a *de novo* separate decision on what is the right outcome.").

49 OCC Banking Circular No. 272 (June 11, 1993). Ombudsman Golden explained: "There were no forms that were required; there was no infrastructure that was required. You simply frame[d] the issue that you [had]." Golden Interview, *supra* note 12.

50 The OCC Ombudsman's Office initially consisted of Ombudsman Golden and a single administrative assistant, but it hired three additional staff members in the first year. Rehm, *supra* note 47, at 18; Golden Interview, *supra* note 12.

51 OCC policy allowed both examination staff and bank management the opportunity to request a telephone or in-person meeting. *See* OCC Banking Circular No. 272 (June 11, 1993). Under the direction of Ombudsman Golden, staff from the Ombudsman's Office would almost always visit the bank. Golden Interview, *supra* note 12.

52 *Appeals Process*, 13 OCC QUARTERLY J. 61 (Mar. 1994).

53 Golden Interview, *supra* note 12. *See also* Bill Atkinson, *Bankers Not Shy About Appealing OCC Decisions*, AM. BANKER, Jan. 31, 1994, at 6.

chief executive officer effused: "(Mr. Golden) is probably the best thing to happen to the OCC in a long time . . . . He's bringing a discipline to the agency that is long overdue."[54]

Banks not regulated by the OCC took note and wanted other regulators to adopt a similar process.[55] Based in part on the initial success of the OCC appeals process,[56] Congress mandated that each banking regulator provide an "independent intra-agency appellate process . . . to review material supervisory determinations made at insured depository institutions."[57]

The appeals process must provide "a review by an agency official who does not directly or indirectly report to the agency official who made the material supervisory determination under review."[58] Regulators must also provide appropriate safeguards to protect financial institutions that appeal from retaliation by the regulator.[59]

Appealable MSDs are defined to include "examination ratings," "the adequacy of loan loss reserve provisions," and "loan classifications on loans that are significant to an institution."[60] However, MSDs do not

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[54] Terrence O'Hara, *To Feisty CEO, 'Needs to Improve' Meant War*, AM. BANKER, May 17, 1994, at 8 (quoting Carl J. Schmitt, CEO, University National Bank and Trust Co.).

[55] Golden Interview, *supra* note 12 ("[The FDIC and Federal Reserve] would not have independently [created an independent MSD appeals process] had it not been for state banks who said, 'Why do national banks have that and we don't?' So that's when Congress essentially mandated that they would do it.'"). It is not clear whether credit unions were equally interested in an appeals process. *See* Ulan Interview, *supra* note 12 (stating that she did not recall credit unions "clamoring for [an appeals] process").

[56] OCC REPORT OF THE OMBUDSMAN 1996-1995, at 3.

[57] Riegle Community Development and Regulatory Improvement Act of 1994, Pub. L. No. 103-324, § 309, 108 Stat. 2160, 2218-20 (codified at 12 U.S.C. § 4806(a)). The statute applies to "each appropriate Federal banking agency and the National Credit Union Administration Board." *Id*. "Federal banking agency" is currently defined to include only the OCC, Federal Reserve, and FDIC. *See* 12 U.S.C. §4801(1); 12 U.S.C. §1813(q). The newly created Consumer Financial Protection Bureau ("CFPB"), although generally thought of as an additional bank regulator, does not fall within the ambit of the statute. The CFPB has voluntarily established a supervisory appeals process, but notes that it is "is not intended to nor should it be construed to . . . create or confer upon any person, including one who is the subject of CFPB supervisory, investigation or enforcement activity, any substantive or procedural rights or defenses that are enforceable in any manner." CFPB Bulletin 2012-07, Appeals of Supervisory Matters (Oct. 31, 2012), *available at* http://www.consumerfinance.gov/f/201210_cfpb_bulletin_supervisory-appeals-process.pdf. There is no substantive reason that the CFPB should not be required by statute to provide an appeals process on par with other financial institution regulators.

[58] 12 U.S.C. § 4806(f)(2).

[59] *Id*. at § 4806(b)(2).

[60] 12 U.S.C. § 4806(f)(1)(A).

include regulators' decisions to close financial institutions or take prompt corrective action, including the removal of officers and directors, from undercapitalized institutions.[61] Furthermore, the MSD appeals process does not "affect the authority of an appropriate Federal banking agency or the National Credit Union Administration Board to take enforcement or supervisory action."[62]

Congress expected that the MSD appeals processes would "provide an avenue of redress for insured depository institutions . . . from uneven treatment by examiners."[63]

II. APPEALS PROCESSES BY REGULATOR

Each federal financial institution regulator has taken a different path for providing the intra-agency review process required by statute. This Part first provides a description of each regulator's MSD appeals process. It then describes how institutions have used the appeals processes.

This Part draws on information from my interviews of past and current regulators who handle (or handled) MSD appeals.[64] It also reports appeals data I gathered from public sources and through FOIA requests. While some information about MSD appeals is still not available, this Part provides the most comprehensive look at the MSD appeals processes to date.

A. OCC

The Office of the Comptroller of the Currency supervises banks and thrifts with national charters.[65] The OCC currently oversees 1,654

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61 *Id*. at § 4806(f)(1)(B).

62 *Id*. at § 4806(g).

63 S. REP. NO. 103-169, at 51 (1994), *reprinted in* 1994 U.S.C.C.A.N. 1881, 1935 (explaining that "[e]venhandedness is important to maintain confidence in our regulatory system").

64 I sought interviews with many past and current agency officials. The Federal Reserve has adopted a process that essentially creates an *ad hoc* review committee for each appeal. *See infra* notes 163-164 and accompanying text. Thus, it was impossible to identify an individual who could give a first-person account of the functioning of the appeals process as a whole. My attempts to secure interviews with FDIC officials were unsuccessful. I did, however, gather significant information from interviews of past and current OCC Ombudsmen and past and current members of the NCUA's Supervisory Review Committee. *See supra* note 12.

65 *About the OCC*, OCC, http://www.occ.treas.gov/aboutocc.htm. In 2011, the OCC gained regulatory authority over national thrifts when the Dodd-Frank Act shuttered the Office of Thrift Supervision. *See* 12 U.S.C. § 5411-12.

banks,[66] including all of the largest U.S. banks—Bank of America, Wells Fargo Bank, JP Morgan Chase, Citibank, U.S. Bank, PNC Bank and TD Bank.[67] Although the OCC is often thought of as the large bank regulator, it also supervises about 1,400 banks with less than $1 billion in assets.[68] The OCC has 3,823 full-time equivalent employees.[69]

1. OCC Appeals Process

As discussed in Part II.B, the OCC was the first federal bank regulator to establish an independent MSD appeals process. Because the Congressional mandate was based on the OCC's existing process,[70] the statute did not require changes at the OCC. Since 1994, the OCC has updated its procedures on four occasions, but the basic structure of the appeals process remains the same.[71]

Under current OCC guidelines,[72] banks are encouraged to first attempt to resolve any disagreement with examiners informally during the examination process.[73] If a bank is dissatisfied with informal attempts to resolve the disputed MSD, the bank may initiate a formal appeal with either the Ombudsman or the Deputy Comptroller of the supervisory dis-

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[66] *See Statistics on Depository Institutions*, FDIC, http://www2.fdic.gov/sdi/ (last visited Jan. 17, 2014).

[67] *See Summary of Deposits*, FDIC, http://www2.fdic.gov/sod/ (linking to Summary Tables, which provides a table for the Top 50 Commercial Banks and Savings Institutions by Deposits) (June 30, 2012 report).

[68] *See Statistics on Depository Institutions*, FDIC, http://www2.fdic.gov/sdi/ (last visited Jan. 17, 2014).

[69] OCC ANNUAL REPORT: FISCAL YEAR 2012, inside front cover.

[70] *See supra* notes 55-57 and accompanying text.

[71] The OCC revised the procedures in 1996, 2002, 2011, and 2013. *See* OCC Independent Regulatory Appeals Process, 61 Fed. Reg. 7042 (Feb. 23, 1996); OCC Bulletin 1996-18 (Feb. 23, 1996); OCC Bulletin 2002-9 (Feb. 25, 2002); OCC Bulletin 2011-44 (Nov. 1, 2011); OCC Bulletin 2013-15 (June 7, 2013).

[72] OCC Bulletin 2013-15 (June 7, 2013); OCC, APPEALS PROCESS FOR NATIONAL BANKS AND FEDERAL SAVINGS ASSOCIATIONS (Apr. 2012), *available at* http://www.occ.gov/topics/dispute-resolution/bank-appeals/bank-appeals-process-brochure.pdf [hereinafter OCC BANK APPEALS PROCESS BROCHURE]. In addition to these two documents, the OCC Policies and Procedures Manual (PPM) 1000-9 (Revised), Administering Appeals from National Banks (Feb. 2002) discusses appeals. However, a 2011 Office of Inspector General Report suggests that parts of the Policies and Procedures Manual are "outdated and not consistently followed or enforced." OCC OIG REPORT, *supra* note 11, at 11.

[73] OCC Bulletin 2013-15 (June 7, 2013).

trict that oversees the bank.[74] The choice of whether to file an appeal with the Ombudsman or Deputy Comptroller is left to the discretion of the appealing bank.[75] Although the Deputy Comptroller oversees the supervisory function that led to the initial MSD,[76] the Ombudsman "operates independently from the bank supervision process and reports directly to the Comptroller of the Currency."[77] Since the OCC established the MSD appeals process, it has had only two Ombudsmen: Samuel P. Golden (1993–2008) and Larry L. Hattix (2008–present).[78] The OCC Ombudsman's office currently has two other seasoned former examiners dedicated to the appeals function full-time.[79]

Whether the bank chooses to start its appeal with the Deputy Comptroller or the Ombudsman, it must submit a written document fully describing the matter in dispute.[80] The bank must also show that its board of directors has approved the appeal.[81] While some institutions choose to have outside attorneys prepare the appeals documentation, the OCC's process is designed to be simple enough that banks can pursue appeals without attorneys.[82]

If a bank appeals to the Deputy Comptroller, the Deputy Comptroller then "contacts the bank to discuss the appeals process and applicable supervisory standards related to the issue(s) in dispute, and to ensure that he or she has all the information needed to determine if the issue(s) in dispute are appealable."[83] The Deputy Comptroller also contacts OCC

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74 *Id*.

75 *Id*.

76 *See id*. ("A formal appeal to the Deputy Comptroller shall be filed with the Deputy Comptroller responsible for the unit that issued the decision or action in dispute.").

77 *Id*.

78 Press Release, OCC, The Office of the Comptroller of the Currency Names Larry Hattix to be Ombudsman (Feb. 8, 2008), *available at* http://www.occ.gov/news-issuances/news-releases/2008/nr-occ-2008-12.html. Before becoming Ombudsman both men had lengthy careers as OCC examiners. *Id*.

79 Hattix Interview, *supra* note 12. Three additional Ombudsman Office employees assist with the appeals function as needed. *Id*. The Ombudsman calls on other experts throughout the OCC to help with appeals on a case-by-case basis. *Id*.

80 OCC Bulletin 2013-15 (June 7, 2013). If an appeal is made to the Ombudsman, the bank must additionally "include the supervisory standards that the bank deems were inappropriately applied by OCC officials." *Id*.

81 *Id*.

82 Hattix Interview, *supra* note 12.

83 OCC Bulletin 2013-15 (June 7, 2013).

examination staff to get a "written response to the appeal."[84] If the Deputy Comptroller or his or her supervisor "participated in making the decision under review, he or she must transfer the appeal to the Ombudsman."[85] Under normal circumstance, the Deputy Comptroller will issue a written decision letter within 45 days.[86]

If the bank is unhappy with the Deputy Comptroller's decision or prefers to begin the appeal with an independent party,[87] the bank can appeal to the Ombudsman. Like the Deputy Comptroller, the Ombudsman must contact the bank to discuss the appeal and seek a response to the appeal from OCC examination staff.[88] In some cases, the Ombudsman or his staff visits the appealing bank.[89] Under normal circumstances, the Ombudsman will reach a decision within forty-five days of the filing of the appeal.[90]

Banks may use the MSD appeals process to challenge a wide variety of determinations. In addition to examination ratings, allowances for loan and lease losses, and loan classifications (all of which are appealable under the statute itself[91]), OCC guidance allows banks to appeal violations of law, fair-lending-related decisions, licensing decisions, and other "[m]aterial supervisory determinations such as matters requiring

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84 *Id*.

85 *Id*.

86 *Id*.

87 Because the Deputy Comptroller oversees the examination function, some banks may fear retaliation is more likely if the first appeal is filed with the Deputy Comptroller. The OCC's process allows these banks to bypass the Deputy Comptroller.

88 OCC Bulletin 2013-15 (June 7, 2013).

89 Hattix Interview, *supra* note 12 ("There have been . . . occasions when sometimes I will visit [the appealing bank] if I think that that's appropriate. There are times also when the banks have asked if they can come in, and we always allow that. . . . [B]ut it's not the majority. It's the minority."). In contrast Mr. Hattix's predecessor, Ombudsman Samuel P. Golden, reports that he or his staff nearly always visited appealing banks. He explains:

> Most of the time, if I want to know how you live, I'm going to go to your house. You can tell me about how you live, and then I go to your house and it is junky as hell. You know, seriously. If you want to know the real facts, you literally go. So ninety-five percent of the time we went to the bank.

Golden Interview, *supra* note 12.

90 Hattix Interview, *supra* note 12 ("[O]ur goal is to try and get things resolved within forty-five days. Right now we are probably averaging probably closer to sixty, and I think that that has to do with the types of cases that we are getting right now with the economy being what it is."). OCC Bulletin 2013-15 (June 7, 2013).

91 12 U.S.C. § 4806(f)(1)(A).

attention, compliance with enforcement actions, or other conclusions in the report of examination."[92] The OCC guidance specifically excludes some matters from review, including formal enforcement actions and "other agency decisions that are subject to judicial review other than those described in the" OCC guidance.[93] For the purposes of the guidance, "a formal enforcement-related action or decision includes the underlying facts that form the basis of a recommended or pending formal enforcement action and the acts or practices that are the subject of a pending formal enforcement action."[94] The guidance, however, leaves open the possibility of appeal for informal enforcement actions (like memoranda of understanding) and also allows room for banks to challenge examination ratings and other examination conclusions while under formal enforcement actions.[95]

Once a bank submits an appeal, the Deputy Comptroller or the Ombudsman has seven days to determine whether the appeal concerns an appealable matter.[96] Ombudsman Hattix urges all banks with examination complaints to bring them to the Ombudsman.[97] He believes the OCC's authority on appeal is often broader than banks believe.[98] In the event the matter is not considered an MSD, the Ombudsman may still be able to serve as an informal mediator between the bank and the OCC's examination staff.[99]

Generally, "material supervisory decisions and actions are not stayed during the pursuit of an appeal."[100] "In appropriate circumstances, however, the Ombudsman or appropriate OCC official, upon written re-

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92 OCC Bulletin 2013-15 (June 7, 2013).

93 *Id*. Additionally, banks may not appeal decisions to close a bank, preliminary conclusions that have not yet been finalized, formal and informal rulemaking, formal and informal adjudications under the Administrative Procedures Act, and FOIA decisions. *Id*.

94 *Id*.

95 *See* OCC Bulletin 2013-15 (June 7, 2013) ("While banks may not appeal a decision by the supervisory office to pursue a formal enforcement-related action, banks may appeal conclusions in the [report of examination]."); Hattix Interview, *supra* note 12 ("[I]f you're under an enforcement agreement and that's what you are appealing, the enforcement document itself, then we could probably say, 'Yeah, that's probably not going to be appealable.' But a lot of times, the underlying factors, you know, your rating, you can still appeal.").

96 *Id*.

97 Hattix Interview, *supra* note 12.

98 *Id.*

99 *Id*.

100 OCC Bulletin 2013-15 (June 7, 2013).

quest of the bank, may relieve the bank of the obligation to comply with a supervisory decision or actions while the supervisory appeal is pending."[101] Ombudsman Hattix explains that, although the Ombudsman's Office has issued stays, stays are generally only appropriate when the appealing bank would suffer irreparable harm by complying with the supervisory decision.[102]

OCC guidance does not provide a clear standard of review for the Ombudsman or Deputy Comptroller in deciding appeals. The guidance notes that when a bank appeals conclusions in a report of examination while subject to a formal enforcement action, "the appeal is limited to a consideration of whether the examiners appropriately applied agency policies and standards."[103] The guidance is otherwise silent about the standard of review.

Other OCC statements are ambiguous about standard of review for MSD appeals. An OCC brochure provided to bankers and examiners explains that the "Ombudsman provides an independent and objective review to determine if supervisory decisions are reasonable based on available facts."[104] It also notes that "[e]xaminers can be assured that fair, impartial review of appeals will support reasonable decisions based on available facts according to existing standards and guidance."[105] Perhaps this means the Deputy Comptroller and the Ombudsman decide only whether examiner decisions are within a range of reasonableness—something less than a full *de novo* review of the facts underlying the dispute and the determinations of the examination staff.

Former OCC Ombudsman Samuel P. Golden appears to have taken the position that because statutes, regulations, and guidelines did not explicitly narrow the standard of review, he was free to reconsider all findings of fact and conclusions of law. Ombudsman Golden explained that, in general, he employed a *de novo* standard of review.[106] He was free to

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101 *Id*.

102 Hattix Interview, *supra* note 12 (explaining that if an MSD had instructed a bank to reimburse customers for fair lending violations, a stay might be appropriate while the Ombudsman reviewed the violation).

103 OCC Bulletin 2013-15 (June 7, 2013).

104 OCC BANK APPEALS PROCESS BROCHURE, *supra* note 72.

105 *Id*.

106 Golden Interview, *supra* note 12 ("Most appeals *were de novo*, which means this: If you appeal it, what you are asking for is a reassessment of the facts and circumstances and a decision that you believe is fair and balanced. And so what I had was the opportunity to go back and not be bound by the decision that the exam team had made. And that 'not being bound by' means that I could

make a new determination—including a determination that is harsher than the one reached in the initial examination. On most occasions, Mr. Golden and his staff would visit the bank to make their own assessment of underlying facts.[107]

Current Ombudsman Larry L. Hattix, does not use the phrase *de novo* when describing the MSD standard of review. Instead, he describes his decisions as "standard based."[108] For example, if a bank was appealing a loan classification, he would ask both the bank and the examination staff to explain how the loan complies with the OCC's standards for classifying loans. The Ombudsman would then "look at the standards and say, 'Was it applied appropriately or not?'"[109] Under this approach Mr. Hattix explains that he is "not giving deference to either side."[110] On the one hand Mr. Hattix's review seems the equivalent of a *de novo* standard: the Ombudsman looks at the facts and makes his own determination about the how those facts comport with OCC regulations and policies, rather than relying on the initial factfinder's (the examiner's) conclusions of law. On the other hand, this description makes no mention of how the Ombudsman might resolve questions of fact. Without a visit to the bank, the Ombudsman may have little way of resolving questions of fact without giving deference to earlier factfinders. Perhaps cases involving questions of fact are rare instances that are resolved *de novo* by the Ombudsman by visiting the bank. However, Ombudsman Golden often visited banks, but Ombudsman Hattix rarely does so.[111] Perhaps the fewer visits suggest that Ombudsman Hattix uses a different standard than Ombudsman Golden did when reviewing factual disputes.[112]

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change it in any way that we believe that our analysis, the facts and circumstances were that led to the decisions.").

[107] *Id*. While Ombudsman Golden reviewed most appeals *de novo*, he used a more limited standard of review for appeals involving banks with formal enforcement actions. *Id*. In those cases, the Ombudsman had to "take the same facts and circumstances that the exam team had," and then determine whether the examiners' decisions "were consistent with the examination guidelines." *Id*. The OCC's review of findings related to enforcement action is more limited now. OCC Bulletin 2013-15 (June 7, 2013); *Hearing on H.R. 3461*, *supra* note 5, at 53 (testimony of Eugene A. Ludwig, Founder & CEO, Promontory Financial Group, LLC).

[108] Hattix Interview, *supra* note 12.

[109] *Id*.

[110] *Id*.

[111] *See supra* note 89.

[112] The OCC guidance does not provide distinctions between a Deputy Comptroller appeal and an Ombudsman appeal that suggest these officials might employ a different standard of review.

Regardless of the standard of review, once the Ombudsman has reached a decision, he issues a written response to both the bank and the examination staff.[113] The Ombudsman also publishes summaries of each decision.[114] This disclosure is meant to "provide transparency and openness in [the OCC's] decision-making process,"[115] while still maintaining the confidentiality of the appealing bank and its customers.[116]

The OCC appeals guidelines include a process designed to discourage examiner retaliation. After an appeal, the Ombudsman must contact the bank twice to ask whether retaliation has occurred.[117] If a bank reports retaliation, the Ombudsman investigates.[118] "If the Ombudsman finds that retaliation has occurred, he or she will forward the complaint directly to the Inspector General."[119] Ombudsman Hattix reported that, on a few occasions, he has forwarded complaints to the Inspector General for further investigation.[120] The OCC guidance warns that "[a]ppropriate action, including disciplinary action consistent with OCC policies, will be taken as warranted."[121] The Ombudsman also has authority to "recommend to the Comptroller that the next examination of the bank exclude personnel involved in the ruling appealed by that bank."[122]

See OCC Bulletin 2013-15 (June 7, 2013). However, because I did not interview any Deputy Comptrollers, it is hard to know whether they approach appeals like the Ombudsmen.

113 OCC Bulletin 2013-15 (June 7, 2013).

114 *See infra* notes 127-116 and accompanying text.

115 *See* Rachel Witkowski, *OCC's Ombudsman Opposed Appeal Reform Bill*, AM. BANKER, Apr. 19, 2012, *available at* 2012 WLNR 8174226 (quoting OCC Ombudsman Larry Hattix).

116 Golden Interview, *supra* note 12 (noting that, while it was usually possible to preserve confidentiality while still having meaningful disclosure, occasionally "the summaries had to be neutered to the point where it was difficult to" fully describe the appeal).

117 OCC Bulletin 2013-15 (June 7, 2013) ("The Ombudsman will contact bank management (1) 60 days after the date of the decision letter and (2) 60 days after the completion of the first examination of the appellant bank following its appeal"). Banks may also contact the Ombudsman about retaliation at their convenience. *Id.*

118 *Id*.

119 *Id*.

120 Hattix Interview, *supra* note 12.

121 OCC Bulletin 2013-15 (June 7, 2013). Ombudsman Hattix explains that disciplinary action might be taken by either the Inspector General or the Ombudsman. Hattix Interview, *supra* note 12.

122 OCC Bulletin 2013-15 (June 7, 2013) (noting that "[t]he Comptroller will make the final decision on any such exclusion").

2. OCC Appeals

Banks supervised by the OCC may file an initial appeal with either the Ombudsman or the Deputy Comptroller of the supervisory district that oversees the bank.[123] The OCC does not provide any public information about Deputy Comptroller appeals. Through FOIA, I requested information on Deputy Comptroller appeals since January 1, 1993. In response, I received a list summarizing 11 appeals.[124] Of those appeals, 4 involved examination findings, and 3 involved composite and component ratings. There was 1 appeal each for a licensing decision, a supervisory letter, a Community Reinvestment Act rating, and a loan classification. Of the 11 appeals, 6 upheld the examiner decision, 2 reversed the examiner decision, 2 partially reversed the examiner decision, and 1 appeal was withdrawn. Only 3 Deputy Comptroller decisions were appealed to the Ombudsman.

These FOIA data appear incomplete. The earliest decision included in the list of Deputy Comptroller appeals is dated 2002.[125] It is unlikely there were no appeals prior to 2002. Indeed, 3 Ombudsman opinions in 1994 and 1 in 2000 indicate that they were appeals from Deputy Comptroller decisions. Data for later appeals may also be incomplete.[126]

Information about bank appeals filed directly with the Ombudsman is more plentiful and reliable. As previously mentioned, the OCC publishes summaries of each Ombudsman opinion.[127] Initially the OCC pub-

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[123] *See supra* notes 72-77 and accompanying text.

[124] Letter from Frank D. Vance, Jr., Manager, Disclosure Service & FOIA Officer, OCC to author (Feb. 28, 2014) (on file with author).

[125] The letter accompanying the appeals list explains: "Our Deputy Comptroller Offices were unable to locate any documents showing evidence of any appeals at their level prior to June 2002." *Id*. In response to a prior FOIA request for the same documents, the OCC advised that "some underlying documents from the 1990s would have been destroyed through our normal destruction schedules." Letter from Frank D. Vance, Jr., Manager, Disclosure Service & FOIA Officer, OCC to author (Aug. 21, 2013) (on file with author).

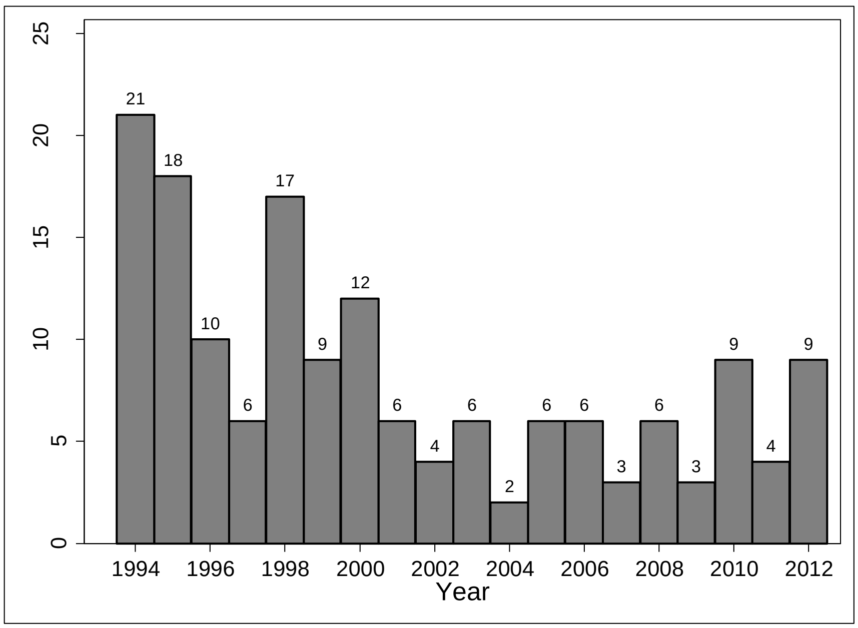
[126] Current OCC Ombudsman Larry Hattix estimates that 20 percent of appeals originate with a Deputy Comptroller. Hattix Interview, *supra* note 12. There were 58 Ombudsman appeals between 2002 and 2012. *See infra* Figure 1. The 11 Deputy Comptroller appeals would be less than 20 percent of the total number of appeals during that time.

[127] *See supra* note 114 and accompanying text.

lished the summaries in quarterly journals and annual reports.[128] With the advent of the Internet, the OCC now posts summaries on its webpage.[129]

According to these sources,[130] the OCC's Ombudsman decided 157 appeals between 1994 and 2012. On average this would amount to about 9 appeals per year, but the number of appeals per year was not constant during this time period.

Figure 1: OCC Material Supervisory Determinations Ombudsman Appeals per Year (1994-2012)



As Figure 1 shows, there were many more appeals during the early years of the OCC's Ombudsman's Office. Economic conditions[131] may partly explain the generally larger number of appeals in the 1990s. These

[128] *See, e.g.*, Appeals Process, 13 No. 1 Q.J. 61, 61-66 (1993-1994); OCC REPORT OF THE OMBUDSMAN 1996-1995, at 23-184.

[129] *See* OCC, Bank Appeals Summaries, http://www.occ.gov/topics/dispute-resolution/bank-appeals/summaries/index-summaries.html (last visited Jan. 17, 2014). Due to the workload in the Ombudsman's Office, it currently takes about 90 to 120 days after the decision for the summary to appear on the Internet. Hattix Interview, *supra* note 12.

[130] The printed and Internet sources contained minor discrepancies. When sources conflicted, I relied on the printed source.

[131] *See supra* note 44 and accompanying text.

early appeals may also evidence pent-up demand for an appeals process. They may also reflect the Ombudsman Golden's efforts to market the new appeals process.[132]

Appeals then fell to an historic low of 2 in 2004, before increasing some in recent years. The recent uptick in appeals corresponds with the financial crisis that began in 2008. Economic downturns may lead to more appeals either because financial conditions result in harsher MSDs or because regulators increase their scrutiny or both. The overall decline in appeals over the life of the appeals process could be partly explained by the significant consolidation in banking between 1994 and 2012. The OCC regulated 3602 banks in 1993. By the end of 2012, that number had dropped to 1783.[133] Whatever the reason, there are fewer appeals now than in the 1990s.

Because the summary decisions were crafted to protect the identity of the appealing bank and its customers, little information is available about which banks utilize the appeals process. Many of the appeals give no indication as to the size or type of bank appealing. Others provide general information: 29 described the appealing bank as "small" or as a "community bank"; 10 described the appealing bank as "large"; and 4 described the appealing bank as a "limited-purpose" bank. Ombudsman Hattix estimates that "maybe two-thirds of the appeals are [brought by] community banks."[134] A report prepared by the Department of the Treasury Office of Inspector General stated that "community banks filed 22 formal appeals from 2007 to 2011."[135]

The MSDs at issue vary widely from appeal to appeal. Figure 2 summarizes the issues that generated at least 5 Ombudsman appeals. Many appeals involved more than one issue. Of the 47 appeals involving the CAMELS ratings, the composite rating was most often appealed (37 times). The management rating followed closely (32 times). Capital (22), assets (21), earnings (19), liquidity (14), and sensitivity to market risk (11) ratings were appealed less often. Again, it was common for a single appeal to challenge more than one rating. Because the composite and

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[132] Ombudsman Golden explained: "I traveled, the first year, over 200,000 miles making sure that everyone understood—that no one was fearful of [the appeals] process . . . ." He credited the early number of appeals with this communication strategy. Golden Interview, *supra* note 12.

[133] *See Statistics on Depository Institutions*, FDIC, http://www2.fdic.gov/sdi/ (last visited Jan. 17, 2014).

[134] Hattix Interview, *supra* note 12.

[135] OCC OIG REPORT, *supra* note 11, at 11 (this number includes appeals filed with both the Ombudsman and the appropriate Deputy Comptroller).

management ratings are often identified as the more subjective of the CAMELS ratings, [136] it is not surprising that they were appealed more often.

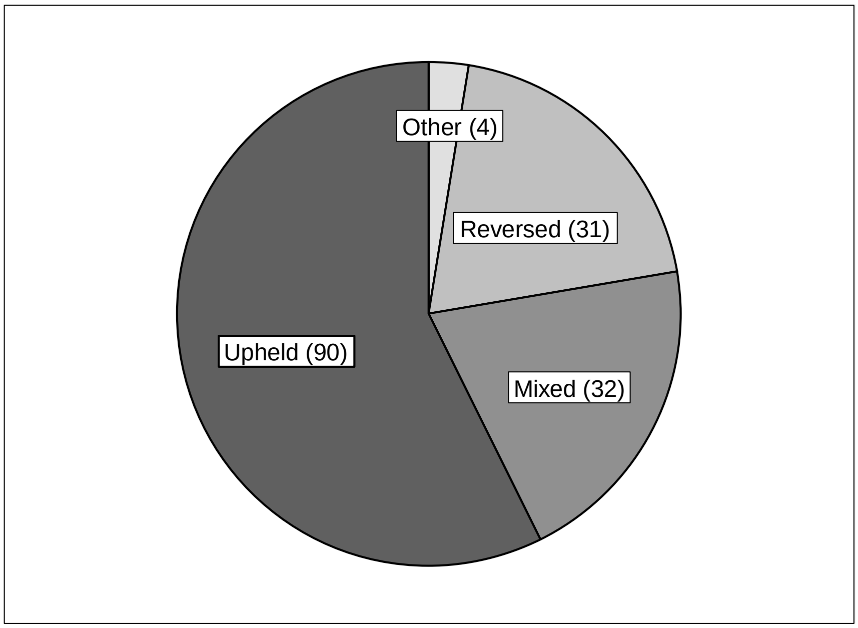
Figure 2: OCC Material Supervisory Determinations Appealed to Ombudsman (1994-2012)

Reason for Appeal	**Number**
CAMELS Composite or Component Ratings	47
Loan or Asset Classifications	27
Community Reinvestment Act Exam Ratings or Conclusions	24
Issues Related to a Formal or Informal Enforcement Actions	17
Accounting Issues	15
Unprofessional, Abusive, or Retaliatory Examiner Conduct	13
Allowance for Loan and Lease Losses	10
Insider Lending / Regulation O	10
Consumer Compliance Exam Ratings or Conclusions	9
Designation of the Bank as "Troubled"	8
Lending Limit Rules	8
Determination that Bank Must Amend Its Call Report	6
Truth in Lending Act / Regulation Z	6

Not all of the appeals seeking a change in a CAMELS rating disclosed the rating the bank had received, but many did. A three-rating was the most likely to prompt an appeal. Seventy-nine of the CAMELS composite or component ratings appealed were three-ratings. In comparison, 12 two-ratings were appealed, 32 four-ratings were appealed, and 17 five-ratings were appealed.

[136] *See, e.g.*, Joe Adler, *Why Camels Aren't as Secret as You Think*, AM. BANKER, Aug. 15, 2011, at 1 ("[M]ost agree it is impossible to replicate the official ratings exactly, since the regulators likely include highly subjective information about individual institutions in determining a Camels score. One crucial element of the rating system is the quality of a bank's management, which is not necessarily quantifiable."); Kathryn Reed Edge, *Anatomy of a Bank Failure*, 48-Apr. TENN. B.J. 25 (2012) ("The composite is not an average of the other ratings and is sometimes highly subjective.").

Figure 3: Outcomes of OCC Material Supervisory Determination Appeals to Ombudsman (1994-2012)



Banks seldom win appeals. The Ombudsman has upheld 57 percent (90/157) of the examiner decisions. In contrast, the appealing bank was the clear winner in only 20 percent (31/157) of the appeals. Although the success rate of appeals has fluctuated from year to year, the generally low number of appeals makes it impossible to glean any meaningful trends from the yearly data.

B. Federal Reserve

The Federal Reserve System is probably best known as the central bank of the United States.[137] However, the Board of Governors of the Federal Reserve System, along with twelve regional Federal Reserve Banks (collectively the "Federal Reserve"), supervises and examines banks that are members of the Federal Reserve.[138] A bank becomes a member of the Federal Reserve by application and by purchasing stock

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137 *See* BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 99TH ANNUAL REPORT 1 (2012).

138 *See id.*

in the Federal Reserve Bank in its district.[139] While all nationally chartered banks must be members of the Federal Reserve,[140] the OCC is primarily responsible for supervising and examining those banks.[141] Thus, the Federal Reserve focuses its supervisory attention on state-chartered banks that have chosen to become members of the Federal Reserve.[142] There are currently 852 state-chartered member banks.[143] The Federal Reserve coordinates examinations of these institutions with state banking regulators.[144]

The Federal Reserve also has supervisory authority over bank holding companies and savings and loan holding companies.[145] There are currently 5,088 bank holding companies and 689 savings and loan holding companies.[146] While some of these holding companies are massive and complex,[147] many are small and engage in little business other than owning financial institution stock.[148] For this reason, the Federal Reserve does not conduct on-site inspections of all holding companies annually.[149] In 2012 the Federal Reserve conducted 200 on-site inspections of

[139] 12 U.S.C. §§ 222, 321.

[140] 12 U.S.C. § 222.

[141] *See supra* Part II.A.

[142] *See* 12 U.S.C. § 325; BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 99TH ANNUAL REPORT 51-52 (2012).

[143] *See Statistics on Depository Institutions*, FDIC, http://www2.fdic.gov/sdi/ (last visited Jan. 17, 2014).

[144] BOARD OF GOVERNORS OF THE FEDERAL RESERVE, COMMERCIAL BANK EXAMINATION MANUAL § 1000.1 (2012) ("Under the alternate-year examination program, those banks that qualify are examined in alternate examination cycles by the Reserve Bank and the state.").

[145] 12 U.S.C. §§ 1844, 1467a. "The Federal Reserve also has responsibility for supervising the operations of all Edge Act and agreement corporations, the international operations of state member banks and U.S.[bank holding companies], and the U.S. operations of foreign banking organizations." BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 99TH ANNUAL REPORT 51 (2012).

[146] BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 99TH ANNUAL REPORT 51 (2012).

[147] For example, the four largest bank holding companies each have total assets exceeding $1 billion. Federal Reserve System, National Information Center, Top 50 HCs, http://www.ffiec.gov/nicpubweb/nicweb/Top50Form.aspx (last visited Jan. 17, 2014).

[148] *See* BOARD OF GOVERNORS OF THE FEDERAL RESERVE, COMMERCIAL BANK EXAMINATION MANUAL § 2060.2 (2012) (noting the existence of "small shell" holding companies that do not have "formal written budgets or [financial] plans").

[149] *See* Federal Reserve, Supervision and Regulation Letter 02-1 (Jan. 9, 2002), *available at* http://www.federalreserve.gov/boarddocs/srletters/2002/sr0201.htm (Revisions to Bank Holding

bank holding companies with less than $1 billion in assets and repeatedly inspected the largest bank holding companies.[150]

In 2011, there were 3,686 Federal Reserve employees whose responsibilities focused on supervision and regulation of financial institutions, and the Federal Reserve expected these ranks to increase.[151]

1. Federal Reserve Appeals Process

Following Congress's passage of the Riegle Community Development and Regulatory Improvement Act of 1994, the Federal Reserve Board issued guidelines for appealing MSDs.[152] These Board guidelines are still in effect today and are broad enough to allow appeals by not only state-chartered member banks, but also bank holding companies and other entities that are subject to the Federal Reserve's examination or inspection authority.[153] By having agency-wide guidelines, the Federal Reserve Board sought to ensure that all institutions receive "the same appellate rights regardless of the Federal Reserve district in which they reside."[154] The Board guidelines themselves, however, were designed to "allow each Reserve Bank to administer its own appellate process."[155] The guidelines seemed to contemplate that each regional Reserve Bank would adopt additional policies governing appeals of MSDs.[156] Most have done so,[157] but my FOIA request failed to yield appeals policies for

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Company Supervision Procedures for Organizations with Total Consolidated Assets of $5 Billion or Less).

150 BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 99TH ANNUAL REPORT 53 (2012).

151 BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 99TH ANNUAL REPORT BUDGET REVIEW 37, 41 (2012) (noting that there were 347 supervision employees at the Board of Governors and 3,339 supervision employees at the regional Federal Reserve Banks).

152 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470 (1995).

153 *Id*. at 16,473.

154 *Id*. at 16,472.

155 *Id*.

156 *See id*. at 16,473 ("Each Reserve Bank shall make these guidelines and the Reserve Bank's process for selecting a review panel available to each institution in its district, any institution appealing a material supervisory determination, and any member of the public who requests them.").

157 Federal Reserve Bank of Atlanta, Procedures for Appeals of Material Supervisory Determinations (Mar. 2, 2010), *available at* http://www.frbatlanta.org/documents/banking/sr/FRBATL_Appeals%20_Proc_030210.pdf [hereinafter FRB Atlanta Appeals]; Federal Reserve Bank of San Francisco, Division of Banking Supervision and Regulation, Policy Statement on Appeals of Material Supervisory Determinations (Feb. 2013), *available at* http://www.frbsf.org/banking-supervision/regulation/appeals-policy/FRBSF-

the Federal Reserve Banks of Boston, Cleveland, Chicago, and St. Louis.[158]

At the Federal Reserve, financial institutions dissatisfied with an MSD may file a written appeal with the "Secretary of the Reserve Bank or other appropriate Reserve Bank official."[159] The appeal must be approved by the institution's board of directors and must "contain all the facts and arguments that the institution wishes to present."[160] When a Federal Reserve Bank receives an appeal, it must forward a copy to staff of the Federal Reserve Board.[161] The MSD that is the subject of the appeal remains in effect during the appeals process.[162]

According to the Board guidelines, the initial appeal is considered "by a person or persons selected by the Reserve Bank . . . who . . . did not participate in the material supervisory determination[,] do not directly or indirectly report to the person who made the material supervisory

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Appeals-Policy.pdf [hereinafter FRB San Francisco Appeals]; Federal Reserve Bank of Philadelphia, Policy Statement on Appeals of Material Supervisory Determinations (Sept. 24, 2001) (affirmed Jan. 28, 2011), *available at* http://www.phil.frb.org/bank-resources/supervision-and-regulation/appeals-policy/AppealPolicy.pdf [hereinafter FRB Philadelphia Appeals]; Federal Reserve Bank of Kansas City, Procedures for Appealing Material Supervisory Determinations (date unavailable), *available at* http://www.kansascityfed.org/publicat/banking/membership/smb/AppealProcedures.pdf [hereinafter FRB Kansas City Appeals]; Federal Reserve Bank of Richmond, Policy Statement on Appeals of Material Supervisory Determinations (Aug. 14, 2012), *available at* http://www.richmondfed.org/banking/supervision_and_regulation/pdf/policy_statement_on_appeals.pdf [hereinafter FRB Richmond Appeals]; Federal Reserve Bank of New York, Procedures for Appeals of Adverse Material Supervisory Determinations (date unavailable), *available at* http://www.newyorkfed.org/banking/pdf/appeals_procedures.pdf [hereinafter FRB New York Appeals]; Federal Reserve Bank of Minneapolis, Procedures for Appealing Material Supervisory Determinations (Feb. 6, 2004), *available at* http://www.minneapolisfed.org/banking/appeals/appealsprocedures.pdf [hereinafter FRB Minneapolis Appeals].

158 A 2012 Federal Reserve Office of Inspector General audit of the community bank examination process "found that all 12 Reserve Banks have established appeals policies that follow Board guidance." FEDERAL RESERVE OIG REPORT, *supra* note 11, at 24. To gather such policies, I made a FOIA request to the Federal Reserve for all "policies currently in effect for handling . . . appeals of material supervisory determinations." The Federal Reserve's response did not contain policies from the Federal Reserve Banks of Boston, Cleveland, Chicago, or St. Louis. *See* E-mail from Denise Harris, FOIA Office, Federal Reserve Board to author (June 10, 2013) (on file with author). I telephoned the Federal Reserve's FOIA Office and confirmed that no policies were available for these Reserve Banks. Telephone call with Denise Harris, FOIA Office, Federal Reserve Board (June 21, 2013).

159 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,472 (1995).

160 *Id*.

161 *Id*.

162 *Id*. at 16,473

determination under review[,] and . . . are qualified to review the material supervisory determination."[163] Some Reserve Banks' policies specify that the review panel should consist of at least three individuals who are appointed by the Federal Reserve Bank Office in Charge of Supervision and Regulation.[164] Federal Reserve Chairman Ben S. Bernanke recently explained that these "review panels" are "selected after consultation with staff at the [Federal Reserve] Board in Washington."[165] The review panels are often composed of employees from Reserve Banks other than the Reserve Bank that handled the examination.[166] This process means that the initial review panels are created on an *ad hoc* basis and vary in makeup from appeal to appeal.

An institution submitting an appeal is entitled to appear in person before the review panel.[167] The review panel may choose to allow the institution to present witnesses.[168] The Federal Reserve Bank of New York specifically allows the institution to be represented by counsel and notes that allowed witnesses might include accountants and other experts.[169] It also notes that in some instances the review panel may request that examination staff participate in or present testimony at the hear-

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[163] *Id*. at 16,472.

[164] *See* FRB ATLANTA APPEALS, *supra* note 157, at 2 (providing for a three person review panel), at 2; FRB PHILADELPHIA APPEALS, *supra* note 157, at 4 (specifying that a review panel consists of three or five individuals); FRB RICHMOND APPEALS, *supra* note 157, at IV.B (stating that the reserve panel must contain at least three individuals). *But see* FRB SAN FRANCISCO APPEALS, *supra* note 157, at 3 (failing to specify the number of individuals on a review panel); FRB KANSAS CITY APPEALS, *supra* note 157, at 4 (stating that the size of the panel should be determined "in light of the nature of the appeal, availability of independent qualified officers and staff, and other factors deemed relevant by the Appropriate Reserve Bank Official"); FRB NEW YORK APPEALS, *supra* note 157, at 7(a) (stating that the review panel must consist of at least one individual); FRB MINNEAPOLIS APPEALS, *supra* note 157, at 5 (stating that the size of the panel should be determined "in light of the nature of the appeal, availability of independent qualified officers and staff, and other factors deemed relevant by the Appropriate Reserve Bank Official").

[165] Ben S. Bernanke, Chairman, Bd. of Governors of the Federal Reserve System, Speech at the Future of Community Banking Conference (Feb. 16, 2012), *available at* 2012 WL 523933.

[166] FEDERAL RESERVE OIG REPORT, *supra* note 11, at 22 ("According to Board staff, members of the independent panel are often selected from other Reserve Banks to ensure their independence.").

[167] Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,472 (1995).

[168] *Id*.

[169] FRB NEW YORK APPEALS, *supra* note 157, at 9(a).

ing.[170] Most regional Reserve Banks' policies provide for transcribing or recording the proceedings.[171]

As an initial matter, the review panel must decide whether the institution's complaint falls within the scope of appealable MSDs.[172] The Federal Reserve Board guidelines state that "[t]he term 'material supervisory determination' includes, but is not limited to, material determinations relating to examination or inspection composite ratings, the adequacy of loan loss reserves and significant loan classifications."[173] The Federal Reserve Bank of San Francisco's policy adds that an appeal "may cover any type of examination, including safety and soundness, trust, transfer agent, electronic data processing, consumer compliance, and CRA."[174] Institutions may not use the MSD appeals process to challenge prompt corrective action directives, enforcement actions, or capital directives.[175] If the review panel concludes that the matter is not subject to appeal, the institution can appeal that decision in the same way it could appeal a decision on the merits of the appeal.[176]

If the review panel concludes the matter is appealable, it then turns its attention to the merits of the appeal. The Board guidelines provide no guidance on the standards the review panel should use in evaluating the appeal. Regional Reserve Banks have filled this void with conflicting policies. The Federal Reserve Bank of New York allows the most robust review, stating that "[t]he Review Panel will use a '*de novo*' standard of review in reaching its decision."[177] On the other hand the Federal Reserve Banks of Minneapolis and Kansas City state that the review panel has power to determine the standard of review.[178] "Generally, the stand-

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170 *Id*. at 9(c).

171 Some Federal Reserve Banks' policies allow the review panel to determine whether a transcript or recording is made. FRB ATLANTA APPEALS, *supra* note 157, at 2; FRB SAN FRANCISCO APPEALS, *supra* note 157, at 5; FRB PHILADELPHIA APPEALS, *supra* note 157, at 7. Other Federal Reserve Banks' policies require a transcript or recording. FRB KANSAS CITY APPEALS, *supra* note 157, at 6; FRB RICHMOND APPEALS, *supra* note 157, at V.B.5.d; FRB NEW YORK APPEALS, *supra* note 157, at 9(d); FRB MINNEAPOLIS APPEALS, *supra* note 157, at 8.

172 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,473 (1995).

173 *Id*.

174 FRB SAN FRANCISCO APPEALS, *supra* note 157, at 2.

175 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,472 (1995).

176 *Id*.

177 FRB NEW YORK APPEALS, *supra* note 157, at 10(a).

178 FRB KANSAS CITY APPEALS, *supra* note 157, at 6; FRB MINNEAPOLIS APPEALS, *supra* note 157, at 7.

ard of review will focus on whether the Reserve Bank's findings and conclusions are based on sufficient evidence and are consistent with [Federal Reserve System] policy."[179] These Reserve Banks explicitly state that "[i]n most cases, a *de novo* review will not be undertaken."[180] The remaining regional Reserve Bank's policies do not directly address the standard of review.[181] Given this lack of clarity, it seems the standard of review employed can vary widely depending on the location of the institution, the make-up of the review panel, and other unexplained factors deemed important by the review panel.

Once the review panel reaches a conclusion, it must prepare a written decision.[182] The decision should summarize the factual and legal basis for the panel's conclusions.[183] The review panel sends the written decision to the institution.[184] Regional Reserve Bank policies also require that the decision be sent to Federal Reserve staff members who oversee the institution's examinations or inspections, the Board of Governors of the Federal Reserve, and any relevant state regulators.[185] Ordinarily, the review panel should reach a decision "within 30 calendar days of the filing of an informationally complete appeal."[186]

The institution, with the consent of its board of directors, may appeal the review panel's decision to the regional Reserve Bank Presi-

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179 FRB KANSAS CITY APPEALS, *supra* note 157, at 6; FRB MINNEAPOLIS APPEALS, *supra* note 157, at 7.

180 FRB KANSAS CITY APPEALS, *supra* note 157, at 6; FRB MINNEAPOLIS APPEALS, *supra* note 157, at 7.

181 The policies of the Federal Reserve Banks of Philadelphia and Richmond state that the written decision should "set forth the Review Panel's conclusions, including the scope of the review." FRB PHILADELPHIA APPEALS, *supra* note 157, at 8; FRB RICHMOND APPEALS, *supra* note 157, at V.C.1.

182 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,472 (1995).

183 *See, e.g.*, FRB KANSAS CITY APPEALS, *supra* note 157, at 7 ("The written decision will include a memorandum outlining the basis for the Appeal Panel's conclusions, including appropriate citations of legal authority or [Federal Reserve System] policies and documentation provided by the Appellant or the Reserve Bank.").

184 *See, e.g.*, FRB PHILADELPHIA APPEALS, *supra* note 157, at 8.

185 *See, e.g.*, FRB ATLANTA APPEALS, *supra* note 157, at 4-5.

186 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,472 (1995). Federal Reserve Bank policies generally provide that an appeal is not considered "informationally complete" until any requested hearing has been held. *See, e.g.*, FRB RICHMOND APPEALS, *supra* note 157, at V.B.3.

dent.[187] As with the initial appeal, this secondary appeal should contain "all facts and arguments that the institution wishes to be considered."[188] The Board guidelines provide little guidance on this stage other than to note that the President should issue a written decision to the institution within "30 calendar days of the filing of an informationally complete appeal."[189]

Regional Reserve Bank policies on this second level of appeal are scant and varied. Some policies focus on the mechanics of the review. For example, some policies provide that the Reserve Bank President should obtain a record of the initial appeal and should allow supervisory staff an opportunity to respond to any new claims raised by the institution.[190] Only the Federal Reserve Banks of Kansas City and Minneapolis attempt to address the standard of review, and they provide the Federal Reserve Bank President with complete discretion to determine the standard and scope of the review.[191]

If the financial institution is still dissatisfied, it can appeal "to the appropriate [Federal Reserve Board] Governor by filing a written appeal with the Secretary of the Board."[192] Currently, Federal Reserve Governor Daniel K. Tarullo is tasked with handling such appeals.[193] The Governor is instructed to "consult with the director of the appropriate division of the Board of Governors" and reach a written decision "within 60 calendar days of the filing of an informationally complete appeal."[194] The

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[187] Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,472 (1995). The Federal Reserve Bank of New York's policy provides that the second level of appeal may be heard by the Federal Reserve Bank "President or his or her appointed delegate (e.g., the [Federal Reserve Bank's] Management Committee." FRB NEW YORK APPEALS, *supra* note 157, at 11(a).

[188] Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,472 (1995).

[189] *Id*.

[190] FRB PHILADELPHIA APPEALS, *supra* note 157, at 9; FRB RICHMOND APPEALS, *supra* note 157, at VI.C; FRB MINNEAPOLIS APPEALS, *supra* note 157, at 10-11.

[191] According to these policies:

> The President may rely upon all resources within the Reserve Bank in the review of the appeal and underlying material supervisory determination. Specific standards for review are not set, but rather the President may base his decision on whatever facts and information the President deems relevant under the circumstances.

FRB KANSAS CITY APPEALS, *supra* note 157, at 8; FRB MINNEAPOLIS APPEALS, *supra* note 157, at 10-11.

[192] Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,473 (1995).

[193] Ben S. Bernanke, Chairman, Bd. of Governors of the Federal Reserve System, Speech at the Future of Community Banking Conference (Feb. 16, 2012), *available at* 2012 WL 523933.

Board guidelines do not discuss the standard of review the Governor should use in deciding the appeal. The Governor's decision cannot be appealed further.

The Board guidelines require that each regional Reserve Bank adopt "safeguards to protect appellants from retaliation."[195] Most policies state that Federal Reserve staff who retaliate against institutions will be disciplined.[196] Four Reserve Banks prevent examination staff who participated in the appealed decisions from participating in the institution's next exam and allow for longer exclusions on a case-by-case basis.[197]

The Board guidelines also assign the Federal Reserve's Ombudsman a role in discouraging retaliatory behavior by examiners. The Ombudsman must contact appealing institutions twice—once "six months after an appeal as been decided" and once "six months after the date of the next examination" to ask whether the institution has been subject to retaliation.[198] Institutions can contact the Ombudsman with a complaint of retaliation at any time.[199]

2. Federal Reserve Appeals

The Federal Reserve does not publicly release appeals decisions in any form. My FOIA requests for appeals decisions since 1994 yielded a table summarizing each appeal filed between 2001 and 2012.[200] For each appeal, the Federal Reserve provided the date of the initial appeal, the

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194 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,473 (1995).

195 *Id*.

196 *See, e.g.*, FRB RICHMOND APPEALS, *supra* note 157, at VIII.B.

197 FRB ATLANTA APPEALS, *supra* note 157, at 4; FRB SAN FRANCISCO APPEALS, *supra* note 157, at 7; FRB PHILADELPHIA APPEALS, *supra* note 157, at 10; FRB RICHMOND APPEALS, *supra* note 157, at VIII.A. Other Reserve Banks' policies specify that protections are crafted based on the circumstances of the case by the review panel or other Reserve Bank officials. FRB KANSAS CITY APPEALS, *supra* note 157, at 9-10; FRB NEW YORK APPEALS, *supra* note 157, at 12(b); FRB MINNEAPOLIS APPEALS, *supra* note 157, at 10-11.

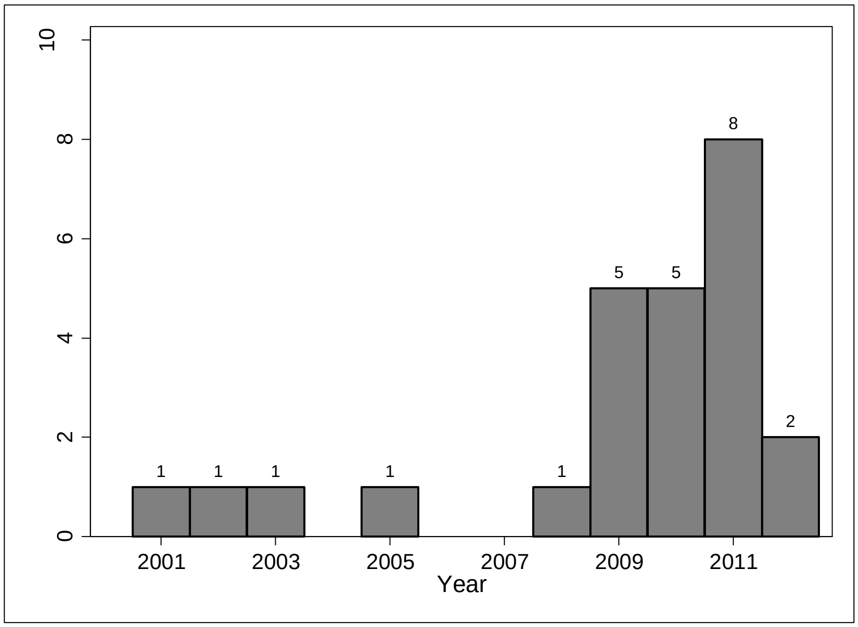
198 Board of Governors of the Federal Reserve System, Ombudsman Policy Statement, http://www.federalreserve.gov/aboutthefed/ombpolicy.htm (last updated Nov. 6, 2009). *See also* Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,473 (1995) ("The Board's Ombudsman will periodically contact institutions after their appeal to make certain that no retaliation has occurred.").

199 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,473 (1995).

200 Letter from Margaret McCloskey Shanks, Associate Secretary of the Board, Board of Governors of the Federal Reserve System, to author (Aug. 20, 2012) (on file with author); Letter from Robert deV. Frierson, Secretary of the Board, Board of Governors of the Federal Reserve System, to author (July 2, 2013) (on file with author).

reason for the appeal, the level of the appeal, and a summary of the outcome of the appeal. Because the Federal Reserve did not provide any of the underlying appeals decisions, it is impossible for me to confirm its characterization of the reason for and outcome of each appeal.

Figure 4: Federal Reserve Material Supervisory Determinations Appeals per Year (2001-2012)



Between 2001 and 2012, the Federal Reserve received 25 appeals of MSDs. As with the OCC, there was an increase in the number of appeals corresponding with the 2008 financial crisis.[201]

The vast majority of appeals were resolved at the initial review panel stage. Of the 25 appeals, only 6 pursued an additional appeal to the regional Reserve Bank President, and only 4 of those filed an appeal with the Federal Reserve Board Governor tasked with resolving appeals. The Federal Reserve did not indicate which regional Reserve Bank handled each appeal.

Little is known about the entities bringing these appeals. In one instance the reason for the appeal and the outcome suggest the appellant

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[201] It is also possible that information on appeals, particularly from the earlier years is complete.

was a bank holding company, but in all other instances there is no description of the appealing institution.

As with the OCC, Federal Reserve appeals most frequently involved CAMELS composite or component ratings. Figure 5 details issues raised by at least two appeals.

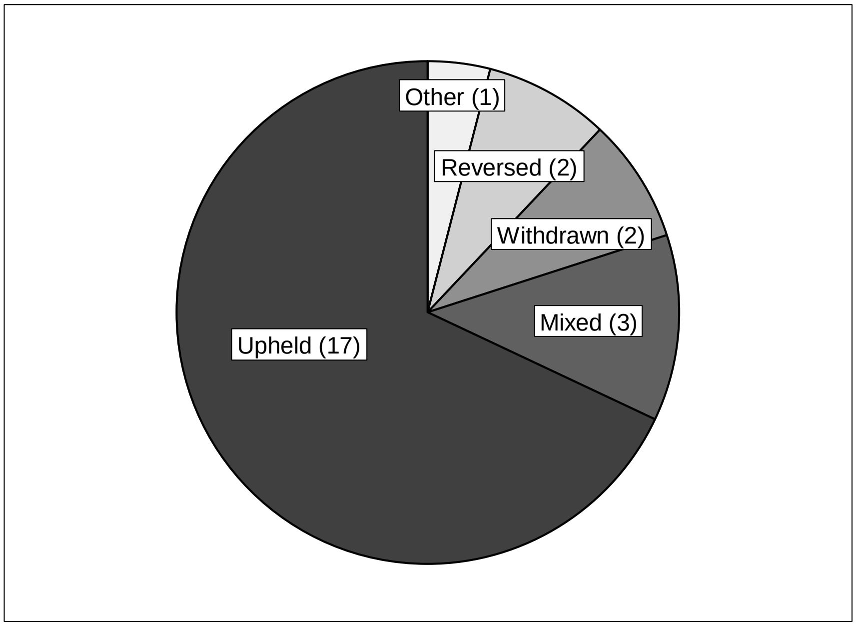
Figure 5: Federal Reserve Material Supervisory Determinations Appealed (2001-2012)

Reason for Appeal	**Number**
CAMELS Composite or Component Ratings	16
Loan or Asset Classifications	7
Capital Calculations	2
Limitation or Restriction of Dividend Payments	2
Issues Related to a Formal or Informal Enforcement Actions	2

Of the 16 appeals involving CAMELS composite or component ratings, 12 specify "[c]omposite/component ratings" as the reason for the appeal. Two appeals involved the management component rating. One appeal involved the asset quality component rating. And 1 appeal involved only the appeal of a composite rating. The Federal Reserve did not provide any data about the actual rating (1-5) that the appealing entity received.

The Federal Reserve's appeals process rarely overturns MSDs. The process upheld the examiner determination 68 percent (17/25) of the time. Only 2 appeals (8 percent) reversed the examiner determination.

Figure 6: Outcomes of Federal Reserve Material Supervisory Determination Appeals (2001-2012)



Appeals were most successful at the review panel level. The review panel upheld 18 cases, reversed 2 cases, and issued mixed decisions in 2 cases. Appeals escalated to the regional Reserve Bank President were never successful; all 6 president-level decisions upheld the examination determinations. Of the 4 appeals that were ultimately brought to a Federal Reserve Board Governor, 2 upheld the MSD, 1 was withdrawn before the Governor issued an opinion, and 1 resulted in a mixed decision. Because the Federal Reserve did not provide any underlying information about any of the appeals, it is impossible to assess whether the Federal Reserve has been consistent in its decision-making.

C. FDIC

The Federal Deposit Insurance Corporation insures bank deposits.[202] Although the FDIC provides insurance for banks regulated by the OCC and Federal Reserve, the FDIC does not serve as the primary regulator for those banks.[203] The FDIC is the primary federal regulator only

[202] 12 U.S.C. §§ 1811, 1814-15 (2012).

[203] *See supra* Parts II.A and II.B (describing the examination authority of the OCC and Federal Reserve), 12 U.S.C. § 1820(b)(3) (giving the FDIC examination authority over all insured

for state-chartered banks and thrifts that are not members of the Federal Reserve System.[204] Because non-member state banks are also regulated by state authorities, the FDIC "and state regulators coordinate their supervisory programs and, in many instances, alternate examinations or conduct joint examinations."[205] The FDIC currently serves as the primary federal regulator for 4,304 banks.[206] More than 90 percent of those banks have assets of less than $1 billion.[207] The FDIC has 7,476 full-time equivalent employees.[208]

1. FDIC Appeals Process

Before Congress mandated that federal regulators provide an independent intra-agency review process for MSDs, the FDIC had an informal policy of reviewing "examination finding and similar decisions during the examination process."[209] Under that policy, banks could address a written request for "supplementary review" to the Division of Supervision Director in Washington, D.C.[210] The Director would then "make a good faith effort to evaluate and resolve the issues raised."[211]

In response to the Reigle Community Development and Regulatory Improvement Act of 1994, the FDIC Board of Directors adopted new, more formal guidelines.[212] The FDIC has amended these guidelines on four occasions, adjusting the scope of appealable matters, the composition of the appellate review committee, and the process for handling appeals.[213]

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banks), CARNELL, MACEY, & MILLER, *supra* note 21, at 632 (describing the examination conventions employed by federal regulators).

[204] FDIC OIG REPORT, *supra* note 11, at 2.

[205] *Id*.

[206] *See Statistics on Depository Institutions*, FDIC, http://www2.fdic.gov/sdi/ (last visited Jan. 18, 2013).

[207] *See id*. (listing 3,982 state-chartered non-member banks with less than $1 billion in assets).

[208] FDIC ANNUAL REPORT 2012, at 133.

[209] FDIC Financial Institution Letter 11-92 (Feb. 7, 1992) (Procedures for Requesting Review of Supervisory Decisions).

[210] *Id*.

[211] *Id*.

[212] FDIC Intra-Agency Appellate Process, 60 Fed. Reg. 15,923 (1995).

[213] *See* FDIC Intra-Agency Appeal Process, 69 Fed. Reg. 41,479 (2004) (reducing the Supervisory Appellate Review Committee from five to three members and adjusting the process for

As currently written, the FDIC guidelines encourage, but do not require, banks to make "a good-faith effort to resolve any dispute concerning a material supervisory determination with the on-site examiner and/or the appropriate Regional Office."[214] If the bank is still unhappy with an MSD, the bank may request that the Division or Office Director overseeing the examination conduct a formal review.[215] The request for review must include a description of the issues with citations to relevant legal authority.[216] The request for review must also indicate that the bank's board of directors has authorized the review.[217]

The FDIC's guidelines do not specify how the Division or Office Director should go about deciding the appeal. To fill this void, in 2004 the Division of Supervision and Consumer Protection (now known as the Division of Depositor and Consumer Protection) adopted its own policy

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triggering review by that Committee); FDIC Guidelines for Appeals of Material Supervisory Determinations, 73 Fed. Reg. 54,822, 54,824 (2008) ("eliminate[ing] the ability of an FDIC-supervised institution to file an appeal with the [Supervisory Review Committee] with respect to determinations or the facts and circumstances underlying a recommended or pending formal enforcement-related actions or decisions"); FDIC Intra-Agency Appeal Process, 75 Fed. Reg. 20,358 (2010) (extending various deadlines for FDIC decisions on appeals); FDIC Intra-Agency Appeal Process, 77 Fed. Reg. 17,055 (2012) (making changes to reflect organizational adjustments necessitated in part by the elimination of the Office of Thrift Supervision).

The 2004 process changes suggest that the FDIC also amended the policy in 1999. *See* FDIC Intra-Agency Appeal Process, 69 Fed. Reg. 41,479, (2004) ("The 1995 SARC guidelines were amended in 1999 . . . to provide formally that the Directors of DOS and DCA (now the DSC Director) would not vote on cases brought before the SARC involving their respective (now consolidated divisions) . . . . .") However, when I made a FOIA request for documents related to a 1999 change, the FDIC responded that it had no responsive documents, explaining that "the FDIC did not publish a 1999 edition of the Guidelines for Appeals of Material Supervisory Determinations." *See* Letter from Jim Braun, Senior FOIA Specialist, FDIC to author (July 9, 2013) (on file with author).

214 FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,057.

215 *Id*. (specifying that appeals should be made to "either the Director, [Division of Depositor and Consumer Protection], Director, [Division of Risk Management Supervision], or Director, [Office of Complex Financial Institutions]"). The Division of Risk Management Supervision has responsibility for safety and soundness examinations as well as trust operations, information technology controls, and Bank Secrecy Act compliance. The Division of Depositor and Consumer Protection conducts examinations to assess compliance with the Community Reinvestment Act and consumer protection laws. The Office of Complex Financial Institutions is tasked with overseeing the supervisory, insurance, and resolution risks presented to the FDIC by large and complex financial institutions. FDIC OIG REPORT, *supra* note 11, at 2-3.

216 FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,057 (additionally requiring a description of "how resolution of the dispute would materially affect the institution, and whether a good-faith effort was made to resolve the dispute with the on-site examiner and the Regional Office").

217 *Id*.

for handling its appeals.[218] There the Director appoints a three person committee to prepare "a memorandum that summarizes the institution's position, the Regional Office's position, and if applicable the State banking authority's position, as well as the basis for the Panel's recommendation regarding each material supervisory determination."[219] After reviewing this information the Director makes his or her own assessment.[220] In any event, the Division or Office Director will issue a written decision within forty-five days of receipt of the request.[221]

If the bank is still not satisfied, it may appeal to the FDIC's Supervision Appeals Review Committee. The Committee consists of three voting members, including one FDIC inside board member and one deputy or special assistant to a board member.[222] "The [FDIC's] General Counsel is a non-voting member of the [Committee]."[223] The current Supervision Appeals Review Committee consists of FDIC Vice Chairman Thomas E. Hoenig, Deputy to the Chairman Kymberly Copa, and Deputy to the Director Marianne Hatheway.[224] FDIC Acting General Counsel Richard Osterman serves as a nonvoting member of the Committee.[225]

The bank must provide the Committee with contact information for the bank, the Division or Office Director's determination, and an explanation of "all the reasons, legal and factual, why it disagrees with the Division or Office Director's determination."[226] The bank is generally prohibited from raising arguments or providing evidence that was not

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[218] FDIC, The Division of Supervision and Consumer Protection's (DSC) Guidelines for Processing Requests for Review of Material Supervisory Determinations, http://www.fdic.gov/regulations/laws/sarc/dscguidelines.html (last updated Dec. 17, 2004) [hereinafter FDIC DSC Guidelines]. Although the name of the division has changed and the FDIC's appeals guidelines have been updated since 2004, *see supra* note 213, it does not appear that the Division has updated its process guidelines.

[219] FDIC DSC Guidelines, *supra* note 218. If the subject matter of the appeal was the "joint product" of the FDIC and a state regulator, the FDIC must notify the state regulator of the appeal and provide that regulator with an opportunity to comment on it. FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,057.

[220] FDIC DSC Guidelines, *supra* note 218.

[221] FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,058.

[222] *Id*. at 17,056.

[223] *Id*.

[224] Letter from Jim Braun, Senior FOIA Specialist, FOIA/Privacy Act Group, FDIC to author (July 15, 2013) (on file with author).

[225] *Id*.

[226] FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,058.

considered by the Division or Office Director.[227] The Committee will not consider changes in facts or circumstances that arose after the completion of the examination.[228] The appealing bank is not entitled to "discovery or other such rights."[229]

The FDIC guidelines contain a list of appealable items that includes CAMELS ratings, determinations concerning the adequacy of loan loss reserves, and "[c]lassifications of loans and other assets in dispute the amount of which individually or in the aggregate, exceeds 10 percent of the institution's total capital."[230] The guidelines specify that banks may not appeal "[f]ormal enforcement-related actions and decisions, including determinations and the underlying facts and circumstances that form the basis of a recommended or pending formal action, and FDIC determinations regarding compliance with an existing formal enforcement action."[231]

At the FDIC, the appeals process itself is not a trial-like review of the MSD. An appealing bank may request that it be allowed to make an oral presentation,[232] but the Committee need not grant the request. The guidelines specify that oral presentation should only be granted if it "is likely to be helpful or would otherwise be in the public interest."[233] According to Sandra L. Thompson, Director of the FDIC's Division of Risk Management Supervision, institutions' requests for oral presentation are "normally granted."[234] If the Committee allows an oral presentation, the Committee can question the institution and require that FDIC staff participate in the proceeding.[235] The Committee "review[s] the appeal for con-

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[227] *Id*. ("Evidence not presented for review to the Division or Office Director may be submitted to the [Committee] only if authorized by the [Committee] Chairperson.").

[228] *Id*.

[229] *Id*. at 17,060.

[230] *Id*. at 17,057. Banks may also appeal IT ratings, CRA ratings, consumer compliance ratings, trust ratings, securities dealer examination ratings, findings of statutory or regulatory violations, Truth in Lending Act restitution, and "any other supervisory determination . . . that may affect the capital, earnings, operating flexibility, or capital category for prompt corrective action purposes of an institution, or otherwise affect the nature and level of supervisory oversight accorded an institution." *Id*.

[231] *Id*.

[232] *Id*. at 17,058.

[233] *Id*.

[234] *Hearing on H.R.* 3461, *supra* note 5, at 145 (written testimony of Sandra L. Thompson, Director, FDIC Division of Risk Management Supervision).

[235] FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,058.

sistency with the policies, practices, and mission of the FDIC and the overall reasonableness of, and the support offered for, the positions advanced."[236] The bank bears the "burden of proof as to all matters at issue in the appeal."[237]

Regardless of whether there is a hearing, the Committee must convene to discuss the appeal within ninety days of the time the bank's request for review was filed. Once the Committee has met, it has forty-five days to prepare a written decision and provide it to the appealing bank.[238] The Committee then publishes the decision online, redacting it to omit confidential information about the bank or the bank's customers.[239] "In cases in which redaction is deemed insufficient to prevent improper disclosure, published decisions [are] presented in summary form."[240]

The FDIC's guidelines prohibit examiners from retaliating against banks that use the appeals process. Retaliation "constitutes unprofessional conduct and will subject the examiner or other personnel to appropriate disciplinary or remedial actions."[241] The process for handling allegations of retaliation is less clear. Banks are first "encouraged to contact the Regional Director," but later the guidelines provide that institutions may file complaints of retaliation with the FDIC Ombudsman.[242] If a bank complains of retaliation to the Ombudsman, the Ombudsman is instructed to "work with the appropriate Division or Office Director to resolve the allegation of retaliation."[243]

2. FDIC Appeals

At the FDIC appeals must first be addressed to a Division Director.[244] The Director's decision can then be appealed to the Supervision

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[236] *Id*.

[237] *Id*.

[238] *Id*.

[239] *Id*. (noting that the appeals decisions can be cited as precedent); FDIC, Supervision Appeals Review Committee – Decisions, http://www.fdic.gov/regulations/laws/sarc/sarcappeals.html (last updated Aug. 8, 2012).

[240] FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,058. *See, e.g.*, Appeal of Compliance and CRA Ratings, SARC-2007-04 (May 2, 2008).

[241] FDIC Intra-Agency Appeal Process, 77 Fed. Reg. at 17,059.

[242] *Id*. 17,058.

[243] *Id*.

[244] See supra note 215-221 and accompanying text.

Appeals Review Committee.[245] FDIC does not publicly release Director-stage decisions. I requested those decisions through FOIA. The FDIC eventually provided a summary table listing the type of determination, the date the Director appeal was received, the action taken by the Director, the date of any appeal to the Committee, and the Committee's decision.[246]

It appears that some of this FOIA gathered data is incomplete—particularly for appeals filed before 2005. The FOIA data list only 6 pre-2005 Committee appeals. In contrast, the FDIC's webpage contains 46 pre-2005 Committee decisions.[247] Because each appeal had to first be addressed to the appropriate Director, some Director appeals are missing from the FOIA data.[248]

The FOIA-provided Director-level data from 2005 onward seem more complete.[249] The FOIA data show 56 appeals filed between 2005 and 2012. Of those, 25 generated appeals to the Committee.

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245 *See supra* notes 222-225 and accompanying text.

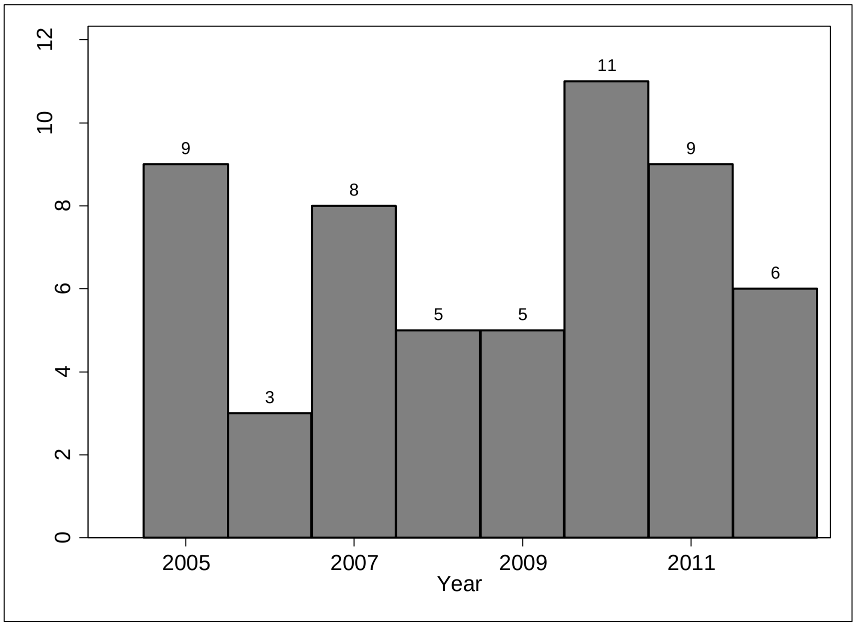
246 Initially, the FDIC denied my request asserting the information was protected bank examination material under 5 U.S.C. § 552(b)(8). Letter from Jim Braun, Senior FOIA Specialist, FOIA/Privacy Act Group, FDIC, to author (June 18, 2013). I appealed the denial to the FDIC's General Counsel. Letter from author to Richard J. Osterman, Jr., Acting General Counsel, Federal Deposit Insurance Corporation (June 19, 2013) (on file with author). The FDIC then agreed to provide the summary information. Letter from Barbara Sharshil, Senior Counsel, FDIC to author (July 30, 2013) (on file with author). The initial table provided by the FDIC omitted Committee information for some appeals. Letter from Barbara Sharshil, Senior Counsel, FDIC to author (July 30, 2013) (on file with author). A further FOIA request yielded the missing information. Letter from Jim Braun, Senior FOIA Specialist, FOIA/Privacy Act Group, FDIC to author (Oct. 10, 2013) (on file with author).

247 Appeals to the Supervision Appeals Review Committee are summarized in Figure 8.

248 Record making and keeping during the pre-2005 time period may have been lacking. *Cf*. FDIC Intra-Agency Appeal Process, 69 Fed. Reg. at 41,481 (noting a financial institution's complaint that it had never been "informed of [the Director's] denial of its request for review or that the request has been passed to the SARC").

249 In three instances, I still could not reconcile the FOIA data with the FDIC's Supervision Appeals Review Committee decisions webpage. One webpage Committee decision did not appear on the FOIA list: Appeal of rate restrictions under 12 C.F.R. § 337.6, SARC-2010-04, http://www.fdic.gov/regulations/laws/sarc/sarcappeals/sarc201004.pdf (Sept. 7, 2010). Two Committee appeals on the FOIA list did not appear as decisions on the FDIC's webpage. One was a March 24, 2005 appeal of a "[c]omposite rating; capital, management, earning, and liquidity component ratings" that was reportedly denied by the Committee. The other was a February 1, 2005 appeal of a "[c]onsumer compliance rating" that was reportedly denied by the Committee.

Figure 7: FDIC Material Supervisory Determination Appeals Filed with a Division Director (2005-2012)



In comparison, information about appeals decided by the Supervision Appeals Review Committee is more available and more complete. The FDIC has published online redacted or summary versions of every decision issued by its Supervision Appeals Review Committee since 1995.[250]

According to the FDIC webpage, the Committee issued 63 decisions between 1995 and 2012. As shown in Figure 8, the Committee handled more appeals during its early years of operations. As with the OCC, the early number of appeals might be partly attributable to economic conditions and pent-up demand for an appeals process. At the FDIC, there is another likely reason: until 2004, any Division Director who decided an appeal against a bank was required to forward the appeal to the Supervision Appeals Review Committee for review.[251] In 2004, the FDIC amended its process to allow the appealing bank to determine whether it wanted to pursue the additional appeal to the Committee.[252]

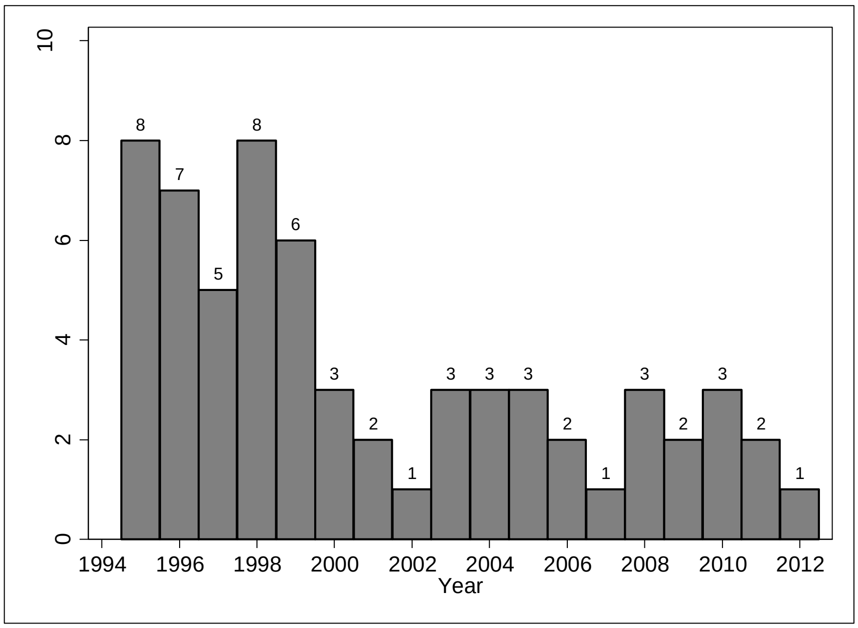
250 *See supra* note 239-240 and accompanying text.

251 FDIC Intra-Agency Appellate Process, 60 Fed. Reg. at 15,930.

252 FDIC Intra-Agency Appeal Process, 69 Fed. Reg. at 41,481.

This change may have resulted in fewer appeals sent to the Committee after 2004.

Figure 8: FDIC Supervision Appeals Review Committee Decisions per Year (1995-2012)



As with the OCC and Federal Reserve, complaints about CAMELS composite or component ratings generated the most appeals (35). Community Reinvestment Act examination ratings also generated a significant number of appeals (19). Figure 9 summarizes issues raised by at least two appeals from 2005 through 2012.

Of the appeals between 2005 and 2012 involving CAMELS ratings, the management rating was most commonly appealed (22 times), followed closely by the composite rating (19). Earnings (15), capital (14), and asset (12) ratings were also frequently appealed. Liquidity (6) and sensitivity to market risk (7) were appealed less frequently.

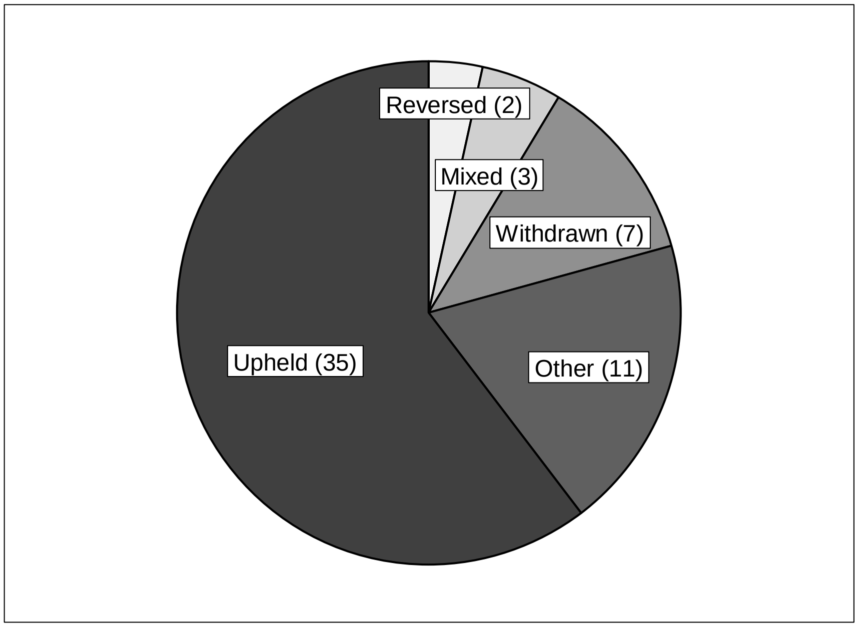
Figure 9: FDIC Material Supervisory Determinations Appealed (2005-2012)[253]

Reason for Appeal	**Number**
CAMELS Composite or Component Ratings	35
Community Reinvestment Act Rating	19
Loan or Asset Classifications	13
Consumer Compliance Exam Rating or Conclusions	12
Fair Housing Act / Equal Credit Opportunity Act Findings or Violations	7
Capital Calculations or Classification and Resulting Restrictions	6
Issues Related to a Formal or Informal Enforcement Actions	6
Allowance for Loan and Lease Losses	3
Accounting Issues	3
Insider Lending / Regulation O	3
Designation of the Bank as "Troubled"	2
Determination that Bank Must Amend Its Call Report	2

Data on the numerical ratings appealed are only available for those appeals handled by the Supervision Appeals Review Committee. During the 2005 to 2012 time period, appeals of a three-rating were most likely to be heard by the Committee: 47 three-ratings were appealed. In comparison, 23 two-ratings were appealed, 16 four-ratings were appealed, and 5 five-ratings were appealed. When compared with OCC-regulated banks FDIC-regulated banks appear more likely to appeal a two-rating.

[253] Data for this figure were compiled from the FOIA-provided summary of Director-level appeals. As such, it contains the issues as characterized by the FDIC. I attempted to reconcile the FOIA information with the Supervision Appeals Review Committee Decisions. *See supra* note 252. In cases where the Director decision was appealed to the Committee, the FDIC's description of the issued appealed was generally accurate.

Figure 10: Outcomes of FDIC Material Supervisory Determination Appeals (2005-2012)[254]



When banks appeal MSDs using the FDIC's process, they rarely win. Between 2005 and 2012,[255] only 2 decisions were entirely in favor of the bank[256] and 3 were decided partially in favor of the bank.[257] This means that the appealing bank secured something it wanted in less than

[254] Data for this figure were compiled from both the data received through FOIA and the publicly available appeals decisions; the figure shows the ultimate outcome whether reached at the Director level or at the Supervision Appeals Review Committee Level. For this reason, it contains data on two more appeals than the data in Figures 8 and 9. *See supra* note 249 describing minor data inconsistencies. For those curious about just those appeals before the Supervisory Review Committee (1995-2012): 58 upheld the examiner determination, 4 reversed the examiner determination, and 1 was a mixed decision.

[255] It is unclear whether this same pattern holds for pre-2005 appeals. Of the Supervision Appeals Review Committee decisions issued before 2005, 39 upheld the examiner determination, 4 reversed the examiner determination, and 4 were mixed decisions. On the other hand, the likely incomplete FOIA list (*see supra* note 248 and accompanying text) of appeals show 5 appeals upholding the examiner, 8 reversing the examiner, 6 mixed decisions, and 2 withdrawn appeals.

[256] In one of those cases the regional office reconsidered and upgraded the appealed management rating before the Director decided the appeal. The other bank win was issued at the Director-level.

[257] One mixed decision was issued at the Director-level. The other two were issued by the Supervision Appeals Review Committee.

10 percent of appeals (5/58). In contrast, the process fully upheld the examiner 60 percent (35/58) of the time. Of the 11 appeals falling in the "other" category, the Director or Committee determined that 7 were ineligible for review and returned them without a written decision.[258]

D. NCUA

The National Credit Union Administration supervises federally chartered credit unions[259] as well as federally insured state-chartered credit unions.[260] Credit unions are distinct from the financial institutions previously discussed because they are owned by their "members" (rather than investors),[261] have limited authority to engage in commercial lending,[262] and pay fewer taxes.[263] Credit unions are, on average, smaller than banks.[264] Notwithstanding these differences, the NCUA evaluates credit unions using the CAMEL rating system[265] and, like the other federal regulators, must provide an "independent intra-agency appellate process . . . to review material supervisory determinations."[266] As of the end of 2012, the NCUA supervised 4,272 federal credit unions and 2,547 federally

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[258] The outcomes of 3 appeals were categorized as "other" because the bank was closed or deposit insurance was terminated. The final "other" appeal was "Returned/PCA notice rescinded."

[259] 12 U.S.C. § 1756 (2012).

[260] *Id*. §§ 1782, 1784. Credit union deposits can be insured by the National Credit Union Share Insurance Fund, an insurance fund operated by the federal government that is similar to the FDIC's insurance fund for banks. *Id*. at § 1783. Both federally chartered and state chartered credit unions are eligible for this federal insurance, and most elect its coverage. *See id*. at § 1781(a) ; *The State of the Credit Union Industry: Hearing Before the S. Comm. on Banking, Housing and Urban Affairs*, 111th Cong. 25 (written statement of Deborah Matz, Chairman, NCUA).

[261] 12 U.S.C. § 1759 (describing membership in federal credit unions); 12 U.S.C. § 1752(6) (describing "State credit union" as "a credit union organized and operated according to the laws of any State, the District of Columbia, the several territories and possessions of the United States, the Panama Canal Zone, or the Commonwealth of Puerto Rico, which laws provide for the organization of credit unions similar in principle and objective to Federal credit unions").

[262] 12 U.S.C. § 1757a.

[263] 26 U.S.C. § 501(c)(14)(A) (2011) (providing that credit unions, as non-profit, mutual organizations, are exempt from federal income tax).

[264] TIMOTHY W. KOCH & S. SCOTT MACDONALD, BANK MANAGEMENT 40-41 (7th ed. 2010).

[265] *See supra* notes 18-20 and accompanying text.

[266] 12 U.S.C. § 4806(a).

insured state-chartered credit unions.[267] It has 1,191 full-time equivalent employees.[268]

1. NCUA Appeals Process

The NCUA adopted its process for reviewing MSDs in 1995 following the Congressional mandate.[269] Although the NCUA has made minor changes to the scope of appealable matters, the structure of its appeals process has remained largely unchanged.[270]

Like other regulators, the NCUA prefers to address credit unions' complaints informally.[271] However, when such avenues prove ineffective, the NCUA's MSD appeals process is open to both federally chartered credit unions and federally insured state-chartered credit unions.[272] State-chartered credit unions can only appeal those determinations that were made by an NCUA examiner.[273] If the MSD at issue was made by a state examiner, the NCUA refers the appeal to the state for appropriate action.[274]

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[267] NCUA, December 31, 2012: Overall Trends, http://www.ncua.gov/Legal/Documents/Reports/FT20121231.pdf.

[268] NCUA 2012 ANNUAL REPORT 12.

[269] NCUA, Guidelines for the Supervisory Review Committee, 60 Fed. Reg. 14,795 (Mar. 20, 1995) (also known as NCUA Interpretive Ruling and Policy Statement 95-1).

[270] In 2001, the NCUA adopted a program known as RegFlex that allowed strong credit unions exemptions from some regulatory requirements. The NCUA subsequently amended the appeals process to allow credit unions to appeal the NCUA's determination as to whether the credit union qualified for RegFlex. *See* NCUA, Guidelines for the Supervisory Review Committee, 67 Fed. Reg. 19,778 (Apr. 23, 2002) (also known as NCUA Interpretive Ruling and Policy Statement 02-1); NCUA, Proposed Guidelines for the Supervisory Review Committee, 76 Fed. Reg. 3674 (Jan. 20, 2011); NCUA, Guidelines for the Supervisory Review Committee, 76 Fed. Reg. 23,871 (Apr. 29, 2011) (combining two previous sets of guidelines). Later, the NCUA abandoned the RegFlex program and accordingly adjusted the list of appealable issues. NCUA, Guidelines for the Supervisory Review Committee, 77 Fed. Reg. 32,004 (May 31, 2012) (removing RegFlex determinations from the list of appealable matters).

[271] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[272] *Id*.

[273] *Id*. As explained earlier, the NCUA only conducts on-site examinations of those state-chartered credit unions that pose greater risk to the share insurance fund. *See supra* note 17.

[274] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf. This situation would most likely arise when the state credit union regulator conducted the examination that led to the appeal. *See* Lee Interview, *supra* note 12.

According to an NCUA policy statement, the first step in the appeals process is to "contact the regional office regarding the examiner's decision within 30 days of the examiner's final determination."[275] The policy statement is somewhat unclear about whether this mandatory step is simply a notification to the office that oversees the examiner or whether the notification is intended to be treated as an appeal to the examiner's supervisor. The policy statement provides that "the dispute will be handed [sic] by the Region and become appealable to the [Supervisory Review] Committee either 30 days after a regional determination or 60 days after the regional office has been contacted if it has not made a determination."[276] According to Joy K. Lee, the current chair of the Supervisory Review Committee, the regional directors routinely investigate credit union appeals and respond in writing during the 30 day period.[277]

In any event, if the credit union's "contact" with the regional office does not resolve the dispute, the next step in the appeals process is to submit an appeal in writing to the NCUA's Supervisory Review Committee.[278] The appeal must be authorized by the board of directors of the credit union and "must include the name of the appellant credit union, the determination or denial being appealed and the reasons for the appeal."[279] The policy statement encourages credit unions "to submit all information and supporting documentation relevant to the matter in dispute."[280] In practice, the material submitted varies widely—from a four page letter to several binders of material.[281] The Committee may then

[275] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf. Corporate credit unions "must contact the Office of Corporate Credit Unions," the subdivision of the NCUA that oversees their examination and enforcement. *Id*. Current chair of the NCUA's Supervisory Review Committee, Joy K. Lee, notes that before raising the issue with the regional director, a credit union should have already raised the issue with the examiner, the supervisory examiner, and the associate regional director. Lee Interview, *supra* note 12.

[276] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[277] Lee Interview, *supra* note 12.

[278] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[279] *Id*.

[280] *Id*.

[281] Lee Interview, *supra* note 12.

"request additional information" from the credit union or the regional office.[282] The Committee often sends a letter detailing these additional required materials, but it is also common for the chair of the Committee to have a telephone discussion with the credit union to provide more guidance on potentially helpful documentation.[283] The Committee also reviews the material that was submitted to the Regional Director and the Regional Director's decision.[284]

The NCUA's Supervisory Review Committee is made up of three "members of the NCUA's senior staff as appointed by the NCUA Chairman."[285] No members of the Committee can directly oversee the examination function.[286] All Committee members serve a one year term, but can be reappointed for additional terms.[287] Until recently, the NCUA treated the make-up of the Committee as a closely guarded secret.[288] However, facing calls for greater transparency in the wake of the financial crisis, the NCUA now publishes the names of Committee members on its website.[289] The Committee currently consists of a program officer, the Secretary to the NCUA Board, and the Special Assistant to the Executive Director.[290] A FOIA request for the names and titles of past members of the Committee reveals that it is common for the Committee to

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282 NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

283 Lee Interview, *supra* note 12.

284 *Id*.

285 *Id*.

286 *Id*. (stating that no members of the Committee "shall be currently serving as a Regional Director, Associate Regional Director, Executive Director, Director of the Office of Small Credit Union Initiatives, or Senior Policy Advisor of Chief of Staff to a Board Member").

287 *See id*.

288 *See* Sara Snell Cooke, Editor's Column, *The Absence of Light Causes Darkness*, CREDIT UNION TIMES MAG., Nov. 7, 2012, at 4 (stating that when the Credit Union Times reported the name of the Chairman of the Supervisory Review Committee, the NCUA ask the Credit Union Times to remove the information from the Internet).

289 NCUA, Guidelines for the Supervisory Review Committee, 76 Fed. Reg. 23,871, 23,872 (Apr. 29, 2011).

290 NCUA, Supervisory Review Committee, http://www.ncua.gov/Resources/CUs/Pages/SRC.aspx (last visited Mar. 2, 2014) (listing Joy Lee, Special Assistant to the Executive Director, Gerard Poliquin, Secretary of the Board, and Judy Graham, Program Officer as members of the committee).

contain an attorney[291] as well as former credit union examiners. Most Committee members serve only one or two years.[292]

Perhaps the most novel part of the NCUA appeals process is the scope of appealable determinations. Under NCUA's policy statement, appealable MSDs include: "(1) Composite CAMEL ratings of 3, 4, and 5 and all component ratings of those composite ratings; (2) adequacy of loan loss reserve provisions; and (3) loan classifications on loans that are significant as determined by the appealing credit union."[293]

On the one hand, the NCUA's scope of appealable matters is narrow. Under the policy statement, credit unions can only appeal a component CAMELS rating if the overall composite CAMELS rating is a 3, 4, or 5. So, for example, a credit union that received a 3 management rating could not appeal that rating if the credit union received a composite rating of 1 or 2.[294]

On the other hand, in some respects the scope of appealable matters is quite broad. The Supervisory Review Committee can review loan classifications if the *appealing credit union* considers the classification significant.[295] Moreover, a credit union's right to appeal is not cut off if NCUA imposes formal or informal enforcement action on the credit union.[296] However, in those circumstances, the credit union must comply

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[291] Attorneys who have served on the committee include: John Ianno (Trial Attorney, 1995), Sheila Albin (Associate General Counsel, 1996-97), Hattie Ulan (Special Counsel to the General Counsel, 1998-2000), Chrisanthy Loizos (EEO Counselor, 2003-05), Regina Metz (Staff Attorney, 2006-07), Linda Dent (Staff Attorney, 2008), Ross Kendall (Trial Attorney, 2009-10, 2012-2013), and Gerard Poliquin (Sr. Trial Attorney, 2011). Letter from Regina Metz, Staff Attorney, NCUA to Author (Mar. 22, 2013) (on file with author) (responding to a FOIA request for members and titles for the NCUA Supervisory Review Committee). None of the attorneys has served as chair of the committee. *Id.*

[292] *Id*.

[293] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[294] Lee Interview, *supra* note 12.

[295] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf (emphasis added); Lee Interview, *supra* note 12 (noting that appealing credit unions can "determine if they feel like it's a material size loan or not").

[296] According to Supervisory Review Committee Chair Lee, there is "really no connection" between enforcement actions and the right to appeal an MSD. "Anybody can [appeal]. It doesn't matter if you have a regional director letter, a preliminary warning letter, a letter of understand and agreement, or cease-and-desist." Lee Interview, *supra* note 12.

with the enforcement action while the appeal is pending,[297] and a reversal of the MSD would not necessarily terminate the enforcement action.[298] Nevertheless, an enforcement action does not preclude review of an MSD by the Committee.

In deciding the appeal, the Committee has "free rein" to "talk to anybody" that would provide useful information, including the original examiner or other experts within the NCUA.[299] However, the Committee members have not, to date, visited an appealing credit union.[300] The appealing credit union is "entitled to a personal appearance before the Committee."[301] The credit union can choose whether to allow directors or executives to present their case or whether to employ attorneys.[302] In the last few years, the NCUA has made an effort to formalize this "appearance," making it a court-like process.[303] A court reporter transcribes the proceedings and the Committee goes "off the record and on the record."[304] The Committee also questions the credit union.[305]

After the appearance, the Committee members meet to discuss the appeal and reach a decision.[306] The NCUA policy statement does not specify what standard of review the SRC should use in evaluating appeals. Joy K. Lee, the current Chairman of the NCUA Supervisory Review Committee, explains the standard of review as follows:

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[297] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[298] According to Supervisory Review Committee Chair Lee, if the committee during the appeals process found a significant error, the NCUA would have to revisit the need for the enforcement action, but termination of the enforcement action would not be "automatic." Lee Interview, *supra* note 12 (noting that this circumstance has not yet arisen at the NCUA).

[299] *Id*. (describing circumstances where the committee chair spoke with an examiner, a supervisory examiner, a chief accountant, and a record keeping specialist).

[300] *Id*.

[301] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf (allowing the "personal appearance" to be held "through teleconference").

[302] *See* Lee Interview, *supra* note 12.

[303] *Id*.

[304] *Id*.

[305] *Id*. (stating that the Committee generally asks "very limited questions").

[306] *Id*. (explaining that the meeting might be immediately after the appearance or on a later date, depending on the length of the appearance).

> I view myself as a completely independent party. And so I look at it like it's a brand new thing. I don't totally go with whatever the examiner said and I just don't, you know, completely just say, "Well, this is the examiner's deal, the regional director's determination, so I'm not going to open my eyes to the credit union." I don't. I really and truly look at this as an independent authority, and I look at both sides of the coin, and try to understand, you know, the reasons why for both parties.[307]

Ms. Lee also noted that she has broad investigative power to talk with those at the credit union and within the NCUA.[308]

Once the Committee has reached a conclusion, it drafts and edits a written decision.[309] Under normal circumstances, the Committee will reach a decision on the appeal within 30 days of the time the credit union filed the appeal.[310] The Committee sends the written decision to the credit union as well as to the Regional Director that oversees the credit union.[311] The decisions are not routinely circulated further within the NCUA[312] or released (even in redacted or summary form) to the general public.[313]

If the appealing credit union is unhappy with the Supervisory Review Committee's decision, it can appeal to the NCUA Board.[314] Board decisions are final.

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307 *Id*.

308 *Id*.

309 *Id*.

310 NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf (noting that the 30-day timeframe is "subject to adjustment by the Committee, whether on its own or upon request of the appellant or the Regional or other office involved.").

311 Lee Interview, *supra* note 12.

312 In cases where the appeal receives media attention, the decision is circulated to the NCUA's public and congressional affairs staff as well as the NCUA Chairman. *Id*.

313 The NCUA released redacted decisions in response to my FOIA request. Letter from Regina Metz, Staff Attorney, NCUA to author (Sept. 19, 2012). This is the only time decisions have been released. *See* Lee Interview, *supra* note 12 (noting that redacted opinions had been released in response to a single FOIA request).

314 NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

At the NCUA the Inspector General is tasked with resolving allegation of suspected retaliation.[315] According to the policy statement, "[a]ny retaliation by the NCUA staff against a credit union making any type of appeal will subject the employee to appropriate disciplinary or remedial action by the appropriate supervisor."[316] The NCUA recently added language about their non-retaliation policy to the cover sheet that accompanies all examination reports.[317]

2. NCUA Appeals

The NCUA does not publicly release appeals decisions in summary or redacted form. Moreover, for much of its history, the Supervisory Review Committee's recordkeeping was lacking. A 2012 report by the NCUA's Inspector General "determined that the [Supervisory Review Committee] [kept] all of its records in hard-copy format in a cardboard box. During a change in [Committee] chairpersons in late 2011, the outgoing chairperson passed the cardboard box of files to the newly appointed chairperson."[318]

Nevertheless, in response to my FOIA requests, the NCUA provided redacted Supervisory Review Committee decisions.[319] The NCUA also provided a spreadsheet containing information about written "contacts"[320] about MSDs that credit unions filed with NCUA Regional Offices.[321] The spreadsheet shows the year the credit union contacted the Regional Office, whether the credit union was a federal or state-chartered

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[315] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[316] *Id*.

[317] Mary Dunn, *NCUA Responding to CU Exam Issues*, CREDIT UNION TIMES MAG., June 2012, at 59 (noting that a credit union trade group had received a letter from the NCUA stating that "as a result of your input, we will add specific language on the exam report cover page to emphasize NCUA's non-retaliation policy").

[318] NCUA OIG REPORT, *supra* note 11, at 25. The NCUA

[319] *See* Letter from Regina Metz, Staff Attorney, NCUA, to author (Sept. 19, 2012) (on file with author); Letter from Regina Metz, Staff Attorney, NCUA, to author (July 19, 2013) (on file with author).

[320] As previously explained, the NCUA describes the first stage of its review process as "contact with the regional office" rather than as an appeal. *See supra* note 275-277 and accompanying text. Consequently, I have used the "contact" language throughout this section when describing appeals to Regional Offices.

[321] Letter from Regina Metz, Staff Attorney, NCUA, to author (Sept. 16, 2013) (on file with author).

credit union, the general subject matter of the contact, the Region's actions, and whether an appeal was filed with the Supervisory Review Committee. Data in the spreadsheet begin in 2002.

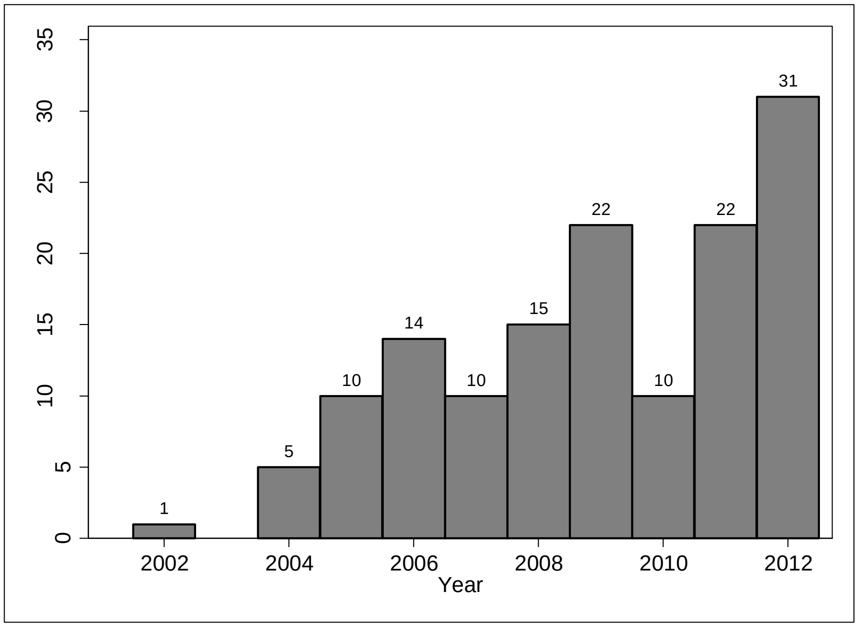
The FOIA information provided shows 140 total Regional Office contacts. As illustrated in Figure 11, the NCUA-provided data show an upward trend in the number of contacts per year. There are several possible explanations. First, information about early contacts may be incomplete. Although my FOIA request sought information on regional office contacts beginning on January 1, 1995, the information provided began in 2002. Information about earlier contacts may not have been kept, or, if it was kept, was subsequently destroyed.[322] Second, the financial crisis beginning in 2008 could have led to more appeals.[323] Third, the NCUA has recently undertaken an effort to publicize its process for appealing MSDs.[324] This may have increased credit unions' utilization of the appeals process.

[322] Additionally, 2 Supervisory Review Committee decisions (2008 and 2012) do not seem to appear on the NCUA's list of regional office contacts. Perhaps the credit union simply did not approach the regional office (*see supra* note 275-277 and accompanying text), or perhaps this information was missing from the information provided.

[323] Lee Interview, *supra* note 12 (noting the financial crisis had increased appeals and that credit unions tended to "lag behind the banks in terms of financial crisis").

[324] *See* Lee Interview, *supra* note 12; Ulan Interview, *supra* note 17. *See also* Letter from Debbie Matz, Chairman, NCUA to Federally Insured Credit Unions (Jan. 2013), *available at* http://www.ncua.gov/Resources/Documents/LCU2013-01.pdf) (noting that "information on all formal and informal appeal options available to credit unions is now included in the exam report cover letter").

Figure 11: NCUA Material Supervisory Determination Contacts Filed with a Regional Office (2002-2012)



Which credit unions initiated contacts? Of the 140 contacts, 126 (90 percent) were made by credit unions with a federal charter, and only 14 (10 percent) were made by credit unions with a state charter. Although the disparity seems large, there are almost twice as many federal credit unions as there are state credit unions.[325] In addition, the NCUA does not annually conduct examinations at each state-chartered credit union; it examines only those credit unions with the most risk.[326] Finally, until recently, the NCUA did not release its examination ratings of state-chartered credit unions to the credit unions themselves.[327] Each of these factors explains why more federal credit unions that state credit unions contact regional offices regarding MSDs.

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[325] *See supra* note 267.

[326] *See supra* note 17.

[327] Letter from Debbie Matz, Chairman, NCUA to Federally Insured Credit Unions (Aug. 2011), *available at* http://www.ncua.gov/Resources/Pages/LCU2011-12.aspx (NCUA Letter 11-CU-12).

Figure 12: NCUA Material Supervisory Determinations Prompting Contact with Regional Office (2002-2012)[328]

Reason for Appeal	**Number**
CAMEL Composite or Component Ratings	65
Document of Resolution	47
Examiner Findings / Examination Findings	20
Report of Examination / Report Wording	14
Examiner Conduct (including Examiner Communication)	11
Risk Rating	4
Insurance Review Examination Rating	3

Figure 12 summarizes issues raised by at least two Regional Office contacts. As with the OCC, Federal Reserve, and FDIC, disagreement over CAMEL composite or component ratings was the most common reason that credit unions used the MSD appeals process. Additionally, 47 appeals involved a document of resolution, an enforcement tool used by examiners encouraging the credit union to agree with recommended remedial actions.[329] Because the NCUA provided this information in spreadsheet form, little else is know about the substance of these appeals.

When credit unions do contact the Regional Office, they rarely succeed in overturning the initial examination determination. Seventy percent of Regional Office contacts resulted in a decision that upheld the initial examiner decision.[330] Less than 20 percent (25/140) of Region Office contacts resulted in an amendment to the MSD made by the initial examiner.

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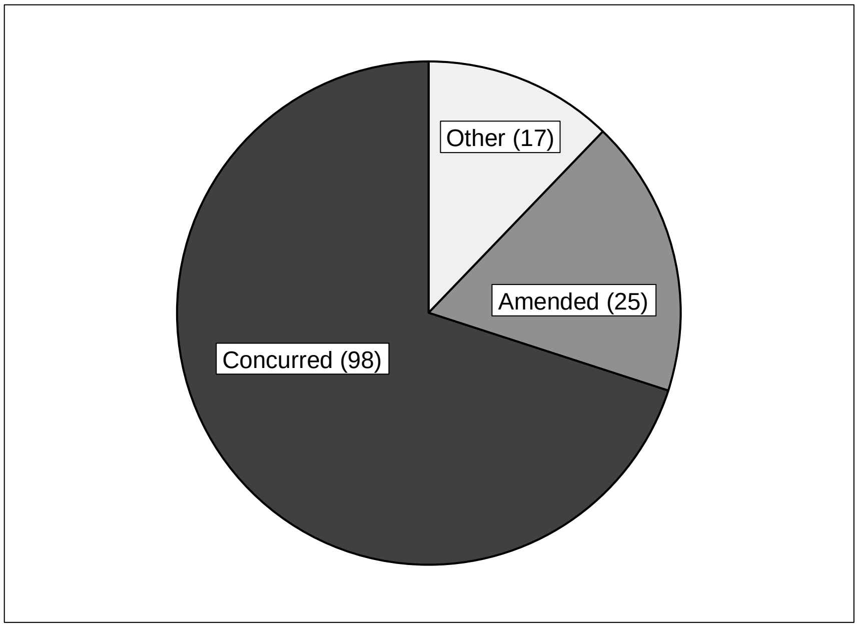
[328] Data for this figure were compiled from NCUA-provided summaries of regional office contacts. As such, it contains the issues as characterized by the NCUA.

[329] NCUA, EXAMINER'S GUIDE 20-4 (2004), *available at* http://www.ncua.gov/Legal/GuidesEtc/ExaminerGuide/chapter20.pdf (describing documents of resolution)

[330] Outcome data for regional office contacts were compiled from the FOIA-provided summary of regional office contacts. *See supra* note 320-321 and accompanying text (describing these data). "Amended" refers to those instances where the appeals process reversed the examiner decision in whole or in part. As such, it is the combination of the "reversed" and "mixed" data categories reported for OCC, Federal Reserve, and FDIC appeals. *See supra* Figures 3, 6, and 10. The "Other" category consists of contacts that the NCUA described as "resolved" (1), "reevaluated" (1), "addressed" (11), "explained" (2), and "updated" (2).

Figure 13: Outcomes of NCUA Material Supervisory Determination Appeals Process (2002-2012)



In spite of the low rate of credit union success at the Regional Office contact level, there are few appeals filed with the NCUA's Supervisory Review Committee. The Committee issued only 6 decisions between 1995 and 2012.[331] Five appeals concerned CAMEL composite or component ratings.[332] In each of those cases, the Committee upheld the examiner decisions. In one of those cases, the credit union also alleged that "agency field staff require[d] [the credit union] to submit additional monthly reporting information in retaliation for a complaint lodged by the credit union against a supervisory examiner." On that issue, the Committee concluded that "the Region's material supervisory determination was based upon objective criteria." Thus, the complaint of retaliation

[331] Complete information for 2013 is not available. Preliminary information shows that the Committee issued at least three decisions in 2013. These decisions involved appeals of CAMEL composite and component ratings and resulted in decisions upholding the initial examiner decision. This is consistent with the increase in regional office contacts illustrated in Figure 11.

[332] In most cases, the NCUA redacted the numerical ratings (1-5) that the credit union received from the appeals decisions before releasing the decision through FOIA.

was "not within the purview of the [Committee]."[333] The single non-CAMEL appeal involved a $5,000 grant reimbursement denial by the Office of Small Credit Union Initiatives. There the Committee overturned the previous decision and granted reimbursement. Only one MSD appeal has been filed with the NCUA Board, and it was withdrawn before the Board issued a decision.[334]

III. WEAKNESSES IN THE APPEALS PROCESSES

Analysis of the MSD appeals processes shows significant weaknesses. This section will address three weaknesses in more detail: (1) the lack of consistency among regulators, (2) the small number of appeals, and (3) the lack of transparency regarding appeals.

A. Variations Among Regulators

First, there are significant differences among the MSD appeals processes used by each regulator. This is true even though regulators, at the urging of Congress, generally strive for consistency in the examination process.[335] Any time four separate regulators implement a single statute, differences are likely to arise. While policies should be tailored to meet the unique structure of the agency and the nature of the regulated institutions, policies should not advantage or disadvantage financial institutions based solely on the institutions' primary federal regulator. Regulatory decisions regarding the scope of appealable items and the standard of review used when evaluating an appeal have the potential to significantly

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[333] It is possible that the Committee appeals contained additional issues, but the decisions have been redacted so heavily it is impossible to tell. The press widely reported that Commodore Perry Federal Credit Union brought an appeal alleging that "its examiner retaliated by reporting inaccurate exam findings because management complained to the NCUA that he sexually harassed and bullied [Credit Union] employees." Heather Anderson, *Ohio CU's Appeal*, CREDIT UNION TIMES (Oct. 31, 2012), *available at* 2012 WLNR 23050051. The redacted Committee decisions from this time period do not discuss any retaliation issues. Of course, it is also possible that the press reports simply do not match the information contained in the credit union's appeal.

[334] Heather Anderson, *Commodore Stops Appeal*, CREDIT UNION TIMES (Apr. 3, 2012), *available at* 2013 WLNR 8114836 (noting that a credit union had filed, but then withdrawn a Board-level appeal); Lee Interview, *supra* note 12 (stating the Board had never decided an appeal).

[335] Congress created the Federal Financial Institutions Examination Council in 1979 to "prescribe uniform principles and standards for the Federal examination of financial institutions . . . and to make recommendations to promote uniformity in the supervision of these financial institutions." 12 U.S.C. § 3301. Working together as part of the Examination Council, officials from each regulator developed the CAMELS system. *See supra* notes 18-20 and accompanying text. To ensure that the CAMELS system is consistently implemented across each of the federal regulators, the Examination Council "conduct[s] schools for examiners and assistant examiners." 12 U.S.C. § 3305(d).

alter the substantive rights of financial institutions. Such differences are inconsistent with Congressional and regulatory policies promoting uniformity.

1. Scope of Appealable Matters

Congress required that regulators provide a process for appealing "material supervisory determinations." Regulators disagree as to what this means. This section will focus on two key differences: (1) differences in the appealability of examination ratings and (2) differences in the appealability of MSDs related to enforcement actions. In both of these cases, differences in the scope of appealable matters mean that some financial institutions have greater access to an appeals process than others.

a. CAMELS Ratings

Congress defined MSD to include "examination ratings."[336] The OCC, Federal Reserve, and FDIC allow financial institutions to appeal any examination rating.[337] The NCUA, however, only allows appeals of "composite CAMEL ratings of 3, 4, and 5 and all component ratings of those composite ratings."[338] That means a credit union with a composite CAMEL rating of 2 and a management rating of 3 or 4 cannot appeal either the composite rating or the management rating.[339] Yet such appeals have been heard by both the OCC and FDIC.[340] Credit unions, thus, have less access to an appeals process.

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[336] 12 U.S.C. § 4806.

[337] The OCC policy allows appeal of "[e]xamination ratings." OCC Bulletin 2013-15 (June 7, 2013). The Federal Reserve policy defines "material supervisory determination" to include "examination or inspection composite ratings" (*see* Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,473 (1995)) and the information provided shows appeals for CAMELS composite and component ratings. The FDIC policy allows appeals of CAMELS ratings, IT ratings, trust ratings, CRA ratings, and consumer compliance ratings. FDIC Intra-Agency Appellate Process, 77 Fed. Reg. 17,055, 17,057 (2012).

[338] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[339] Lee Interview, *supra* note 12.

[340] *See, e.g.*, Appeal of Composite and Component Rating, 25 No. 1 OCC Q.J. 37 (2006); Appeal of the CAMELS Component Ratings for Asset Quality and Management, SARC-2004-02, http://www.fdic.gov/regulations/laws/sarc/sarcappeals/sarc200402.html (Apr. 12, 2004). Although the Federal Reserve's guidelines are worded broadly enough to allow appeals from institutions with a 1 or 2 composite rating, the data gathered through FOIA are insufficient to confirm that the Federal Reserve has actually considered appeals from such institutions.

b. Enforcement-Related Determinations

The handling of MSDs related to enforcement actions is even more fractured. Congress specified that MSDs do not include regulators' decisions to close financial institutions or take prompt corrective action, including the removal of officers and directors, from undercapitalized institutions.[341] Congress added that the MSD appeals process does not "affect the authority of an appropriate Federal banking agency or the National Credit Union Administration Board to take enforcement or supervisory action."[342] While this seems to preclude using the MSD appeals processes to directly challenge prompt corrective action directives, it gives regulators leeway in dealing with determinations related to formal or informal enforcement actions.

OCC-regulated banks can use the MSD appeals process to challenge findings that a bank has not complied with an enforcement action.[343] In addition, an OCC-regulated bank can challenge CAMELS ratings and other MSDs while under an enforcement action,[344] but cannot challenge "the underlying facts that form the basis of a recommended or pending formal enforcement action and the acts or practices that are the subject of a pending formal enforcement action."[345]

The Federal Reserve policy states that its MSD appeals process cannot be used to appeal "prompt corrective action directives . . . actions to impose administrative enforcement actions . . . , capital directives, and orders issued pursuant to applications under the [Bank Holding Company] Act."[346] However, in one instance the Federal Reserve heard an appeal about whether a memorandum of understanding should remain in effect and in another instance evaluated the accuracy of an examination finding that a bank had not complied with an enforcement action.

341 *Id*. at § 4806(f)(1)(B) (citing 12 U.S.C. §§ 1830o, 1790a).

342 *Id*. at § 4806(g).

343 OCC Bulletin 2013-15 (June 7, 2013). Earlier OCC policies did not allow banks to use the MSD appeals process to challenge examiner findings that the bank did not comply with an enforcement action. *See* Appeal of Composite and Component Ratings and Violations of Law (Second Quarter 2012), http://www.occ.gov/topics/dispute-resolution/bank-appeals/summaries/appeal-composite-component-ratings-q2-2012.html.

344 *See supra* note 95 and accompanying text. Under the OCC's initial MSD appeals procedures, banks had more leeway to appeal MSDs underlying enforcement actions. *See* Golden Interview, *supra* note 12; *Hearing on H.R. 3461*, *supra* note 5, at 53 (testimony of Eugene A. Ludwig, Founder & CEO, Promontory Financial Group, LLC).

345 OCC Bulletin 2013-15 (June 7, 2013).

346 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16.473 (1995).

The FDIC's policy is the most restrictive. It explicitly prohibits appeals of formal enforcement actions as well as "determinations and the underlying facts and circumstances that form the basis of a recommendation or pending formal action" and "determinations regarding compliance with an existing formal enforcement action."[347] Furthermore, FDIC does not allow appeals of "decisions to initiate informal enforcement actions (such as memoranda of understanding)."[348]

The NCUA's MSD appeals policy states that it is not available for "appeals of various administrative and enforcement actions."[349] Joy Lee, Chair of the NCUA's Supervisory Review Committee, explains that an enforcement action does not cut off a credit union's right to use the MSD appeals process; credit unions can still challenge facts that relate to the enforcement action.[350]

In sum, regulators reach different conclusions about whether financial institutions can appeal the facts and determinations underlying enforcement actions and about whether institutions can appeal a determination that the institution is not in compliance with an enforcement action.

2. Standard of Review

There is also disagreement and general confusion among regulators about the standard of review for evaluating MSD appeals. "Standard of review" refers to the level of deference the appellate authority affords the earlier decision maker. Possible standards of review range from the deferential "abuse of discretion" standard to the non-deferential "*de novo*" standard.[351] Because changing the standard of review adjusts deference

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[347] FDIC Intra-Agency Appeals Process, 77 Fed. Reg. 17,055, 17,058 (2012). Earlier FDIC policies were not so restrictive. *Id*. at 17,056 (noting the FDIC policy was amended in 2008 "to modify the supervisory determinations eligible for appeal to eliminate the ability of an FDIC-supervised institution to file an appeal with the SARC for determinations, or the facts and circumstances underlying a recommended or pending formal enforcement-related action or decision, and to make limited technical amendments.").

[348] *Id*. at 17,058.

[349] NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

[350] *See supra* note 296-298 and accompanying text.

[351] *See* Amanda Peters, *The Meaning, Measure, and Misuse of Standards of Review*, 13 LEWIS & CLARK L. REV. 233, 243-46 (2009) (explaining that in *de novo* review the appellate body simply reviews the issue anew while in abuse of discretion review the appellate body uses a much higher threshold such as whether the initial decision was "outside the scope of the applicable law").

given to the earlier determination, the Supreme Court has acknowledged that the standard of review used could make a practical difference in the outcome of a case.[352] Thus, financial institutions that are allowed to appeal using a non-deferential standard of review could have a much better chance of success than those appealing under a more deferential standard. The Reigle Community Development and Regulatory Improvement Act of 1994 does not specify a standard of review for the appeals processes. Without direction, regulators have adopted widely differing standards.

The OCC policy states that "the appeal is limited to a consideration of whether the examiners appropriately applied agency policies and standards."[353] The current OCC Ombudsman says this approach is a "standard-based" review that does not give "deference to either side."[354] The inaugural OCC Ombudsman described the standard of review as *de novo*.[355]

The Federal Reserve, while stating that it wanted all institutions to "receive the same appellate rights regardless of the Federal Reserve district in which they reside," did not adopt an agency-wide standard of review.[356] Left to their own judgment, regional Federal Reserve Banks provide a potpourri of standards of review from *de novo* in New York, to *ad hoc* (but specifically not *de novo*) standards set by each review panel in Minneapolis and Kansas City, to no stated standard in other regions.[357]

The FDIC "review[s] the appeal for consistency with the policies, practices, and mission of the FDIC and the overall reasonableness of, and the support offered for, the positions advanced."[358]

Neither the NCUA MSD appeals policy nor the appeals decisions themselves provide a statement on the appropriate standard of review. Joy Lee, Chair of the NCUA's Supervisory Review Committee, de-

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352 Dickinson v. Zurko, 527 U.S. 150, 162 (1999) ("The upshot in terms of judicial review is some practical difference in outcome depending upon which standard is used."). *But see, e.g.*, David Zaring, *Reasonable Agencies*, 96 VA. L. REV. 2317 (2010) (finding that "regardless of the standard of review, courts affirm agencies' actions slightly more than two thirds of the time").

353 OCC Bulletin 2013-15 (June 7, 2013).

354 *See supra* notes 108-110 and accompanying text.

355 *See supra* notes 106-107 and accompanying text.

356 Federal Reserve, Internal Appeals Process, 60 Fed. Reg. 16,470, 16,473 (1995).

357 *See supra* notes 177-181 and accompanying text.

358 FDIC Intra-Agency Appeals Process, 77 Fed. Reg. 17,055, 17,058 (2012)

scribes a review process that does not give deference to either credit union or the examiner.[359]

B. Few Appeals

Another shortcoming of the current MSD appeals processes is that there are few appeals. Thousands of financial institutions have been examined every year since regulators adopted MSD appeals policies in 1995. Yet the OCC Ombudsman has issued 157 decisions, the Federal Reserve has decided 25 appeals (although data from 1995-2000 are unavailable for the Federal Reserve), the FDIC's Supervision Appeals Review Committee has issued 63 decisions, and the NCUA's Supervisory Review Committee has issued 6 decisions.[360] One regulator has touted the small number of appeals as evidence that institutions are happy with the examination process and that examiners make few mistakes.[361] There is, however, reason to believe this view is overly optimistic.

Surveys suggest that financial institutions would like to appeal MSDs far more often than they actually do. In 2011, the Alliance of Bankers Associations, in connection with the American Bankers Association, conducted a nation-wide survey questioning banks about their most recent examination. The survey, which received more than 1,000 responses, asked banks to rate satisfaction with the most recent examination and results on a 1 to 5 scale with 1 being very satisfied and 5 being very unsatisfied. More than 30 percent of responding banks were unsatisfied or very unsatisfied.[362] Respondents were also asked to evaluate

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[359] *See supra* notes 307-308 and accompanying text.

[360] The number of appeals at the FDIC and NCUA is somewhat larger if you consider appeals to or contacts with officials housed within the regulators' examination functions (Director or Regional Office appeals). *See supra* Figures 8 and 11. But even considering these early-stage appeals, utilization of the MSD appeals processes seems low.

[361] Heather Anderson, *Marquis: Lack of Appeals a Sign that Exam System Is Working*, CREDIT UNION TIMES, July 6, 2012, *available at* 2012 WLNR 14198420 ("The fact that only four credit unions have elevated an exam appeal to the NCUA's supervisory review committee in the past 10 years is a sign the exam system is working, [NCUA] Executive Director David Marquis told Credit Unions Times.").

[362] AM BANKERS ASS'N & STATE BANKERS ASS'NS, SUMMARY REPORT FROM THE BANKS SUPERVISED BY THE OFFICE OF THE COMPTROLLER OF THE CURRENCY 5 (Mar. 14, 2012), *available at* http://www.aba.com/aba/documents/news/ReportforOCCMarch2012.pdf (N=203, 10% very dissatisfied, 23% dissatisfied, 17% neutral, 32% satisfied, 18% very satisfied); AM. BANKERS ASS'N & STATE BANKERS ASS'NS, SUMMARY REPORT FOR THE FEDERAL RESERVE (Mar. 14, 2012), *available at* http://www.aba.com/aba/documents/news/ReportforFedMarch2012.pdf (N=133, 15% very dissatisfied, 20% dissatisfied, 17% neutral, 26% satisfied, 21% very satisfied); AM. BANKERS ASS'N & STATE BANKERS ASS'NS, SUMMARY REPORT FOR BANKS EXAMINED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION (Apr. 19, 2012), *available at*

agreement with the assigned CAMELS rating on the same 1 to 5 scale. That question yielded an average of 3.38,[363] evidencing some disagreement with examination ratings.

Moreover, surveys of credit unions produced similar results. In 2010, the Credit Union National Association conducted a survey in which "27% of respondents reported dissatisfaction with their most recent exam."[364] Moreover, "one-in-five (21%) [of the responding credit unions] indicated that they wanted to appeal but did not."[365] "Two-thirds of the credit unions that wanted to appeal indicated they did not appeal for fear of retaliation by examination staff. Nearly the same number indicated they did not appeal because they did not believe it would make a difference in outcome."[366]

The Credit Union National Association performed a second survey about the examination process in 2012. While it did not specifically ask about the MSD appeals process, it did ask about credit unions' agreement with examination results. The survey found that 25 percent of respondents were unhappy with their most recent examination and results.[367] In addition, 22 percent of respondents expressed dissatisfaction with their current CAMEL rating.[368]

These surveys are not without their faults.[369] Each of the surveys relied on financial institutions voluntarily completing the survey form. Those dissatisfied with the examination process may have been more motivated to complete the survey. Thus, it may not be possible to extrap-

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http://www.aba.com/aba/documents/news/ReportforFDICApril2012.pdf. (N=397, 13% very dissatisfied, 21% dissatisfied, 17% neutral, 31% satisfied, 17% very satisfied). *See also* Joe Adler, *Banker-Examiner Relationship, Once Testy, Thaws*, AM. BANKER, June 11, 2012, *available at* 2012 WLNR 12040228 (reporting on the survey).

363 Adler, *supra* note 362.

364 *Hearing on H.R.* 3461, *supra* note 5, at 150 (written statement of Ken Watts, President and CEO, West Virginia Credit Union League) (citing a Credit Union National Association survey).

365 *Id.*

366 *Id.* Additionally, "[o]ver one-third of the credit unions who had examination concerns did not appeal because they were not aware of the process." *Id*.

367 CREDIT UNION NATIONAL ASSOCIATION, 2012 CREDIT UNION EXAMS SURVEY (on file with author) (N=1531, 10% very dissatisfied, 15% somewhat dissatisfied, 15% neutral, 39% satisfied, 21% very satisfied).

368 *Id*. (N=1531, 8% very dissatisfied, 14% somewhat dissatisfied, 17% neutral, 39% satisfied, 23% very satisfied).

369 An FDIC spokesman stated that the Alliance of Bankers Associations survey "has inherent limitations based on geography, sample size and other methodological issues." Alder, *supra* note 362.

olate the survey results to the entire population of financial institutions. Nevertheless, the number of survey respondents that reported dissatisfaction with their examination is far greater than the number of financial institutions that utilized the MSD appeals processes. Thus, while it might not be possible to predict the ideal number of appeals, the survey data suggest the appeal processes are not functioning properly. Some financial institutions believe that appealing is futile. Others fear retaliation.

C. Little Transparency

Finally, the MSD appeals processes are far from transparent. It can be difficult, or even impossible, to get information about appeals decisions. Without transparency it is difficult to realize the objectives Congress sought in mandating MSD appeals processes: correcting "uneven treatment by examiners" and fostering "confidence" in the regulatory process.[370]

Written and regularly disseminated decisions serve several functions. First, they can be a learning tool for regulators themselves. If decisions are public, all regulators can review the decisions and compare them with their current examination practices. How can regulators be expected to achieve any measure of consistency (either within an agency or across agencies) if one regulator has no idea what other regulators are doing?[371] Second, written decisions act as guideposts for financial institutions. Institutions are better able to comply with regulator expectations when they understand what the regulators expect. Third, written decisions give the public a way to evaluate the MSD appeals processes and the examination function overall. As President Obama explains, "[t]ransparency promotes accountability and provides information for citizens about what their Government is doing."[372]

Of course, the OCC and FDIC deserve credit for releasing some appeals decisions. The OCC provides summaries of Ombudsman decisions, and the FDIC provides redacted Supervision Appeals Review

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370 S. REP. NO. 103-169, at 51 (1994), *reprinted in* 1994 U.S.C.C.A.N. 1881, 1935.

371 *Cf.* Patricia M. Wald, *The Rhetoric of Results and the Results of Rhetoric: Judicial Writings*, 62 U. CHIC. L. REV. 1371, 1372 (1995) (asserting that written judicial opinions are a device to "impose consistency and correct the judges who 'err'"). Perhaps some regulatory consistency could be achieved by circulating decisions within an agency and sharing decisions across agencies. However, there is little evidence that regulators do this.

372 Memorandum regarding Transparency and Open Government from Barak Obama, President of the United States, to Heads of Executive Departments and Agencies, 74 Fed. Reg. 4685 (Jan. 21, 2009).

Committee decisions.[373] In both cases, the materials released generally allow readers to determine (1) the reason the appealing bank believes examiners erred, (2) the applicable law, regulation, or agency guidance, (3) and the appellate authority's decision and accompanying reasoning. The Federal Reserve and NCUA are not as forthcoming. Even in response to FOIA requests, the Federal Reserve has never released its opinions.[374] Although the NCUA did release decisions from its Supervisory Review Committee,[375] in many cases the opinions were so heavily redacted it was difficult to determine the precise nature of the controversy, the applicable law (or agency guidance), and the factors influencing the Committee decision.[376]

MSD appeals that result in written decisions by the OCC's Ombudsman, the FDIC's Supervision Appeals Review Committee, and the NCUA's Supervisory Review Committee capture only part of the financial institutions that use the appeals processes. In each of those cases the institution has either the option or the requirement to first pursue an appeal with an agency official who supervised the examination.[377] The decisions reached at these earlier stages of the MSD appeals processes are a near complete black box. No regulator has released any written decision from this stage of the process. Furthermore, no regulator systematically provides summary information about appeals handled at this stage. Do financial institutions appeal? What do they appeal? Do they ever win? What do these decisions teach us about regulatory reasoning? Are these decisions consistent with one another? While I did my best to unravel the answers to these questions through FOIA requests and regulator interviews, much of this stage of the appeals processes remains a mystery.

Secrecy at this early stage of the MSD appeals processes may be especially problematic. These appeals are not addressed by a single appellate authority within each regulator, but are instead handled by a variety of decision-makers. One division, region, or office may decide appeals differently than another division, region, or office. Moreover, because this level of appeal is addressed to an agency official more closely

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373 *See supra* notes 127-130, 250, and accompanying text.

374 *See supra* note 200 and accompanying text.

375 *See supra* notes 319-321 and accompanying text.

376 For example, an NCUA decision contained a paragraph that began: "According to the NCUA's LCU No. 07-CU-12, CAMEL [redacted] credit unions:" The remainder of the paragraph likely contained the NCUA's standard for a 3, 4, or 5 rated credit union. However, the remainder was entirely redacted.

377 *See supra* notes 74-76, 215, 275-277, and accompanying text.

associated with the examination staff, this may be the stage at which the appeal is most likely to induce examiner retaliation.

In sum, the lack of transparency stands as a barrier to consistency and confidence in the examination process.

IV. Strengthening the Appeals Processes

Given the weaknesses in the current MSD appeals processes, I recommend three changes. First, once examiners issue an MSD, financial institutions should have direct access to an appellate authority outside of the examination function. Second, the appellate authority should engage in a robust review; it should consider a broad scope of appealable matters and employ a clear and rigorous standard of review. The scope of review and standard of review should be consistent across regulators. Third, regulators should release detailed information about each decision reached by the appellate authority. This Part will discuss these recommendations in more detail, but one of the virtues of these suggestions is that they could all be implemented voluntarily by the regulators. Congressional action would not be required.[378] This Part will also address a more drastic proposal that would require Congressional action: the creation of a single super-Ombudsman for all financial institution MSD appeals.

A. Strengthened Independence of Review

Once examiners issue an MSD, financial institutions should have direct access to a dedicated appellate authority outside of the examination function. The OCC is currently the only regulator to provide this access; OCC-regulated banks can appeal directly to the Ombudsman.[379] FDIC-regulated banks and credit unions first address an appeal to an official who oversees the examination function.[380] Federal Reserve-regulated institutions first address an appeal to an *ad hoc* committee that changes with each appeal.[381] I propose that FDIC-regulated banks be allowed to appeal directly to the Supervision Appeals Review Committee and credit unions be allows to appeal directly to the Supervisory Review Committee. I propose that the Federal Reserve create an appellate authority to review MSDs. The appellate authority should consist of a per-

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[378] Of course, Congress could also choose to impose these requirements.

[379] OCC Bulletin 2013-15 (June 7, 2013).

[380] *See supra* note 377.

[381] *See supra* notes 163-164 and accompanying text.

son or group of persons who are not part of the examination function. Moreover, membership of the appellate authority should be consistent and not change with each appeal.

The benefits of direct access to a dedicated appellate authority outside the examination function are threefold. First, consistent decisions are more likely to come from a single appellate authority (whether consisting of an individual or a small group) than from a number of different individuals who do not deliberate together (as is the case when appeals are first routed through division, region, or office directors).

Second, a single appellate authority promotes transparency. Regulators do not regularly release any information about early-stage appeals that are routed to a division, region, or office director. Perhaps this is partly because these officials are so connected with the examination function that they presume complete secrecy is preferable. Allowing appeals to instead begin with a dedicated appellate authority outside the examination function may facilitate public release of summary or redacted opinions. A dedicated appellate authority outside the examination function may be better able to balance protection of information that could lead to banking runs with disclosure of information that could improve the examination function. Indeed, the OCC Ombudsman and FDIC Supervision Appeals Review Committee (appellate authorities outside the examination function) already strike a reasonable balance when they release their decisions.

Third, a more independent appellate authority may increase bank confidence in the MSD appeals processes. Financial institutions that disagree with an MSD may view the regulator's examination function with suspicion. Assigning the first step of the examination function to examination officials does little to assuage this concern. Institutions would likely view a dedicated appellate authority outside the examination function as more independent, particularly if that authority publicly disclosed its decisions. The OCC gives its banks the choice of filing with the Ombudsman or the Deputy Comptroller of the supervisory district that oversees the bank.[382] Current Ombudsman Hattix estimates that about eighty percent start directly with the Comptroller.[383] This suggests most banks prefer the appellate authority outside the examination function.

382 OCC Bulletin 2013-15 (June 7, 2013).

383 Hattix Interview, *supra* note 12.

B. Robust Review Authority

Next regulators should empower their appellate authorities to conduct robust reviews of MSDs. Each appellate authority should consider a broad scope of appealable matters. Furthermore, in considering appeals, the appellate authority should employ a consistent and robust standard of review.

1. Broad Scope of Appealable Matters

Financial institutions should be able to use the MSD appeals processes to challenge a wide variety of MSDs. All regulators should define appealable MSDs to include any examination rating. In addition, institutions should be able to appeal some enforcement action-related MSDs.

a. Examination Ratings

The NCUA is the only regulator to restrict institutions' ability to appeal examination ratings.[384] The NCUA allows appeals of CAMEL ratings (composite and component) only when the composite rating is 3, 4, or 5.[385] The NCUA defends excluding credits unions with a 1 or 2 CAMEL composite rating by noting that these credit unions have little reason to appeal.[386] Yet banks have appealed CAMELS 2 ratings.[387] These banks may be worried that unless errors are corrected early, the misunderstanding will eventually lead to further ratings downgrades and enforcement actions. At any rate, even the NCUA would likely concede that allowing appeals from 1 and 2 rated credit unions is unlikely to flood the NCUA's seldom-used system. The NCUA should allow appeals on par with other financial institution regulators.

b. Enforcement-Related Determinations

There is little agreement among regulators about the extent to which institutions can use the MSD appeals processes to challenge determinations related to informal or formal enforcement actions.[388] The

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384 *See supra* Part III.A.1.a.

385 NCUA, Interpretive Ruling and Policy Statement 11-1 (Supervisory Review Committee) (as amended by Interpretive Ruling and Policy Statement 12-1) (2012), *available at* http://www.ncua.gov/Legal/Documents/IRPS/IRPS2011-1.pdf.

386 Ulan Interview, *supra* note 12 (stating that "in practical terms, it doesn't matter whether [a credit union is rated] a 1 or a 2").

387 *See supra* note 340.

388 *See supra* Part III.A.1.b.

issue, however, is important. Regulators typically place institutions that receive a 3, 4, or 5 composite CAMELS rating under informal or formal enforcement action.[389] Although there are processes for contesting formal enforcement actions,[390] doing so is costly and actions are reviewed under standards deferential to the regulator. Thus, most banks do not challenge enforcement actions.[391] All informal enforcement actions[392] and the vast majority of formal enforcement actions are entered by consent.[393] In those circumstances, institutions have little opportunity to correct examiner mistakes. And by excluding enforcement-related determinations from the MSD appeals processes, regulators significantly restrict the usefulness of the processes. For this reason, Eugene A. Ludwig, a former Comptroller of the Currency, proposes that financial institutions be allowed to use the MSD appeals processes for issues related to enforcement actions.[394]

My proposal is more specific. I suggest that institutions be able to use the MSD appeals processes for any material finding or decision underlying an informal or formal enforcement action entered by consent. Institutions should also be able to use the MSD appeals processes to challenge findings that the institution has not complied with an existing enforcement action, unless the regulator is currently asking a court to enforce the existing enforcement action. In either case, the regulator would not be constrained in its ability to pursue an enforcement action and any enforcement action would remain in force during the pendency of the MSD appeal.

389 Rives, *supra* note 23. *See also* 12 U.S.C. § 1818(b)(8) (allowing regulators to impose formal enforcement when an institution receives "a less-than-satisfactory rating for asset quality, management, earnings, or liquidity").

390 *See* 12 U.S.C. § 1818(b), 1831o.

391 *See supra* note 37.

392 Hill, *supra* note 23, at 663 (explaining that "regulators acknowledge that they have informal regulatory powers" to convince banks to willingly enter informal enforcement actions like board resolutions, commitment letters, safety and soundness plans, and memoranda of understanding).

393 *See id*. at 675 (finding that 90 percent of formal capital enforcement actions between 1993 and 2010 were entered with the consent of the bank).

394 Ludwig, *supra* note 42, at 9 ("If the ombudsman cannot delve into enforcement matters, he or she is precluded from getting into a whole variety of issues that could involve mistakes. Furthermore, matters involving enforcement actions typically are of great importance to the regulated financial institution. A second pair of eyes in such important cases not only avoids unnecessary harm but also enhances the agency's stature as a place of probity and fairness.").

I further propose that if the appellate authority decides that one or more MSDs were erroneous, top regulatory officials[395] would consider whether the enforcement action should be withdrawn. If the regulator chooses not to lift the enforcement action, the institution should be given the option to withdraw its consent to the action.[396] The regulator could then pursue formal enforcement actions under existing statutory authority, including statutes that allow for temporary orders without pre-order hearings in high-risk cases.[397] In less urgent cases (such as when a regulator seeks a cease-and-desist order for an unsafe or unsound condition), the institution could contest the action through the hearing process.

In the past, regulators have resisted proposals to allow appeals of enforcement action-related MSDs, claiming that such appeals would dangerously delay the enforcement process.[398] My proposal, however, does not affect enforcement authority; it allows regulators the same essential tools they have now. It only provides a mechanism for institutions to ask regulators to reconsider underlying MSDs. In addition, both the OCC and FDIC have, at times, allowed review of MSDs related to enforcement actions.[399] There is no indication that institutions' use of the MSD appeals processes during the time these appeals were allowed hampered enforcement activity.

Regulators assert additional review of enforcement-related MSDs is unnecessary because agency officials already vet enforcement actions, minimizing the chances for regulatory error and overreach.[400] Regulators, however, tend to give the greatest scrutiny to those enforcement actions contested by financial institutions. Top agency officials rarely review or approve enforcement actions entered with an institution's consent. At the FDIC, enforcement action decisions are commonly made by a regional

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[395] I propose that the review of these enforcement actions happen at the highest level within the regulator: the Comptroller of the Currency, the Federal Reserve Board, the FDIC Board of Directors, and the NCUA Board of Directors.

[396] The financial institution's board of directors should vote to approve the institution's withdrawal from the enforcement action.

[397] *See* 12 U.S.C. §§ 1818(c), 1786(f).

[398] FDIC, Intra-Agency Appellate Process, 60 Fed. Reg. 15,923, 15,925-26 (1995) (rejecting suggestion that "decision to initiate informal enforcement actions . . . be appealable" because of "the possible abuse of the appeals process to delay or otherwise impede well-founded enforcement actions").

[399] *See supra* notes 344 and 347.

[400] FDIC, Guidelines for Appeals of Material Supervisory Determinations, 73 Fed. Reg. 54,822, 54,824 (2008) ("All FDIC formal enforcement actions are reviewed by a number of high-level FDIC officials both prior and subsequent to their initiation.").

director or regional counsel.[401] The FDIC's Washington office only becomes involved if the bank requests a hearing.[402] The process is similar at the OCC[403] and Federal Reserve.[404] Since the vast majority of enforcement actions are entered by consent, the internal and opaque vetting processes provide little assurance of consistency.

Finally, regulators note that financial institutions facing enforcement actions already have access to other appeals mechanisms.[405] If an institution is unhappy with an MSD underlying an enforcement action, why not just contest the enforcement action itself? The answer is that contesting an enforcement action is a formal, expensive, and time-consuming process. The institution must hire an attorney to represent it in a formal hearing before an administrative law judge.[406] Following the recommendation decision by the administrative law judge, the regulator issues a "final decision and order based on the entire record proceeding, which is subject to limited review by an appropriate court of appeals."[407] The entire process can take two to five years.[408] During those two to five years, the regulator continues to examine the bank, making additional material supervisory determinations and requesting or demanding addi-

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401 Hill, *supra* note 23, at 705

402 FDIC, Guidelines for Appeals of Material Supervisory Determinations, 73 Fed. Reg. at 54,824.

403 *Examining the Settlement Practices of U.S. Financial Regulators: Hearing Before the H. Comm. on Financial Srvcs.*, 112th Cong. 115-16 (2012) [hereinafter *Settlement Practices Hearing*] (written statement of Daniel P. Stipano, Deputy Chief Counsel, OCC) (explaining that enforcement actions are generally approved by one of several supervision review committees).

404 Letter from Ben S. Bernanke, Chairman, Board of Governors of the Federal Reserve System to Senator Elizabeth Warren & Representative Elijah E. Cummings, Dec. 16, 2013, *available at* http://democrats.oversight.house.gov/uploads/12%2016%2013%20Reply%20to%20Cummings%20%20Warren%201.pdf (stating that of the "nearly 1,000 formal, public enforcements actions the Federal Reserve has taken over the past 10 years" only 11 were contested and therefore approved by the Federal Reserve Board).

405 Board of Governors of the Federal Reserve System, Final Guideline: Internal Appeals Process, 60 Fed. Reg. 16,470, 16472 (Mar. 30, 1995) (rejecting a suggestion to allow appeals of some enforcement-related items because an existing "alternative appeals mechanism" allowed banks to "contest enforcement actions"); FDIC, Guideline for Appeals of Material Supervisory Determinations, 73 Fed. Reg. at 54,823 ("[T]he administrative hearing process and the right to court review of final enforcement orders have uniformly been found to provide all required due process.").

406 *See generally* 12 U.S.C. §§ 1818(h), 1786. Financial institutions cannot bypass the administrative law judge review. Judicial review is available only after an administrative law judge decision.

407 *Settlement Practices Hearing*, *supra* note 403, at 117 (written statement of Daniel P. Stipano, Deputy Chief Counsel, OCC).

408 *Id*.

tional changes. In these circumstances, it seems reasonable to conclude that institutions would be most likely to contest egregious and costly errors. If an institution could comply with an enforcement action at a lower cost than challenging the enforcement action, that institution might rationally consent to an enforcement action, even if it believes the action is unwarranted.[409]

In contrast, the MSD appeals processes are informal, inexpensive, and speedy. Institutions can make their case directly to the appellate authority; they need not employ an attorney.[410] Even in complicated cases, the appeal is heard and decided within a year.[411] The appealing institution avoids a drawn-out, contentious process with an agency with whom it hopes to preserve a working relationship. Thus, a financial institution might use the MSD appeals process even if it would not contest an enforcement action. There are at least two pieces of evidence to support this conclusion. First, some banks have brought enforcement-related appeals through the MSD appeals processes.[412] Second, in 2008, when the FDIC removed enforcement-related determinations from the list of appealable MSDs, bankers' comments uniformly protested the decision.[413]

In sum, if regulators adopted a broader scope of appealable MSDs, institutions would have more opportunity to correct examiner errors and we could be more confident that the MSD appeals processes provided consistent rights to all financial institutions.

2. Clear and Rigorous Standard of Review

Next, regulators should adopt a clear and rigorous standard of review for MSD appeals. As explained in Part III.A.2, there is inconsistency and confusion regarding the standard of review used by regulators in MSD appeals. Regulatory adoption of a uniform, clear, and rigorous

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409 One hint that not all institutions who enter into enforcement action by consent agree with their regulators: these enforcement actions almost never contain admissions that the institution violated law, policy, or agency guidance. *See id*. at 7, 10 (statements of Scott G. Alvarez, General Counsel, Board of Governors of the Federal Reserve; Richard J. Osterman, Jr., Deputy General Counsel, FDIC; and Daniel P. Stipano, Deputy Chief Counsel, OCC).

410 *See supra* notes 82, 302, and accompanying text.

411 *See* OCC OIG REPORT, *supra* note 11, at 10; FEDERAL RESERVE OIG REPORT, *supra* note 11, at 22; FDIC OIG REPORT, *supra* note 11, at 33; NCUA OIG REPORT, *supra* note 11, at 24-25.

412 *See supra* Figures 2, 5, and 9.

413 FDIC, Guidelines for Appeals of Material Supervisory Determinations, 73 Fed. Reg. 54,822, 54,823 (2008) ("The commenters uniformly expressed support for an independent review or underlying facts, circumstances, and determinations, and that there needs to be 'an effective and non-biased appeals procedure for banks.'").

standard of review could make the MSD appeals processes more useful in achieving consistency. I would select a *de novo* standard for both finding of fact and issues of law and policy.

At present, three regulators look primarily to whether the MSD is consistent with regulator policies and standards.[414] This check is important; examiner decisions should be consistent with the law and previous regulatory pronouncements. However, it is not sufficient to ensure that examiner decisions are consistent. While some appeals may involve MSDs that are straightforward applications of law or written policy,[415] other appeals might present different issues.

Some appeals may involve questions of fact. For example, in rating a loan, one factor considered is the value of the collateral securing the loan.[416] The financial institution and the regulator may have differing conclusions about the value of that collateral. The examiner may have properly classified the loan according to policy, but nevertheless arrived at the wrong classification because the factual assessment of the value of the collateral was incorrect. Standards of review that refer only to law and policy are unhelpful in addressing such factual disputes.

A "consistent with law and written policy" standard is also problematic when existing law and written policy do not cover the issue raised by the financial institution. For example, with respect to capital adequacy, regulators have detailed regulations setting minimum levels, but regulators often require additional capital. Exactly how regulators determine the amount of additional capital is not included in any public pronouncement[417] and is rarely explained to financial institutions. Indeed, in other contexts, financial institution regulators readily admit that some MSDs are not explicitly governed by statute, regulation, or even public

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[414] *See* OCC Bulletin 2013-14 (June 7, 2013); FRB KANSAS CITY APPEALS, *supra* note 157, at 6; FRB MINNEAPOLIS APPEALS, *supra* note 157, at 7; FDIC Intra-Agency Appeals Process, 77 Fed. Reg. 17,055, 17,058 (2012).

[415] Hattix Interview, *supra* note 12 ("Most of what we do, most of it is driven by the number or policy that says, 'Here's how you treat certain situations.'").

[416] *See, e.g.*, FDIC DIVISION OF SUPERVISION AND CONSUMER PROTECTION, RISK MANAGEMENT MANUAL OF EXAMINATION POLICIES § 3.2-41 (2012) ("Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any.").

[417] Hill, *supra* note 23, at 650-57, 698-99

guidance.[418] It is when examiners are exercising individual judgment that variations across examiners are most likely to occur.

So what happens when a financial institution appeals an issue that cannot be easily resolved by consulting governing law or written policies? At present, regulators might review the MSD *de novo*,[419] review it for "overall reasonableness,"[420] or review it under a standard adopted specifically for that appeal.[421] There would be value in simply unifying the standard across regulators so that each appealing financial institution has the same opportunity for review.

Choosing the appropriate level of deference is more difficult. Because judicial deference to administrative decisions is a bulwark of administrative law, some may be tempted to graft similar levels of deference onto the MSD appeals processes. A court reviewing an agency administrative law judge's decision would review questions of fact under a "substantial evidence" or "arbitrary and capricious standard."[422] A court reviewing questions of law or policy would apply *Chevron*,[423] *Skid-*

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418 For example, in addressing a proposal to create an ombudsman outside of each of the financial regulators to hear MSD appeals (*see infra* Part IV.D), David M. Marquis, then NCUA Executive Director explained:

> Currently, much of an examiner's findings are based on sound judgment and sound business or industry practice. . . .
>
> For, example there is no hard-and-true formula about proper asset diversification. Today if an examiner looks at a credit union's books and sees too many mortgages with only a three percent down payment or inappropriately large mortgages, he or she will warn of overconcentration in the exam report. If, however, a credit union appeals this finding to an [authority outside the NCUA, the] NCUA could not point to the violation of a specific regulation, other than citing the fact that overconcentration is an unsafe and unsound practice.

Hearing on H.R. 3461, *supra* note 5, at 131-32 (written statement of David M. Marquis, Executive Director, NCUA).

419 FRB New York Appeals, *supra* note 157, at 10(a).

420 FDIC Intra-Agency Appeals Process, 77 Fed. Reg. 17,055, 17,058 (2012)

421 FRB KANSAS CITY APPEALS, *supra* note 157, at 6; FRB MINNEAPOLIS APPEALS, *supra* note 157, at 7.

422 Agency factfinding established through formal proceeding made "on the record" are reversed only if "unsupported by substantial evidence." 5 U.S.C. § 706(2)(E). Agency factfinding established through informal proceedings are reversed only if "arbitrary" or "capricious." *Id.* at § 706(2)(A).

423 Chevron, U.S.A., Inc v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842-43 (1984) (holding that courts must "give effect to the unambiguously expressed intent of Congress," but gives interpretations of ambiguous statutes "controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute").

more,[424] or *Auer*[425] deference. However, many justifications for judicial deference to agency determinations do not apply here.

First, under *Chevron*, courts defer to agencies because the Administrative Procedure Act, or some other relevant statute, has instructed that they defer.[426] Congress has determined that statutory gaps should be filled by administrative agencies, rather than courts.[427] In contrast, Congress did not specify a standard of review for MSD appeals in either the Administrative Procedure Act[428] or in the Riegle Community Development and Regulatory Improvement Act. Because both the MSD appeals process and the initial examiners are housed within the administrative agency, there is no reason to believe that Congress preferred that the appellate authority defer to the agency officials who reached the initial MSD.

Next, it is sometimes argued that judicial deference to agencies is justified by the agencies' special expertise in the subject matter of the controversy.[429] With MSDs, however, the appellate authorities have expertise. Indeed, agency officials who hear MSD appeals generally have greater training and experience than the examiners who made the initial determination.

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[424] Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944) (holding that when an agency is not empowered to act with the force of law, the weight accorded to the agency's interpretation "will depend on the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade").

[425] Auer v. Robbins, 519 U.S. 452, 461 (1997) (quoting Bowles v. Seminole Rock & Sand Co., 325 U.S. 410, 414 (1945) (holding that interprets a test that is "a creature of [its] own regulations, [its] interpretation of it is, under our jurisprudence, controlling unless 'plainly erroneous or inconsistent with the regulation'").

[426] *See* Motor Vehicle Mfts. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 41 (1983).

[427] Chevron, 467 U.S. at 843-44. *See also* Ronald J. Krotoszynski, Jr., 54 ADMIN. L. REV. 735, 736, 742-43 (2002) ("A reviewing court lacks legitimacy if it attempts to displace an agency's reasonable interpretation of an ambiguous statute with its own interpretation of the statute. After all, Congress vested the agency, not the federal judiciary, with the authority to resolve the meaning of ambiguous statutory text.").

[428] *See* 5 U.S.C. § 555(e) (providing only that agencies provide "[p]rompt notice" and a "brief statement" when denying a "request of an interested person made in connection with any agency proceeding").

[429] *See, e.g.*, SEC v. Chenery Corp., 332 U.S. 194, 209 (1947); Skidmore v. Swift & Co., 323 U.S. 134, 139-40 (1944). *See also* Krotoszynski, *supra* note 427, at 736, 739-41 (noting that pre-*Chevron* case law "squarely held that federal judges should afford persuasive force to the work product of agencies based on the assumption that agencies possessed greater expertise over their own statutes and policies than did federal courts").

Next, some note that judicial deference allows administrative agencies to create a single uniform interpretation of the law. If each court exercised its own judgment, different rules may apply in different jurisdictions.[430] With the MSD appeals process, deference has the opposite effect. The MSD process is an opportunity for a single appellate authority within each regulator to harmonize differing examiner decisions.[431] If the appellate authority instead defers to the original examiner decision, we could end up with many different but "reasonable" interpretations of banking law and policy.

Judicial deference "has also been justified on democratic grounds—namely that agencies are politically accountable and courts are not."[432] Again this deference justification is not applicable because the MSD appeals process is housed within each financial institution regulator, rather than in a separate branch of government. The MSD appellate authority is at least as accountable as the examination staff. Indeed, the appellate authority is even more accountable due to the authorities' generally higher position with each agency. Lower-level agency employees should not be conclusively deciding questions of law and policy (including any controversy about the appropriate application of law and policy).[433] Thus, the appellate authority deciding MSD appeals, should conduct *de novo* review on questions of law or policy.

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[430] *See* Peter L. Strauss, *One Hundred Fifty Cases per Year: Some Implications of the Supreme Court's Limited Resources for Judicial Review of Agency Action*, 87 COLUM. L. REV. 1093, 1105, 1121-22 (1987).

[431] There is still the possibility that each regulator could come to a different conclusion, but adding deference only compounds the potential differences.

[432] Aaron-Andrew P. Bruhl, *Hierarchically Variable Deference to Agency Interpretations*, 89 NOTRE DAME L. REV. 727, 743 (2013) (*citing* Chevron U.S.A. v. Natural Res. Def. Council, Inc. 467 U.S. 837, 865-66 (1984)).

[433] As Professor Mark Seidenfeld explains:

> When an interpretation is made by a low-level official from a program, technical, or enforcement office within an agency as part of his day-to-day functions, the interpretation is likely to reflect the professional perspective of that official. It is unlikely either to go through a serious vetting process within the agency, or be the focus of congressional or White House attention. Thus, such an interpretation is more likely to reflect an idiosyncratic professional perspective than is one that has been reached after consideration by agency officials with different professional backgrounds or an interpretation that is sufficiently central to the agency's mission that it will attract attention of those in the White House or on Capital [sic] Hill.

Mark Seidenfeld, *Chevron's Foundation*, 86 NOTRE DAME L. REV. 273, 301 (2011) (citations omitted). *Cf.* 5 U.S.C. § 557(b) ("On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or by rule.").

Finally, courts defer to agency findings of fact because the agency was in a better position to collect and evaluate the facts underlying the dispute.[434] In the MSD appeals processes, the appellate authority has broad access to the underlying facts.[435] The OCC Ombudsman has even visited financial institutions in order to resolve appeals.[436] Moreover, a *de novo* standard of review of facts is not unprecedented for appeals *within* an administrative agency. For example, if an applicant is denied a Social Security claim, the applicant can request a hearing before an administrative law judge who reviews the facts and law *de novo* in reaching a decision.[437] The administrative law judge does not defer to the agency officials who reached the initial eligibility determination. In MSD appeals the appellate authorities are in much the same position as the administrative law judge. An initial agency decision has been made, often by a relatively low-level agency official. The appeals or hearing process offers the agency the opportunity to correct erroneous factual determinations, as well as errors of law.[438]

Thus, justifications for judicial deference fall short when applied to the MSD appeals process. Moreover, if financial institutions view the MSD appeals process as nothing more than a rubber stamp for the examiners, few institutions will appeal.[439] Consequently, the MSD appeals processes should adopt a clear and robust standard of review.

Some may worry that *de novo* review, particularly when combined with direct access to an independent appellate authority, will encourage financial institutions to "sandbag" examination staff. Rather than raising relevant facts or concerns with examiners, financial institutions might remain silent and then overturn the MSD through the appeals process. This, however, seems unlikely for a variety of reasons. First, the MSD

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[434] *See, e.g.*, James Madison Ltd. v. Ludwig, 82 F.3d 1085, 1096 (D.C. Cir. 1996) ("Generally speaking, district courts reviewing agency action under the APA's arbitrary and capricious standard do not resolve factual issues, but operate instead as appellate courts resolving legal questions.").

[435] *See supra* notes 89, 167-168, 233, 299 and accompanying text.

[436] *See supra* note 89 and accompanying text.

[437] 20 C.F.R. § 416.1429 (2014).

[438] Colleagues have suggested that financial institutions could receive meaningful review if the appellate authority reviews question of law or policy *de novo*, but reviews questions of fact under an arbitrary and capricious standard. For the reasons already explained, I believe the MSD appeal processes would function best with *de novo* review of all appealable issues. However, I believe that a uniform, clearly-established arbitrary and capricious standard for facts would be a significant improvement over the current system.

[439] *See supra* note 366 and accompanying text (explaining that some credit unions report not using the appeals process because they believe it will not make a difference).

appeals process cannot be used to stall enforcement actions. Financial institutions must comply with examiner instructions while any appeal is pending.[440] Second, financial institutions are repeat regulatory players. It is not in their interest to antagonize regulators. Third, the historic success rate for MSD appeals suggests it would be foolhardy for a financial institution to think that winning on appeal is a foregone conclusion. Even if reforms strengthen the appeals process, financial institutions will face risks when using the process.

Some may also worry a robust standard of review will add to the costs of regulating financial institutions. Admittedly, it is difficult to predict what it would cost for appellate authorities to conduct a robust review. It is also difficult to predict to what extent the more robust review would lead to increased use of the MSD appeals processes. Given past utilization of the processes, I think it unlikely that additional costs would be astronomical. To the extent that more complete review does increase regulatory costs, the cost may be justified by the improvement to the regulatory system. Finally, any increased costs will not fall directly on taxpayers. Financial regulators are funded by fees charged to financial institutions[441]— institutions that are generally in favor of strengthening the MSD appeals process.[442]

C. Public Disclosure of Appeal Decisions

Finally, and perhaps most obviously, each appellate authority should provide summary or redacted decisions. The information provided should include (1) the reason the appealing financial institution believes the examiner erred, (2) the applicable law, regulation, or agency guidance, (3) and the decision and accompanying reasoning.

Regulators' primary objection to releasing decisions appears to be that MSD appeals consider confidential information from bank examinations.[443] Regulators keep examination information confidential, believing that negative information could spark a bank run or even a banking panic.[444]

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440 *See supra* notes 100, 162, and 297 and accompanying text.

441 CARNELL, MACEY & MILLER, *supra* note 21, at 61-62; Connie Edwards Josey, Comment, *State v. National Banks: The Battle Over Examination Fees*, 6 N.C. BANKING INST. 463, 466-468 (2002).

442 *See infra* note 449 and accompanying text.

443 Ulan Interview, *supra* note 12.

444 *See generally* Heidi Mandanis Schooner, *The Secrets of Bank Regulation: A Reply to Professor Cohen*, 6 GREEN BAG 2D 389 (2003).

While secrecy may be warranted with respect to the examination itself,[445] there is no need to extend complete secrecy to MSD appeal decisions. The OCC and FDIC have managed to strike a balance between releasing meaningful information and protecting sensitive information.[446] Even during the 2008 financial crisis, disclosure of MSD appeals decisions did not incite a bank run or banking panic. Cloaking the MSD appeals processes in complete secrecy serves only to insulate the processes from public accountability.

D. Another Proposal: The Super-Ombudsman

Others have advocated a more far-reaching change to the MSD appeals processes. Over the last few years, members of Congress have repeatedly introduced legislation that would create an appeals process outside of the regulators to review MSDs.[447] The legislation would establish an Ombudsman Office at the Federal Financial Institutions Examination Council. This "super-Ombudsman"[448] would investigate bank complaints about regulators and hear appeals of MSDs. Financial institution trade groups support such legislation.[449] Yet so far, none of the legislative proposals has made it out of committee.

Regulators oppose a super-Ombudsman. They argue that a new unified arbiter could undercut regulators' ability to effectively monitor the safety and soundness of the banking system. They assert that routing appeals through a super-Ombudsman could:

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[445] Not everyone agrees on this point. *See* Heather Anderson, *Hatchet Buried: N.C. Regulator, NCUA Say No More CAMEL Releases, No More Separate Exams*, CREDIT UNIONS TIMES, Feb. 11, 2013, *available at* 2013 WLNR 3464349 (describing disagreement between the North Carolina credit union regulator and the NCUA over whether it was appropriate to publicly release CAMEL ratings).

[446] *See supra* notes 127-130, 250, and accompanying text. Some might argue that requiring the appellate authority to provide a public, written opinion will delay the appeals processes. Again, however, it appears that the OCC and FDIC have managed to provide decision information without significant delays.

[447] H.R. 3461. 112th Cong. (2011); S. 2160, 112th Cong. (2012); S. 727, 113th Cong. (2013); H.R. 2767, 113 Cong. (2013); S. 798, 113th Cong. (2013).

[448] *See* Hearing on H.R. 3461, *supra* note 5, at 50 (statement of Eugene A. Ludwig, Founder & CEO, Promontory Financial Group, LLC).

[449] *See, e.g*., *Hearing on H.R. 3461*, *supra* note 5, at 78 (written statement of Albert C. Kelly, Jr., Chairman, American Bankers Association) ; *Hearing on H.R.* 3461, *supra* note 5, at 150 (written statement of Ken Watts, President and CEO, West Virginia Credit Union League).

- delay corrective efforts and introduce additional risk in the banking system;[450]
- discourage financial institutions from properly communicating with examiners;[451]
- result in decisions made by people who do not understand the examination process unique to each regulator;[452]
- increase the cost of examinations by effectively requiring "examiners . . . to document each and every finding with specific references to . . . rules and regulations;"[453]
- and increase regulatory costs by creating another government bureaucracy.[454]

I am not necessarily opposed to an appeals process housed outside the financial institution regulators. A single regulator could unify the differing treatment faced by institutions with different regulators. Institutions may also feel more comfortable bringing appeals to an appellate authority outside their primary regulator. To the extent that a super-Ombudsman would motivate regulators to more fully justify and explain examination ratings and other MSDs in examination reports, it would be beneficial to financial institutions and the examination process as a whole.

However, creating a super-Ombudsman would require Congressional action. This may be an uphill battle because regulators uniformly

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[450] According to OCC Ombudsman Larry Hattix:

> Our concern is that creating an outside bureaucracy to hear appeals will significantly delay exam processing. [It would also] delay corrective actions that our supervisory process determines are necessary for the safe and sound operation of that bank or savings association. . . .
>
> If decisions are delayed because of an extended appeals period, bankers may be precluded from conducting certain activities until the appeal is resolved and a final decision rendered.

Witkowski, *supra* note 115 (quoting Larry Hattix, Ombudsman, OCC).

[451] *Id*. (quoting Larry Hattix, Ombudsman, OCC) ("[T]he creation of an outside ombudsman may have a chilling effect on the everyday communication that is critical to effective supervision.").

[452] Lee Interview, *supra* note 12 ("If you had someone totally separate from the agency working on [MSD appeals], I just feel like it would put credit unions kind of at a disadvantage if you have somebody who was just completely unfamiliar with our processes and our institutions.").

[453] *Hearing on H.R. 3461*, *supra* note 5, at 130-31 (written statement of David M. Marquis, Executive Director, NCUA).

[454] *Hearing on H.R. 3461*, *supra* note 5, at 91 (Jennifer Kelly, Senior Deputy Comptroller for Midsize and Community Bank Supervision, OCC); *Hearing on H.R. 3461*, *supra* note 5, at 133 (written statement of David M. Marquis, Executive Director, NCUA).

oppose the proposals. And a super-Ombudsman potentially adds cost for both regulators and financial institutions.[455] Moreover, simply changing the appellate body will not necessarily solve some of the major deficiencies in the current system: namely the inconsistent rules regarding when the appeals processes can be used, lack of a clear and rigorous standard of review, and the lack of transparency. Rather than waiting to see if Congress will impose a super-Ombudsman, regulators should take initiative now to improve their MSD appeals processes.

CONCLUSION

When, in 1994, Congress mandated that each federal financial regulator provide "an intra-agency process . . . to review material supervisory determinations made at insured depository institutions,"[456] Congress hoped the processes would "provide an avenue of redress . . . from uneven treatment by examiners."[457] Now, almost two decades later, the processes adopted pursuant to this mandate have hardly been used. Regulators differ significantly in the access they provide to the appeals process, as well as the standards they use to evaluate appeals. And even finding out basic information about appeals decisions can be difficult. In short, the existing MSD appeals processes do not provide a meaningful avenue for correcting uneven regulatory treatment.

To achieve Congress's goal, regulators must strengthen their MSD appeals processes. Financial institutions should have direct access to a dedicated appellate authority outside of the examination function. Regulators should allow appeals of a broad array of determinations, including all CAMELS rating and determinations underlying enforcement actions entered with the consent of the financial institution. Regulators should employ a clear and rigorous standard of review. Finally, regulators should release appeals decisions in summary or redacted form. While

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[455] A variant of the super-Ombudsman proposal by former Comptroller Eugene A. Ludwig suggests that the super-Ombudsman task force comprised of representatives from each regulator be grafted on top of existing regulatory MSD appeals processes. An institution could approach the taskforce after exhausting the appeals process offered by its regulator. Thus, the taskforce would "play more of a coordinating role among the ombudsmen at the regulatory agencies, and act as a safety valve or an appeals mechanism." *See Hearing on H.R. 3461*, *supra* note 5, at 50 (statement of Eugene A. Ludwig, Founder & CEO, Promontory Financial Group, LLC). Given the small number of appeals that currently make it through the existing MSD appeals processes, it seems doubtful that such a taskforce would be utilized enough to justify the cost. This is particularly true if no changes are made to the existing appeals processes.

[456] 12 U.S.C. § 4806(a).

[457] S. Rep. No. 103-169, at 51 (1994), *reprinted in* 1994 U.S.C.C.A.N. 1881, 1935.

regulators may initially be skeptical of my recommendations, more robust appeals processes benefit regulators by lending credibility to the regulatory structure.