



STATE OF WYOMING

DEPARTMENT OF AUDIT

DIVISION OF BANKING

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Memorandum

To: Chief Executive Officer
All State Chartered Banks

From: Michael E. Williams, Deputy Commissioner
Division of Banking

Date: April 2, 2004

Re: Guidance on Credit Underwriting and Administration

The following guidance on credit underwriting and administration practices will be effective immediately. This guidance will supersede the memorandum of June 1, 1998. Copies of this memorandum should be distributed to all lending personnel.

Loan Documentation Exceptions

Great importance is placed on the bank's written policies, as they are the governance for bank management as set forth by the directorate. Examiners will review the loan policy to ensure that it is clear, concise and above all, prudent. Once this is determined, the bank will be examined for compliance with the policy. History has proven that banks with high percentages of documentation exceptions have experienced severe problems in their loan portfolios. Each bank should set forth in its loan policy its documentation requirements for loans.

In the absence of specific documentation requirements, examiners will utilize the minimum standards detailed in this memorandum for determining exceptions. Loan documentation exceptions will be discussed with management prior to the exit meeting. The final listing will generate the percentage used in the report of examination. The percentage is based on the dollar volume of exceptions divided by the dollar volume of loans reviewed.

1. If the primary collateral is a real estate mortgage on commercial or residential property, an appraisal or evaluation should be done within one year prior to the initial disbursement of loan proceeds. In addition, lien searches or title policies should be obtained to ensure and document the lien position.

2. If the primary collateral is accounts receivable or inventory, an aging schedule or valuation listing should be in the credit file. The schedule or listing should be obtained at origination or renewal and updated at least semi-annually. Loans secured by other types of collateral should have a current listing and evaluation of the collateral at origination and renewal dates.
3. Financial statements should:
 - Be dated as to the date of financial condition;
 - Total and balance;
 - Tie to the subsidiary schedules; and
 - Be signed and dated by all parties listed.
4. Current financial statements are required except in the following instances:
 - Term amortizing loans (only required at origination or renewal);
 - Residential real estate loans (only required at origination or renewal);
 - Borrowers in bankruptcy; and
 - Loans secured in total by deposits and/or U.S. Government Securities.
5. Personal and corporate financial statements should be obtained not more than fourteen months after the last statement date or upon renewal of the note.
6. A loan with guarantees should have current financial statements on each guarantor at origination and each renewal date.
7. All operating and unsecured loans should have a complete tax return in the credit file unless CPA-prepared financial statements are available. Management is encouraged to obtain tax returns for all types of loans.
8. A tax return is considered stale if it is not in the file within sixty days after its filing deadline. If the borrower filed an extension, a copy of the extension should be obtained.
9. Annually, all operating loans should have a budget and a cash flow statement.
10. Any loan to a start-up business should have pro-forma balance sheets and income statements.
11. Loans secured by improved real estate or personal property should have proof of insurance in the file with the bank shown as loss payee.
12. All floor plan loans should have inspections done at least quarterly.
13. Loans secured by livestock should have annual inspections.

Real Estate Loans

Appraisals and evaluations should meet the federal appraisal regulations as well as the requirements set forth in the Interagency Appraisal and Evaluation Guidelines, dated October 27, 1994 and the Interagency Statement on Independent Appraisal and Evaluation Functions, dated October 27, 2003.

Evaluations

When an appraisal is not required, an evaluation may be utilized. A bank should establish prudent standards for the preparation of evaluations. Qualified persons who are capable of rendering unbiased opinions should perform evaluations. While the individual performing an evaluation need not be a state certified or licensed appraiser, the bank is not precluded from using a certified or licensed appraiser to perform evaluations. An evaluation must be in writing and should contain sufficient documentation to substantiate the basis for the value reported for the real estate. The depth and detail of analysis in evaluations should be consistent with the complexity of the property, as well as, the bank's exposure in the transaction.

At a minimum, an evaluation should:

- Be written;
- Include the preparer's name, signature, and the effective date of the evaluation;
- Describe the real estate collateral, its condition, its current and projected use;
- Describe the source(s) of information used in the analysis;
- Describe the analysis and supporting information;
- Provide an estimate of the real estate's market value, with any limiting conditions, and;
- Include calculations, supporting assumptions, and a discussion of comparable sales.

Abundance of Caution

In order for real estate to be considered an abundance of caution the following must apply:

- The bank's position must be fully protected by other collateral and the file documented that the real estate is being taken as additional collateral.
- The extension of credit must be well supported by income.
- If the real estate is the only collateral, then the borrower must be worthy of unsecured credit in conformance with the bank's loan policy and the file documented that the real estate is being taken as an abundance of caution.

Tax Assessments

Tax assessments may be used solely as an estimate of value if the following elements apply:

- When used for home equity lines of credit or second real estate mortgages on the borrower's residence when the sale of the collateral is not the primary source of repayment.
- It is used for non asset-based loans when used in conjunction with an analysis of the borrower's financial condition.
- Bank management is satisfied the assessment represents the fair market value of the property.

Real Estate Mortgages

Generally, a bank may not secure new loans with existing mortgages from earlier transactions unless the following apply:

- The contract terms must obligate future advances from the inception of the loan.
- An earlier mortgage may be used to secure a new loan if the mortgage is amended to show the new money advanced. However, investigation of the bank's lien position would be necessary.

Procedures for Adverse Classification of Agricultural Loans

The portion of an agricultural loan which is secured by livestock or crops will generally be withheld from adverse classification. However, the bank must have properly perfected and enforceable security interest in the assets in question, and the bank must have satisfactory practices for controlling sales proceeds when the borrower sells livestock and crops. The livestock or crops must have a signed independent on-site inspection and the results must be documented.

The following are guidelines for acceptable inspections:

- Performed not more than 90 days prior to the examination start date for feeder livestock operations and for purposes of confirming crops inventories.
- Performed not more than six months prior to the examination start date for breeder stock herds.
- Copies of invoices or bills of sale within the respective three months and six months parameters above are an acceptable substitute for inspection reports.