 TEXAS DEPARTMENT OF BANKING	Bank Name/City:
	Charter #:
	Exam Date:
	Performed By:
#20 – Overdrafts, Cuts, and Kite Suspects	

Assignment Overview

Review of a bank's overdraft activity and procedures is important to assess the bank's control over the unsecured extensions of credit which result from paid overdrafts. Check kiting can occur when a customer is allowed to draw against uncollected funds. Banks have suffered substantial losses from check kiting activity; therefore, monitoring and control systems should be in place to guard against it. Check kiting is illegal and is not covered under standard Blanket Bond insurance policies. "Cuts" refer to that group of deposit items that are not posted in a given day's work. They include insufficient checks, stop/hold suspect items, items with bad account numbers, etc. It is important that these items be researched and posted the following business day. For more information, see the FDIC Examination Manual [Section 3.4](#) on "Cash and Due from Banks" and [Section 4.2](#) "Internal Routine and Controls". The related Reference document on DOBIE for this procedure identifies useful regulations, guidance, and other issuances by various regulatory authorities.

Instructions

IMPORTANT! These procedures are designed to promote critical thinking. Your comments should include what you looked at, what you found, and your conclusions. It is your narrative that should tell the story for a reader who may not be familiar with this bank. The reader/reviewer should have a thorough understanding of what was performed and conclusions made.

Examiners must follow the instructions below and the requirements in the Examiner Bulletin addressing Guidelines for Procedures and Work Paper Documentation for Commercial Examinations. **If there is a conflict between these Instructions and the Examiner Bulletin, the Instructions prevail.** Documentation should support weaknesses and criticisms. All examiners performing these procedures must be listed above in the "Prepared By" section.

Examiners are responsible for exercising sound judgment and utilizing reasonable investigative and analytical skills to arrive at an accurate assessment of the risk profile of this segment of the institution's operations.

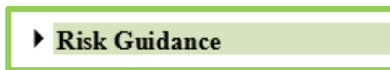
Evaluation Factors, Risk Guidance, and Comments

The focus of this procedure is to evaluate and address each of the Evaluation Factors.

The Risk Guidance is provided to guide the examiner in developing a full and complete analysis for the Evaluation Factor. Examiners should consider the items under Risk Guidance and will use their discretion to determine when to comment on a risk guidance item. Examiners should consider what data or findings merit emphasis and which are secondary or of little importance.

The examiner is expected to write a comment in the Conclusions box that is complete and supportive of findings, recommendations, and ratings.

The examiner may also address areas not included in the Risk Guidance section as it is not intended to be all inclusive.



*To view the Risk Guidance, click on the arrow to the left of the “Risk Guidance” text.
To Hide the Risk Guidance, click on the arrow again.*

Documentation

Supporting documentation should include the standard required documents identified in the Reference Documents section for each Evaluation Factor.

- Embedded documents should be named such that the reviewer will know the contents.
- If a required document will not be included for any reason, DO NOT DELETE the document title, instead, check either :
 - “Not Included” and add a reason why OR
 - “N/A” if a document is not applicable”.
- Any other relevant documents may be added to fully support the examiner’s findings. These documents may be embedded in the Reference Documents section.
- **If a document needs to be referenced in more than one Evaluation Factor comment, include a reference in the comment indicating the Evaluation Factor where the document can be found.**

Documentation is to be sufficient to allow an audit trail of the examiner’s thought process and all significant findings.

Violations of Regulations

Violations of regulations should be addressed under the appropriate Evaluation Factor. Indicate compliance using the drop-down box next to the regulation in the Compliance section. Address non-compliance in the Comment section.

Yes = In compliance

No = Not in compliance

Not Applicable = Requirements in the regulation do not apply. For example, if there were no dividends paid, then the regulation related to approval of dividends would reflect “Not Applicable”.

Nonconformance with Policy

Adherence with best practices identified in Department and Federal financial regulatory policy/guidance should be addressed under the Comments for the appropriate Evaluation Factor. Indicate if the bank adheres to the best practices using the drop-down box next to the appropriate policy in the Adherence to Policy section. Comments regarding best practices should be summarized in the Summary Comments.

Summary Comments and Conclusions

The Summary Comments and Conclusions should be a high-level summary that highlights the examiner's material findings and conclusions. A description of what to include in the Summary Comments and Conclusions is provided. These comments are not intended to be a report ready comment and will contain comments that may not be report worthy. Summary comments must support the Summary Rating.

The EIC will determine if the use of bullet points is appropriate for completing the Summary Comments and Conclusions. *The SEIC/EIC will have discretion in determining what is included in the Report of Examination.*

Navigating this Procedure

This procedure can be easily navigated by clicking on View from the Word menu bar then selecting Navigation Pane found in the Show section. All headings in this document will appear on the left side of the screen for easy navigation through the document.

Performing alternate or expanded procedures not listed with these guidelines may be necessary to complete this risk analysis.

Summary of Findings

#20 Overdrafts and Kite Suspects - Summary Comments and Conclusions

Document conclusions regarding policies, procedures, internal controls, and management oversight of overdrafts and kite suspect activities. Include recommendations for implementing best practices from policies and management's responses to weaknesses. *The SEIC/EIC will determine what to include in the Report of Examination.*

Summary Rating: [**Click Here to Select Rating**](#)

Violations

Prepare a comment for any violation cited. Include management's response.

Overdrafts and Kite Suspects Analysis



Each day during the examination, obtain the NSF report that shows what items will be paid or returned. Provide the report to the examiners working loans.

EVALUATION FACTOR 1:

Review the last examination, most recent internal/external audit, and correspondence to identify any recommendations, violations, Matters Requiring Attention, or regulatory enforcement actions. Determine the Board's and management's efforts to comply with or correct noted deficiencies or concerns.

Reference Documents	Conclusions – Evaluation Factor 1
<p>Prior Examination Criticisms and/or Audit Exceptions</p> <p><input type="checkbox"/> N/A <input type="checkbox"/> Not Included</p> <p>Copy of Management Response/Corrective Action</p> <p><input type="checkbox"/> N/A <input type="checkbox"/> Not Included</p>	

EVALUATION FACTOR 2:

Evaluate the level, trend, and practices related to overdrafts given the size, complexity, and risk profile of the bank.

Risk Guidance

1. Review the overdraft and NSF report each day during the examination.

2. Evaluate the level and trend in the volume and balances of overdrafts. Consider the following:

- a. Is there a high overdraft volume in relation to historical balances?
 - If so, consider possible reasons why, such as (1) a new formal overdraft program, (2) liberal overdraft approval systems, (3) lax charge-off practices, or (4) new or individual officers with a high volume of overdrafts approved.
- b. Are overdraft limits for bank officers reasonable?
- c. Review the overdraft report on random dates. Consider investigating large overdrafts and unusual activity for kiting activity.

3. Assess the practice of extending credit through overdrafts.

- a. Does the bank have limits on the extension of credit through overdrafts?
- b. Are there borrowers with significant overdrafts?
 - i. Aggregate the overdraft with all other outstanding debt to determine compliance with the LLL.

4. Review controls for kite suspects/draws on uncollected funds.

- a. If management allows customers to draw against uncollected funds, determine how management protects the bank from a kite. Consider internal reports, approval processes, and applicable limits.



OPTIONAL: *For training purposes or if there are weaknesses noted, consider reconciling and balancing the overdraft list to the general ledger. Identify overdrafts 30 day or older. Verify that overdrafts are properly reported on RC-C and RC-N. (Note: Examiner performing #14 Loans may also verify content of RC-C and RC-N). If performed, include reconcilements in workpapers below.*

Reference Documents	Conclusions – Evaluation Factor 2
<p>Overdraft Report as of Financial Date and Loan Date</p> <p><input type="checkbox"/> N/A <input type="checkbox"/> Not Included</p> <p>Kite Suspect/Drawn on Uncollected Funds Report</p>	

<input type="checkbox"/> N/A <input type="checkbox"/> Not Included Reconcilements, if applicable <input type="checkbox"/> N/A <input type="checkbox"/> Not Included	
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EVALUATION FACTOR 3:
Determine the adequacy of the Board and management's oversight .

Risk Guidance

- b. Refer to the [Joint Guidance on Overdraft Protection Programs](#) (issued February 23, 2005); the FDIC Overdraft Payment Supervisory Guidance in [FIL-81-2010](#) (issued November 24, 2010).

Adherence to Best Practices in Interagency Policy	
Applies Best Practices to Overdraft Protection Programs as per the Joint Guidance on Overdraft Protection Programs (issued February 23, 2005) and the FDIC Overdraft Payment Supervisory Guidance (issued November 24, 2010) in FIL-81-2010 ?	Select Response

Reference Documents	Conclusions – Evaluation Factor 3

EVALUATION FACTOR 4:
Determine whether the bank complies with applicable regulations.

Risk Guidance

	Conclusions – Evaluation Factor 4 <i>Comment on noncompliance, concerns, or weaknesses.</i>

EVALUATION FACTOR 5: Determine whether there are any uncollectable overdrafts.

Risk Guidance

Reference Documents	Conclusions – Evaluation Factor 5
List of Overdrafts to be Charged Off <input type="checkbox"/> N/A <input type="checkbox"/> Not Included	

APPENDIX

Review of Overdraft Practices, Policies, and Trends

Management and Board Oversight

Management should regularly provide financial and operational reports to the Board, including standardized reports that include overdrafts. The Board should establish limits for relevant committees and officers. The Board or a designated committee should periodically review all authority levels and material actions. The key control objective is that the Board is regularly informed of all significant matters. Overdraft reports are typically reviewed monthly, although the detail included within the report may differ based on the size and risk profile of the institution.

Overdraft policies and procedures should address the following broad areas:

- Account eligibility standards
- Well-defined and properly documented dollar limit decision criteria
- Time frames for when account holders must pay off overdraft balances
- The suspension of overdraft protection services when the account holder no longer meets the eligibility requirements
- Guidelines for addressing a lack of repayment of an overdraft
- Charge-off procedures.

[Return to Evaluation Factor 3](#)