

MEMORANDUM

To: Our Valued Customers

From: Sheshunoff Information Services

Subject: *Credit Risk Management*

We appreciate your order of *Credit Risk Management*, the most important resource available to better manage all aspects of credit risk. This manual provides you with critical information, as well as the tools and techniques you need to ensure stable credit portfolios — essential guidance on risk measurement, loan pricing and structuring, and portfolio diversification.

This update includes two important additions to this manual. Given the significant economic downturn of 2008 and 2009, institutions need to be prepared for increased levels of credit risk from fraud. New Chapter 3B discusses how credit risk managers can address this risk. A brief introduction to this chapter is shown below. Another critical issue for credit risk managers in an economic downturn is the need to continually review and update credit underwriting standards. New Chapter 10B provides a detailed discussion of underwriting procedures for commercial loans to use as an assessment tool for your institution's underwriting program. A brief overview of this chapter also follows below.

- **Chapter 3B — Including High Risk Fraud in Credit Risk Assessments:** Credit risk refers to the potential that a borrower will not fully repay a loan according to contractual terms and conditions. If the borrower is involved in a scheme to defraud the institution, it is unlikely that the institution will be repaid unless the fraudster pays restitution. Therefore, institutions must take the potential for fraud risk into account when evaluating credit management efforts through risk assessments.

When a risk assessment is prepared, the assessment should focus on those lending functions that are most susceptible to fraud. These functions should be evaluated to determine what antifraud controls are in place. Credit risk is increased substantially when a risk assessment concludes that antifraud controls may not be effective in preventing or detecting fraud schemes. These areas are considered at high risk for potential losses. This chapter provides a discussion of some traditional lending areas at high-risk for fraud together with questionnaires that credit managers can use to begin the inquiry process as part of the credit risk assessment process.

- **Chapter 10B — Controlling Commercial Loan Credit Risk through Sound Underwriting Practices:** Underwriting loans is the first and best opportunity to manage credit risk. Underwriting standards should be adjusted periodically based on economic and market conditions to ensure that new loans have the potential to weather adverse economic conditions that may be encountered during the life of the loan. To determine what adjustments may be appropriate, institutions should have well-documented procedures detailing all aspects of the loan underwriting process. These procedures can be used to evaluate opportunities for managing credit risk during the life cycle of a loan. This chapter describes detailed underwriting procedures for commercial loans that can be used to assess an institution's underwriting standards to better manage those standards and overall credit risks.

Thank you again for your interest in Sheshunoff Information Services. If you have comments, questions or would like information on other Sheshunoff products, please call 1-800-456-2340 or visit our Web site at www.sheshunoff.com. If you have any questions about the content of this product, contact the editor directly at jim.baker@sheshunoff.com.