Unsafe or Unsound Practices

A Quick Reference Guide to the OCC and FDIC Final Rule

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What is an "unsafe or unsound practice"?

Final rule definition: "a practice, act, or failure to act, alone or together with one or more other practices, acts, or failures to act, that:
(1) is contrary to generally accepted standards of prudent operation; and
(2)(i) if continued, is likely to—
(A) materially harm the financial condition of the institution; or
(B) present a material risk of loss to the Deposit Insurance Fund ("DIF"); or
(ii) materially harmed the financial condition of the institution."

Harm to financial condition: means "financial losses or other negative impacts to an institution's capital, asset quality, earnings, liquidity, or sensitivity to market risk."

Opportunities missed: The statute gives the agencies authority to penalize "practices," not individual acts; moreover, the majority rule in federal court is that "abnormal risk" means a risk that threatens the "financial stability" or "financial integrity" of the institution. However, the agencies have asserted authority to penalize a single "act, or failure to act" and have developed their own "materiality" standard rather than applying the standard in case law.

How do the standards in the rule work?

Generally accepted standard of prudent operation: “The agencies decline to codify a list of or adopt a bright line” and leave the question to “examiner judgment, based on objective facts and sound reasoning.”

- The test “[does] not require an institution to adopt what the agencies consider to be best practices,” including practices identified through horizontal reviews; but
- “The agencies reserve the right to determine whether widespread practices are generally imprudent . . . based on objective facts and sound reasoning.”

Financial materiality: “The agencies also decline to adopt a quantitative definition for what qualifies as material” and again leave the question to “examiner judgement, based on objective facts and sound reasoning.”

Open question: The new standard for exercise of examiner judgment – i.e., reliance on objective facts and sound reasoning – is not defined.

Do the standards apply differently to supervisory vs. enforcement actions?

Enforcement actions: Harm must be "likely." "Likely" means "more than speculative or merely possible" but not necessarily "more likely than not to occur."

Matters requiring attention (MRAs): Harm must be "reasonably foreseeable." This is intended to be "a lower probability" than "likely."

Supervisory observations: No requirement for likely or foreseeable harm; however, "does not create a requirement or supervisory expectation that the supervisory observation will be presented to the institution's board of directors or that the institution will take corrective action."

Violations of law: Violations of banking or banking-related laws can either be cited as MRAs, when the standard in the rule is met, or as "other violations," when it is not. The agencies "may require an institution to remediate another violation."

Institution-affiliated parties (IAPs): IAPs (e.g., directors and officers of a bank) are not covered by the final rule and thus continue to be subject to more open-ended enforcement standards.

What is tailoring?

Tailoring: Each agency "will tailor its supervisory activities and enforcement actions based on unsafe or unsound practices under 12 U.S.C. 1818 and its issuance of matters requiring attention based on the risks associated with the institution's capital structure, complexity, activities, asset size, and any other financial risk-related factor that the [agency] deems appropriate."

Bottom line: It will be easier to issue an MRA or pursue an enforcement action against a large or complex bank as compared to a small bank. While the agencies have articulated a policy and political basis for this approach, neither the proposed nor final rules identify a clear legal basis for it.

What else do I need to know?

- **The FRB** has not joined this rule, or issued any corresponding proposal of its own, but has issued guidance that is aligned with the FDIC/OCC approach in many respects.
- The **OCC has issued a proposed rule on violations of law,** which would solidify the distinction between **substantive violations** and **technical (or other) violations**. Notably, violations could qualify as substantive without meeting the financial materiality test (e.g., a pattern of BSA non-compliance may be actionable whether or not it poses material financial harm). But isolated controls gaps without tangible real-world effects are substantially less likely to be escalated through the supervision and enforcement process.
- The **OCC** has made public its **Policies and Procedures Manual (PPM) on MRAs**, and updated its **PPM on Enforcement**. The PPMs: (i) constrain the agency's authority to require lookbacks and independent consultant reviews; (ii) constrain the agency's ability to require proof of "sustainability" before closing an MRA; (iii) clarify the OCC's approach to examining compliance with, and closing, enforcement actions; and (iv) remove the "too big to manage" appendix to the Enforcement PPM.
- The **FDIC has updated its Consumer Examination Manual (CEM) and Risk Management Manual (RMM)** to align with the final rule. The RMM update also includes certain timeline and process enhancements to FDIC risk management examinations.
- You can read the **full final rule and its preamble** here: https://www.federalregister.gov/d/2026-17823.

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