Financial Institution Letter FIL-108-98
September 30, 1998

FFIEC

Federal Financial Institutions Examination Council
Washington, D.C. 20037

CALL REPORT DATE: September 30, 1998

THIRD 1998 CALL, NUMBER 205

SUPPLEMENTAL INSTRUCTIONS

September 1998 Call Report Materials

The banking agencies are providing every bank with a sample set of September 30, 1998, report forms as part of this Call Report package because of the high percentage of banks requesting sample forms for this quarter. The enclosed sample set of forms for your bank is generally based on whether your bank has any "foreign offices" (including an International Banking Facility) and on the total assets reported by your bank in its June 30, 1997, Report of Condition (see pages 1 through 4 of the General Instructions section of the Call Report instructions). Based on these criteria, in general:

- Banks of any size that have "foreign offices" must file the FFIEC 031 report;
- Banks without foreign offices and with assets of $300 million or more must file the FFIEC 032 report;
- Banks without foreign offices and with assets of $100 million or more but less than $300 million must file the FFIEC 033 report; and
- Banks without foreign offices and with assets of less than $100 million must file the FFIEC 034 report.

Please retain the enclosed sample set of forms for reference through December 31, 1998. Sample forms for each quarter are available on both the FFIEC's Web site (www.ffiec.gov) and the FDIC's Web site (www.fdic.gov). A paper copy of the Call Report forms, including the cover (signature) page, can be printed from the Web sites. In addition, banks that use Call Report software can print paper copies of the forms from their software. If necessary, you may request the next quarter's sample forms by marking the box located in the section of this quarter's report that asks for the name of your bank's Call Report contact person. Furthermore, for all banks, the banking agencies will include a cover (signature) page in the Call Report materials next quarter.

Submission of Completed Reports

All banks must submit their Call Reports electronically to the banking agencies' electronic collection agent, Electronic Data Systems Corporation (EDS), using one of the two methods described in the agencies' September 30, 1998, cover letter. Banks are no longer permitted to send completed hard-copy (paper) Call Report forms directly to the appropriate federal banking agency, i.e., to the FDIC for national and FDIC-supervised banks and to the appropriate Federal Reserve District Bank for state member banks. For assistance in submitting Call Reports to EDS, contact EDS toll free on (800) 255-1571.

Banks that contract with another party to convert their Call Reports to electronic form for transmission to EDS should deliver their hard-copy reports to that party in sufficient time for EDS to receive their Call Report data files by the submission deadline.

Banks are required to maintain in their files a signed and attested record of the completed Call Report that has been submitted to EDS showing at least the title of each Call Report item and the reported amount. As mentioned above, the cover page of the enclosed sample set of report forms should be used to fulfill the signature and attestation requirement. The signed cover page should be attached to the Call Report that is placed in the bank's files.

Currently, Call Report preparation software products marketed by DBI Financial Systems, Inc.; DPSC Software, Inc.; Electronic Strategies, Inc.; Information Technology, Inc.; Milas LLC; and Sheshunoff Information Services, Inc., have been certified for electronic submission by EDS. Both Electronic Strategies' and Information Technology's software operate on mainframe computers while the other vendors' software products run on personal computers. The addresses and telephone numbers of the vendors with EDS-certified Call Report software are listed at the end of these Supplemental Instructions.

FFIEC Instruction Books

A complete revised Call Report instruction book was sent to each bank last year for use beginning with the reports for September 30, 1997. This book contains the instructions for all four versions of the Call Report forms (FFIEC 031, 032, 033, and 034) in a single volume. When appropriate, the quarterly Call Report materials sent to each bank include an instruction book update. This Call Report package does not contain an update to your instruction book. Your instruction book should include update pages dated 3-98 and 6-98. If your bank has not received the revised instruction book or the updates, copies may be obtained from the FDIC's Call Reports Analysis Section (telephone toll free on 800-688-FDIC) or from your Federal Reserve District Bank. The Call Report instructions are available on both the FFIEC's Web site (www.ffiec.gov) and the FDIC's Web site (www.fdic.gov).

Mortgage and Nonmortgage Servicing Assets

On August 10, 1998, the federal banking agencies published a final rule amending their regulatory capital treatment of servicing assets. This rule increases the maximum amount of servicing assets (when combined with purchased credit card relationships (PCCRs)) that are includable in regulatory capital from 50 percent to 100 percent of Tier 1 capital. Servicing assets include the aggregate amount of mortgage servicing assets (MSAs) and nonmortgage servicing assets (NMSAs). The final rule also applies a further sublimit of 25 percent of Tier 1 capital to the aggregate amount of NMSAs and PCCRs. In addition, the rule subjects the valuation of MSAs, NMSAs, and PCCRs to a 10 percent discount. The final rule is effective October 1, 1998, but institutions may choose to apply the revised limits on servicing assets when they prepare their September 30, 1998, Call Reports.

One effect of the final rule is that NMSAs will for the first time be recognized, rather than deducted, for regulatory capital purposes. As a result, the FFIEC and the banking agencies are considering what the reporting treatment should be for NMSAs in the Call Report in 1999. Until then, banks with NMSAs should continue to report them as part of "All other identifiable intangible assets" in Schedule RC-M, item 6.b.(2). However, when completing Schedule RC-R -- Regulatory Capital, banks may recognize NMSAs in accordance with the provisions of the final rule. As an interim reporting treatment, banks that recognize NMSAs in their regulatory capital calculations should report the amount of NMSAs they include in their Tier 1 capital in Schedule RC-M, item 6.e, "Amount of intangible assets that have been grandfathered or are otherwise qualifying for regulatory capital purposes." This amount, plus the amount of PCCRs included in Tier 1 capital, must not exceed the 25 percent of Tier 1 capital sublimit for NMSAs and PCCRs.

FASB Statement No. 133

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. This statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. Under Statement No. 133, banks must recognize all derivatives as either assets or liabilities on the balance sheet and must measure those instruments at fair value. If certain conditions are met, a derivative may be specifically designated as a "fair value hedge," a "cash flow hedge," or a hedge of a foreign currency exposure of a net investment in a foreign operation. The accounting for changes in the fair value of a derivative (that is, gains and losses) depends on the intended use of the derivative and the resulting designation.

Statement No. 133 is effective for all fiscal quarters of fiscal years beginning after June 15, 1999. Earlier application of ***all*** of the provisions of this statement is encouraged. Statement No. 133 contains further guidance on the initial application of this accounting standard. Piecemeal adoption of Statement No. 133 is not permitted. Banks must adopt Statement No. 133 for Call Report purposes upon its effective date based on their fiscal year. Early application is permitted in the Call Report in accordance with the transition guidance in Statement No. 133. Banks are encouraged to consult with their outside accountants as they plan to implement this new standard.

The transition provisions of Statement No. 133 provide that at the date of initial application, a bank may transfer any debt security categorized as held-to-maturity into the available-for-sale category or the trading category without calling into question the bank's intent to hold other debt securities to maturity in the future. The transition provisions further require that the unrealized holding gain (loss) on a transferred held-to-maturity debt security be reported as part of the cumulative-effect-type adjustment of net income if transferred to the trading category or as part of the adjustment to the change in net unrealized holding gains (losses) on available-for-sale securities if transferred to the available-for-sale category. Any security transferred from the held-to-maturity category as of the date of adoption of Statement No. 133 and sold in the same fiscal quarter should have been transferred to the trading category, not the available-for-sale category. Thus, any unrealized gain (loss) on the security that exists on the date of transfer would be reported in the Call Report income statement in Schedule RI, item 11, "Extraordinary items and other adjustments, net of income taxes," and would not be included in the gain (loss) on the sale of the security in Schedule RI, item 6.b, "Realized gains (losses) on available-for-sale securities."

Reporting of Risk-Weight Information in Schedule RC-R

Items 4 through 9 of Schedule RC-R -- Regulatory Capital are used for reporting the amount of assets and the credit equivalent amount of off-balance sheet items assigned to the four risk-based capital risk weight categories (zero, 20, 50, and 100 percent). Although banks with assets of less than $1 billion whose total risk-based capital is greater than or equal to 8 percent of "adjusted total assets" are not required to complete items 4 through 9, such banks may choose to complete these items at their option. The risk-weight information needed for these items generally should be available to banks because it is used to determine net risk-weighted assets, which all banks must report in item 3.d.(1) of Schedule RC-R. In addition, banks that complete items 4 through 9 of Schedule RC-R will facilitate the banking agencies' verification of the net risk-weighted assets reported in item 3.d.(1).

AICPA Statements of Position 98-1 and 98-5

The American Institute of Certified Public Accountants has recently issued Statement of Position (SOP) 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, and Statement of Position 98-5, *Reporting on the Costs of Start-Up Activities*.

SOP 98-1 provides guidance on whether costs of internal-use software should be capitalized (and then amortized) or expensed as incurred. Internal-use software has the following characteristics: (a) the software is acquired, internally developed, or modified solely to meet the entity's internal needs, and (b) during the software's development or modification, no substantive plan exists or is being developed to market the software externally.

SOP 98-5 requires costs of start-up activities and organization costs to be expensed as incurred. SOP 98-5 defines start-up activities broadly as "those one-time activities related to opening a new facility, introducing a new product or service, conducting business in a new territory, conducting business with a new class of customer or beneficiary, initiating a new process in an existing facility, or commencing some new operation."

Both of these SOPs are effective for financial statements for fiscal years beginning after December 15, 1998, with earlier application encouraged in fiscal years for which annual financial statements have not been issued. For Call Report purposes, banks must adopt these two SOPs upon their effective date based on their fiscal year. Early application is permitted in the Call Report in accordance with the transition guidance in the SOPs. The Glossary entries for "Internally Developed Computer Software" and "Organization Costs" in the Call Report instruction book and other instructions affected by these SOPs will be revised at a later date.

Re-Booking Charged-Off Loans

When available information confirms that a specific loan or lease, or a portion thereof, is uncollectible, a bank should promptly charge this amount off against the allowance for loan and lease losses. When making a full or partial direct write-down of a loan or lease for the amount that is uncollectible, the bank establishes a new cost basis for the asset. As the bank attempts to recover the loan or lease in a period subsequent to the recording of the direct write-down, the bank may determine that the borrower's condition has significantly improved or it may obtain additional collateral from the borrower. In some cases when this has occurred, a bank has attempted to reverse the previous write-down and "re-book" the charged-off loan or lease. Re-booking a charged-off loan is not an acceptable practice under generally accepted accounting principles and, therefore, is not acceptable for Call Report purposes. Consequently, once a new cost basis has been established for a loan or lease through a direct write-down, this cost basis must not be "written up" at a later date.

FASB Statement No. 125

FASB Statement No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, provides consistent standards for determining whether transfers of financial assets should be treated as sales or secured borrowings. The statement includes implementation guidance for the accounting for loan participations and syndications, repurchase agreements including "dollar rolls," transfers of receivables with recourse, servicing of financial assets, securitizations, and securities lending transactions. It also affects the accounting and reporting for certain financial assets that can be prepaid without the holder recovering substantially all of its recorded investment and for servicing contracts.

Banks must adopt Statement No. 125 for Call Report purposes. ***Each bank should ensure that it prepares its September 30, 1998, Call Report in accordance with this accounting standard.*** For summaries of relevant provisions of Statement No. 125, please refer to the Glossary entries for "Transfers of financial assets," "Extinguishments of liabilities," "Servicing assets and liabilities," "Repurchase/resale agreements," and "Securities borrowing/lending transactions" in your Call Report instruction book.

GAAP as the Reporting Basis for the Call Report

When preparing your Call Report, your bank should follow generally accepted accounting principles (GAAP), including the specific reporting guidance that falls within the range of acceptable practice under GAAP (see page 11 of the General Instructions), for recognition and measurement purposes. However, banks must continue to follow the line item instructions in order to determine the specific Call Report line item on which assets, liabilities, income, expenses, and other items are to be reported.

Optional Worksheets and Checklist

Item 3 of Schedule RC-R -- Regulatory Capital requests certain capital and asset amounts used in calculating capital ratios. To assist banks in accurately providing this information, an ***optional*** regulatory capital worksheet is available on request. Because of the limited number of banks subject to the market risk capital guidelines, the worksheet does not include any calculations pertaining to these guidelines. In addition, for assistance in calculating a reasonable estimate of year-to-date applicable income taxes in accordance with FASB Statement No. 109, *Accounting for Income Taxes*, an ***optional*** worksheet geared toward smaller banks is available upon request. Also available upon request is a Report Preparer's Checklist, which banks can use to assist in verifying subtotals, totals, and tie-ins between schedules in the Call Report prior to its submission.

To request a copy of the optional worksheets or checklist, state member banks should contact their Federal Reserve District Bank. National and FDIC-supervised banks should telephone the FDIC's Call Reports Analysis Section in Washington, D.C., toll free on (800) 688-FDIC or call (202) 898-6607. The two optional worksheets for September 30, 1998, also are expected to be available on both the FFIEC's Web site (www.ffiec.gov) and the FDIC's Web site (www.fdic.gov) by that date.

Call Report Software Vendors

For information on available Call Report software, banks should contact:

DBI Financial Systems, Inc.
P.O. Box 60410
Santa Barbara, California 93160
Telephone: (800) 774-3279

Information Technology, Inc.
1345 Old Cheney Road
Lincoln, Nebraska 68512
Telephone: (402) 423-2682

DPSC Software, Inc.
23501 Park Sorrento, Suite 105
Calabasas, California 91302
Telephone: (800) 825-3772

Milas LLC
2936 Graceland Way
Glendale, California 91206
Telephone: (888) 862-7610

Electronic Strategies, Inc.
2405 Schneider Avenue
Menomonie, Wisconsin 54751
Telephone: (715) 235-8420

Sheshunoff Information Services, Inc.
P.O. Box 13203 Capitol Station
Austin, Texas 78711-3203
Telephone: (800) 505-8333