Financial Institution Letter

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REVISIONS TO THE REPORTS OF CONDITION AND INCOME (CALL REPORT) FOR 1998

Contents

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Unless otherwise indicated, the revisions described below apply to all four versions of the Call Report forms (FFIEC 031, 032, 033, and 034). Where appropriate, samples of the revised schedules, or portions thereof, generally from the FFIEC 034 set of forms, are shown to illustrate the specific changes in reporting requirements. These revisions will take effect as of the March 31, 998, report date. In the Call Report for that report date, banks may report a reasonable estimate for any new or revised item for which the requested information is not readily available.

Reductions in Frequency and Detail

Schedule RC-E -- Deposit Liabilities:

Memorandum item 1.e, "Preferred deposits," will be collected annually as of December 31 rather than quarterly as at present. In general, preferred deposits are deposits of states and political subdivisions in the U.S. that are secured or collateralized as required under state law. No changes are being made to the instruction for this Memorandum item.

Schedule RC-E, Memoranda:

- Selected components of total deposits (i.e., sum of item 8, columns A and C).
    - Total Individual Retirement Accounts (IRAs) and Keogh Plan accounts ($.)

- Total brokered deposits ($.)

- Fully insured brokered deposits (included in Memorandum item 1.b above):

    - Issued in denominations of less than $100,000 ($.)

    - Issued either in denominations of $100,000 or in denominations greater than $100,000 and participated out by the broker in shares of $100,000 or less ($.)

- Maturity data for brokered deposits:

    - Brokered deposits issued in denominations of less than $100,000 with a remaining maturity of one year or less (included in Memorandum item 1.c.(1) above) ($.)
    - Brokered deposits issued in denominations of $100,000 or more with a remaining maturity of one year or less (included in Memorandum item 1.b above) ($.)

- Preferred deposits (uninsured deposits of states and political subdivisions in the U.S. reported in item 3 above which are secured or collateralized as required under state law) **(to be completed for the December report only)** ($.)

Schedule RC-D -- Trading Assets and Liabilities (FFIEC 031 and 032 only):

This schedule is completed by banks with $1 billion or more in total assets or with $2 billion or more in notional amount of off-balance sheet derivative contracts. Three existing trading asset items are being eliminated: item 6, "Certificates of deposit (in domestic offices)," item 7, "Commercial paper (in domestic offices), and item 8, "Bankers acceptances (in domestic offices)." As a result, commercial paper held for trading (in domestic offices) will be reported as part of a bank's trading account securities, normally in Schedule RC-D, item 5, "Other debt securities (in domestic offices)." Certificates of deposit and bankers acceptances held for trading (in domestic offices) will be included in Schedule RC-D, item 9, "Other trading assets (in domestic offices)."

Schedule RC-D, FFIEC 031 and 032 only:
ASSETS

- U.S. Treasury securities in domestic offices ($.)
- U.S. Government agency obligations in domestic offices (exclude mortgage-backed securities) ($.)
- Securities issued by states and political subdivisions in the U.S. in domestic offices ($.)
- Mortgage-backed securities (MBS) in domestic offices:

    - Pass-through securities issued or guaranteed by FNMA, FHLMC, or GNMA ($.)

    - Other mortgage-backed securities issued or guaranteed by FNMA, FHLMC, or GNMA (include CMOs, REMICs, and stripped MBS) ($.)

    - All other mortgage-backed securities   ($.   )

- Other debt securities in domestic offices   ($.   )
- - 8   **Not applicable**
- Other trading assets in domestic offices   ($.   )

NOTE: This illustration is for the FFIEC 031 report forms. On the FFIEC 032 report forms, the captions for items 1 through 9 do not refer to domestic offices.

New Items Relating to Regulatory Capital

Item 3 of Schedule RC-R -- Regulatory Capital will be revised through the addition of one new subitem applicable to all banks and two new subitems that will appear only on the FFIEC 031 and 032 report forms applicable to larger banks. Because of these additions to item 3, the existing subitems will be renumbered.

Schedule RC-R:

- Amounts used in calculating regulatory capital ratios (report amounts determined by the bank for its own internal regulatory capital analyses consistent with applicable capital standards):
    - 1. Tier 1 capital   ($.   )
      2. Tier 2 capital   ($.   )
      3. **Tier 3 capital (FFIEC 031 and 032 only)**   ($.   )
    - Total risk-based capital   ($.   )
    - Excess allowance for loan and lease losses (amount that exceeds 1.25% of gross risk-weighted assets)   ($.   )
    - 1. Net risk-weighted assets (gross risk-weighted assets less excess allowance reported in item 3.c above and all other deductions)   ($.   )

      2. **Market risk equivalent assets (FFIEC 031 and 032 only)**   ($.   )
    - **Maximum contractual dollar amount of recourse exposure in low level recourse transactions (to be completed only if the bank uses the "direct reduction method" to report these transactions in Schedule RC-R)**   ($.   )
    - "Average total assets" (quarterly average reported in Schedule RC-K, less all assets deducted from Tier 1 capital)   ($.   )

Reporting of Low Level Recourse Transactions for Risk-Based Capital Purposes

According to the agencies' risk-based capital standards, the amount of risk-based capital that must be maintained for assets transferred with recourse should not exceed the maximum amount of recourse for which a bank is contractually liable. This low level recourse rule applies to transactions in which a bank contractually limits its risk of loss or recourse exposure to less than the minimum risk-based capital requirement for the assets transferred -- generally, four percent for qualifying first lien residential mortgages and eight percent for most other assets. The rule also may apply to sales and securitizations of assets in which contractual cash flows (e.g., interest-only strips receivable and so-called spread accounts), retained subordinated interests, or other assets (e.g., collateral invested amounts or cash collateral accounts) act as credit enhancements. If the rule does apply to a credit enhancement of this type, the maximum contractual dollar amount of the bank's exposure as of a Call Report date is generally limited to the amount carried as an asset on the balance sheet (Schedule RC)in accordance with generally accepted accounting principles.

The FFIEC will revise the Call Report instructions to give banks the option of reporting their low level recourse exposures in Schedule RC-R under either the gross-up or direct reduction method. In conjunction with this change, new item 3.e will be added to Schedule RC-R for the "Maximum contractual dollar amount of recourse exposure in low level recourse transactions." The reporting of this information will enable the banking agencies to verify the capital and risk-weighted asset amounts reported in item 3 by banks choosing the direct reduction method. Banks applying the direct reduction method on Schedule RC-R would include in item 8 any on-balance sheet asset amounts that represent low level recourse exposures. Banks preferring to report their low level recourse exposures under the gross-up method may continue to do so and would report a zero in new item 3.e.

Capital Requirements for Market Risk (FFIEC 031 and 032 only)

In 1996, the banking agencies amended their risk-based capital standards to require banks with substantial trading activity to hold capital based on their market risk exposure. This new rule applies to banks with either (1) total trading assets and trading liabilities of at least $1 billion or (2) total trading assets and trading liabilities in excess of 10 percent of total assets. The rule took effect on January 1, 1998, for all banks meeting these criteria except those exempted by their supervisory agency. The market risk rule supplements the risk-based capital ratio calculations that focus principally on credit risk and adjusts both the risk-based capital ratio denominator and numerator. These adjustments involve "market risk equivalent assets" for the denominator and "Tier 3 capital" for the numerator.

To enable the agencies and other users of the Call Report to calculate the risk-based capital ratios of those banks subject to the market risk rule, new subitems for "market risk equivalent assets" and "Tier 3 capital" will be added to Schedule RC-R, item 3, "Amounts used in calculating regulatory capital ratios." These new subitems are for the FFIEC 031 and 032 report forms only.

In addition, the FFIEC will revise the instructions for items 4 through 7 of Schedule RC-R, which are the items in which banks report their assets and the credit equivalent amounts of their off-balance sheet items by risk weight category. The FFIEC also will revise the instruction for item 8, "On-balance sheet asset values excluded from and deducted in the calculation of the risk-based capital ratio." As revised, the instructions will tell banks that are subject to the market risk rule to exclude from items 4 through 7 the amounts of their "covered positions" (except foreign exchange positions outside the trading account and over-the-counter derivative positions which must be included in risk-weighted assets). Banks will report the amounts of those "covered positions" that are on-balance sheet assets in item 8. "Covered positions" are all positions in a bank's trading account, and all foreign exchange and commodity positions, whether or not in the trading account.

Reporting by Banks With Foreign Offices of Investment Securities Holdings in the Domestic Office Assets and Liabilities Schedule (FFIEC 031 only)

On the FFIEC 031 version of the Call Report forms, banks with foreign offices report a breakdown of the investment securities they hold in domestic offices by type of security in Schedule RC-H -- Selected Balance Sheet Items for Domestic Offices. These banks currently report their domestic office investment securities in Schedule RC-H on the same basis as they report these securities on the consolidated balance sheet (Schedule RC), i.e., held-to-maturity securities are reported at amortized cost while available-for-sale securities are reported at fair value. In the (consolidated) securities schedule (Schedule RC-B), banks report both the amortized cost and fair value of their held-to-maturity and available-for-sale securities.

The domestic office securities data reported in Schedule RC-H are used in analyses and comparisons which also include data on securities that are held domestically by nonbank sectors and reported on a cost basis. Therefore, banks with foreign offices will begin to report their investment securities held in domestic offices on a cost basis in items 10 through 17 of Schedule RC-H. This means that available-for-sale debt securities will be reflected in these schedule RC-H items at amortized cost rather than at fair value while equity securities will be included at historical cost.

This change will not affect how a bank reports its held-to-maturity and available-for-sale securities on the Call Report balance sheet (Schedule RC) or on the securities schedule (Schedule RC-B).

Schedule RC-H, FFIEC 031 only:
In items 10-17, report the amortized (historical) cost of both held-to-maturity and available-for-sale securities in domestic offices.

- U.S. Treasury securities ($.)
- U.S. Government agency obligations (exclude mortgage-backed securities) ($.)
- Securities issued by states and political subdivisions in the U.S. ($.)
- Mortgage-backed securities (MBS):
    - Pass-through securities:
        - Issued or guaranteed by FNMA, FHLMC, or GNMA ($.)
        - Other pass-through securities ($.)
    - Other mortgage-backed securities (include CMOs, REMICs, and stripped MBS):
        - Issued or guaranteed by FNMA, FHLMC, or GNMA ($.)
        - All other mortgage-backed securities ($.)

- Other domestic debt securities ($.)
- Foreign debt securities ($.)
- Equity securities:
    - Investments in mutual funds and other equity securities with readily determinable fair values ($.)
    - All other equity securities ($.)
- **Total amortized (historical) cost of both held-to-maturity and available-for-sale securities (sum of items 10 through 16)** ($.)

Allowance for Credit Losses

The American Institute of Certified Public Accountants' *Audit and Accounting Guide for Banks and Savings Institutions*, issued as of April 1, 1996, requires the allocation on the balance sheet of the allowance for credit losses between on-balance sheet financial instruments and off-balance sheet credit exposures. Previously, these allowance components often were reported in the aggregate in the allowance for loan and lease losses (ALLL).

During 1997, the FFIEC advised banks to allocate the allowance for credit losses on Schedule RC -- Balance Sheet consistent with their allocation methodology for other financial reporting purposes. For example, portions of the allowance related to off-balance sheet credit exposures that are reported as liabilities are to be included in Schedule RC, item 20, "Other liabilities," and in item 4 of Schedule RC-G -- Other Liabilities. Banks also were advised to aggregate these components of the allowance for credit losses when completing Schedule RI-B, part II -- Changes in Allowance for Loan and Lease Losses. Institutions have been encouraged to disclose the amounts of these components in Schedule RI-E, item 9, "Other explanations."

The FFIEC is retaining this method of reporting the allowance for credit losses. Therefore, Schedule RI-B, part II, will be retitled Changes in Allowance for Credit Losses, and item 4.a of Schedule RI -- Income Statement will be recaptioned "Provision for credit losses." However, Schedule RI-B, part I -- Charge-offs and Recoveries on Loans and Leases will not be changed. In part I, banks will continue to disclose only their loan and lease charge-offs and recoveries.

Schedule RI

- Net interest income (item 1.g minus 2.f) ($.)
- Provisions:
    - Provision for credit losses ($.)
    - Provision for allocated transfer risk ($.)

Schedule RI-B
Part II. Changes in Allowance for Credit Losses

- Balance originally reported in the December 31, 1997, Reports of Condition and Income ($.)

- Recoveries (must equal or exceed part I, item 6, column B above) ($.)

- LESS: Charge-offs (must equal or exceed part I, item 6, column A above) ($.)

- Provision for credit losses (must equal Schedule RI, item 4.a) ($.)

- Adjustments (see instructions for this schedule) ($.)

- Balance end of current period (sum of items 1 through 5) (must equal or exceed Schedule RC, item 4.b) ($.)

Under the reporting standards in effect prior to the effective date of the revised audit and accounting guide, banks had included all of the portion of the allowance related to off-balance sheet credit exposures in Tier 2 capital for risk-based capital purposes, subject to specified limits. This regulatory capital treatment remains in effect under the new reporting standards set forth in the revised audit and accounting guide.

Reporting of Securitized Consumer Loans for Vehicle Purchases (FFIEC 031 and 032 only)

On the FFIEC 031 and 032 versions of the Call Report forms, banks report annually as of September 30 the amount of their securitized consumer installment loans to purchase private passenger automobiles and the amount of all other securitized consumer installment loans (excluding credit cards and related plans) in Schedule RC-L, Memorandum items 5.a and 5.c, respectively. According to the current instructions for these items, consumer loans for the purchase of pickup trucks and vans go in the "all other" category rather than the "private passenger automobiles" category.

After reviewing the manner in which these data are used for analyzing consumer credit markets, the FFIEC has determined that securitized consumer loans for the purchase of pickup trucks, other light trucks, and vans for personal use should go in the "private passenger automobiles" category. The instructions for Memorandum item 5.a will be revised so that banks can begin to include securitized consumer loans to purchase vans and light trucks (such as pickup trucks) for personal use in this item rather than in Memorandum item 5.c. In addition, the word "installment" will be removed from the captions and instructions throughout Memorandum item 5.

Schedule RC-L, Memoranda, FFIEC 031 and 032 only:

- Loans to individuals for household, family, and other personal expenditures that have been securitized and sold (with servicing retained), amounts outstanding by type of loan:

    - Loans to purchase private passenger automobiles (to be completed for the September report only) ($.)

    - Credit cards and related plans (to be completed quarterly) ($.)

- All other consumer credit (including mobile home loans) (to be completed for the September report only) ($.)

Categorization of Industrial Development Bonds on the Balance Sheet

Industrial development bonds (IDBs), sometimes referred to as "industrial revenue bonds," are typically issued by local industrial development authorities to benefit private commercial and industrial development. The Call Report instructions currently require all IDBs that are rated by a nationally-recognized rating service to be reported as securities in item 3.c of Schedule RC-B -- Securities. The instructions also state that nonrated IDBs that meet the definition of a "security" in Financial Accounting Standards Board (FASB) Statement No. 115, "Accounting for Certain Investments in Debt and Equity Securities," must be measured in accordance with Statement No. 115. Unless a bank chooses to review the characteristics of each nonrated IDB it holds, the bank must report its nonrated IDBs as loans in Schedule RC-C -- Loans and Lease Financing Receivables. If a bank decides to review each nonrated IDB, those with more of the characteristics of a security are to be reported in Schedule RC-B while those with more of the characteristics of a loan are to be reported in Schedule RC-C.

In order to achieve greater consistency between a bank's Call Reports and its other public financial statements and to reduce reporting burden, the Call report instructions governing the treatment of IDBs will be revised. As revised, the instructions will indicate that IDBs (both rated and nonrated) should be reported as securities in Schedule RC-B or as loans in Schedule RC-C, consistent with the manner in which the bank reports IDBs on the balance sheet for other financial reporting purposes. All IDBs that meet the definition of a "security" in FASB Statement No. 115 must continue to be measured in accordance with Statement No. 115.

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[1]In general, this method requires the bank to multiply the maximum amount of its recourse exposure by the reciprocal of the minimum risk-based capital requirement for the assets transferred. The resulting dollar amount is reported as an off-balance sheet credit equivalent amount in the risk weight category appropriate to the assets transferred. For example, if the bank's maximum contractual exposure is $10 million and the transferred assets would be in the 100 percent risk category, the bank would report a credit equivalent amount of $125 million [$10 million x (1/.08)] in the Schedule RC-R item for credit equivalent amounts of off balance sheet items assigned to the 100 percent risk category (item 7.b).

Current Call Report instructions require a bank to report its low level recourse transactions in Schedule RC-R -- Regulatory Capital using the so-called "gross-up" method.[1] However, in certain circumstances, the use of the gross-up method tends to distort a bank's risk-based capital ratios. Although this distortion can be eliminated by using the so-called "direct reduction" method, the Call Report instructions do not currently permit banks to use this alternative. Under the direct reduction method, a bank generally would directly reduce its Tier 1 capital by the maximum amount of its recourse exposure (and would exclude this amount from its assets if the exposure were in the form of an on-balance sheet asset).