

FFIEC
Federal Financial Institutions Examination Council

Washington, D.C. 20006

CALL REPORT DATE: December 31, 2001

FOURTH 2001 CALL, NUMBER 218

SUPPLEMENTAL INSTRUCTIONS

December 2001 Call Report Materials

A sample set of the December 31, 2001, report form applicable to your bank is enclosed. Banks with domestic offices only must file the FFIEC 041 report form. Banks with domestic and foreign offices must file the FFIEC 031 report form.

Please retain the enclosed sample report form for reference. Sample forms also 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 generally can print paper copies of blank forms from their software.

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' cover letter for the December 31, 2001, report date. For assistance in submitting Call Reports to EDS, contact EDS toll free at (800) 255-1571.

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. Either the cover page of the enclosed sample set of report forms, a photocopy of the cover page, or a copy of the cover page printed from Call Report software or from the FFIEC's or the FDIC's Web site 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.; Financial Architects US; FRS, an S1 Corporation Business; Information Technology, Inc.; The InterCept Group; Jack Henry & Associates, Inc. (Banker-II Data Center); Milas LLC; and Sheshunoff Information Services have been certified for electronic submission by EDS. 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 in two installments as part of the March 31 and June 30, 2001, Call Report materials. The next update to your instruction book is expected to be distributed with the Call Report materials for the first quarter of 2002.

Copies of the Call Report instructions may be obtained from the FDIC's Reports Analysis and Quality Control Section (telephone toll free at 800-688-FDIC) or from your Federal Reserve District Bank. The Call Report instructions are also available on both the FFIEC's and the FDIC's Web sites.

Servicing, Securitization, and Asset Sale Activities

Schedule RC-S, Securitization and Asset Sale Activities, collects data on a bank's servicing activities along with information on the bank's involvement with securitizations and asset sales. In Memorandum items 2.a, 2.b, and 2.c of Schedule RC-S, banks should report the principal balance of financial assets (e.g., loans) serviced for others. The instructions state that banks should include the balance of those assets for which the bank has purchased the servicing directly as well as the balance of those assets that the bank has acquired and sold with servicing retained. Financial assets can be acquired either by originating them or by purchasing them. Thus, when your bank reports the volume of servicing in these Memorandum items, you should include (1) the principal balance of loans and other financial assets that your bank has either originated or purchased and subsequently sold while retaining the servicing plus (2) the principal balance of loans and other financial assets owned by others for which your bank has purchased the servicing. Please note that the information on 1-4 family residential mortgage loan servicing that your bank is currently requested to report in Memorandum items 2.a and 2.b was - through December 31, 2000 - collected in items 4.a through 4.d of Schedule RC-M. Similarly, Memorandum item 2.c of Schedule RC-S on the servicing of other financial assets, which must be completed when the volume of this servicing exceeds \$10 million, corresponds to former item 13 of Schedule RC-M.

Items 1 through 8 of Schedule RC-S collect information pertaining to securitization structures sponsored or otherwise established by the reporting bank where the bank's transfer of assets in connection with the securitization qualified for sale accounting under generally accepted accounting principles. In particular, a bank should report in item 1 the outstanding balance of loans that it has sold and securitized when the bank has continuing involvement with the loans by either retaining servicing or providing recourse or other credit enhancements. However, when a bank sells 1-4 family residential mortgages to the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac) and this government-sponsored agency in turn securitizes the loans, the bank should not report the outstanding balance of these loans in Schedule RC-S, item 1, column A. If these loans have been sold to Fannie Mae or Freddie Mac with recourse or other seller-provided credit enhancements, the outstanding principal balance of these loans should be reported in Schedule RC-S, item 11, column A, and the maximum credit exposure arising from the enhancements should be reported in item 12, column A. If servicing has been retained on the residential mortgages, the outstanding principal balance of the mortgages should be reported in Memorandum item 2.a or 2.b depending on whether the servicing is performed with or without recourse or other servicer-provided credit enhancements. In those cases where the bank has both retained the servicing and provided credit enhancements, the principal balance of the residential mortgages will be reported in Schedule RC-S, item 11, column A, and in Memorandum item 2.a.

In items 2, 9, and 12 of Schedule RC-S, banks report maximum amounts of credit exposure arising from credit enhancements provided by the reporting institution to support securitizations

and other asset sales. These maximum exposure amounts should be reported gross rather than net of any tax effects, e.g., any associated deferred tax liability.

Fiduciary and Related Services

Banks that have fiduciary or related activities in the form of assets or accounts must provide information on these assets and accounts and, if certain conditions are met, on fiduciary income, expense, and losses in new Schedule RC-T, Fiduciary and Related Services. If the bank has Individual Retirement Accounts, Keogh Plan accounts, and similar accounts that hold deposits in the bank itself and are administered solely for this purpose, these accounts should not be reported in Schedule RC-T.

In item 4, column A, of Schedule RC-T, banks must report the market value of managed assets held in personal trust and agency accounts. A breakdown of these managed assets by type of asset is reported in Memorandum items 1.a through 1.k, with the total reported in Memorandum item 1.l. Because this total must equal item 4, column A, only the proportionate share of the assets of common trust funds and collective investment funds that are held for participating accounts that are managed should be reported in Memorandum items 1.a. through 1.k. The proportionate share of fund assets held for non-managed participating accounts should not be included in these Memorandum items.

Impairment of Servicing Assets

FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, provides guidance on evaluating and measuring impairment of servicing assets. Servicing assets must be stratified and impairment recognized through a valuation allowance for an individual stratum when its carrying amount exceeds its fair value. The valuation allowance would be adjusted to reflect subsequent changes in the measurement of impairment. Impairments recognized on mortgage servicing assets should be reported in Schedule RI, item 5.f, "Net servicing fees." Similarly, if the fair value of a servicing liability increases above its carrying amount, the increased obligation should be recognized as a loss in current earnings and reported in Schedule RI, item 5.f.

FASB Statements Nos. 141 and 142

In July 2001, the FASB issued Statement No. 141, *Business Combinations*, and Statement No. 142, *Goodwill and Other Intangible Assets*. Statement No. 141 supersedes the previous accounting standard on business combinations (i.e., mergers and acquisitions), Accounting Principles Board (APB) Opinion No. 16, and requires that all business combinations initiated after June 30, 2001, (except for combinations between two or more mutual enterprises) be accounted for by the purchase method. The use of the pooling-of-interests method for those business combinations is prohibited. Statement No. 141 also changes the requirements for recognizing intangible assets as assets apart from goodwill in business combinations accounted for by the purchase method for which the date of acquisition is July 1, 2001, or later. The statement specifically identifies core deposit intangibles as one type of intangible that must be recognized as an asset separate from goodwill.

Statement No. 142 supersedes the previous accounting standard on intangible assets, APB Opinion No. 17. This new standard addresses how intangible assets that are acquired individually or with a group of other assets (but not in a business combination) should be

accounted for upon their acquisition. It also explains how goodwill and other intangible assets should be accounted for after they have been acquired.

Under Statement No. 142, goodwill acquired in a business combination for which the acquisition date is after June 30, 2001, should not be amortized, but should be tested for impairment in accordance with the provisions of this accounting standard. Goodwill acquired in a business combination for which the acquisition date is before July 1, 2001, should continue to be amortized until an institution first applies all of the provisions of Statement No. 142 in accordance with the effective date of the standard. Statement No. 142 is effective for fiscal years beginning after December 15, 2001, with early application permitted for institutions with fiscal years beginning after March 15, 2001, in the manner described in the standard. For banks with a calendar year fiscal year, Statement No. 142 takes effect January 1, 2002.

Banks must adopt FASB Statements No. 141 and 142 for Call Report purposes in accordance with the effective dates of these standards based on their fiscal years. For a bank that is a subsidiary of a holding company or other company, this includes applying the provisions of Statement No. 142 on goodwill impairment testing by a subsidiary. These provisions require all goodwill recognized by such a bank on its Call Report balance sheet to be accounted for in accordance with Statement No. 142 and to be tested for impairment at the bank level.

Banks with other than calendar year fiscal years that choose to early apply all of the provisions of Statement No. 142 prior to 2002 should report any impairment losses recognized as a result of the standard's required transitional impairment testing as the effect of a change in accounting principle. The effect of the accounting change and related income tax effects should be reported in the Call Report income statement, Schedule RI, item 11, "Extraordinary items and other adjustments, net of income taxes," and disclosed in Schedule RI-E, item 3. Until the Call Report income statement format is changed, any goodwill impairment loss that does not result from a transitional impairment test should be included in Schedule RI, item 7.c, "Amortization expense of intangible assets."

Although the accounting rules for goodwill and other intangible assets are changing, there has been no change in the regulatory capital treatment of these assets. The existing regulatory capital limits on servicing assets and purchased credit card relationships remain in effect, and goodwill and other intangible assets continue to be deducted from capital and assets in determining a bank's capital ratios.

Questions about the application of Statement Nos. 141 and 142 for Call Report purposes may be directed to the FDIC's Reports Analysis and Quality Control Section (telephone toll free at 800-688-FDIC) or your Federal Reserve District Bank. Banks also are encouraged to consult with their outside accountants concerning their implementation of these two new accounting standards.

Overnight Federal Home Loan Bank Advances

Immediately available funds borrowed from a Federal Home Loan Bank for one business day meet the definition of federal funds purchased. Accordingly, these so-called overnight advances should be reported on the Call Report balance sheet in Schedule RC, item 14, "Federal funds purchased and securities sold under agreements to repurchase." These overnight advances should not be included on the balance sheet in Schedule RC, item 16, "Other borrowed money," nor should they be included in the breakdown by remaining maturity of "Other borrowed money"

that is reported in Schedule RC-M, item 5. Although Schedule RC-M, item 5.a, covers Federal Home Loan Bank advances, only those advances that are part of "Other borrowed money" on the balance sheet should be included in item 5.a.

Allowance for Credit Losses on Off-Balance Sheet Credit Exposures

Since 1996, the *Audit and Accounting Guide - Banks and Savings Institutions*, published by the American Institute of Certified Public Accountants, has stated that credit losses related to off-balance sheet financial instruments should be accrued and reported separately as liabilities "if the conditions of FASB Statement No. 5 are met." Consistent with this accounting guidance, the Call Report instructions state (on Glossary page A-3) that "each bank should also maintain, as a separate liability account, an allowance sufficient to absorb estimated credit losses associated with off-balance sheet credit instruments." Off-balance sheet credit instruments include off-balance sheet loan commitments, standby letters of credit, and guarantees.

On the Call Report, a bank must report its "Allowance for credit losses on off-balance sheet credit exposures" in item 3 of Schedule RC-G, Other Liabilities, *not* as part of its "Allowance for loan and lease losses" in Schedule RC, item 4.c. However, for risk-based capital purposes, the "Allowance for credit losses on off-balance sheet credit exposures" is combined with the "Allowance for loan and lease losses" and the total of these two allowances is included in Tier 2 capital up to a limit of 1.25 percent of a bank's gross risk-weighted assets. For further information on the inclusion of these allowances in Tier 2 capital, please refer to the instructions for Call Report Schedule RC-R, item 14.

Reporting Income from Insurance-Related Activities in the Income Statement

Banks conduct certain insurance-related activities in various ways depending on their organizational structure. This has led to questions about how income from sales of annuities and from certain other types of insurance activities should be reported in Call Report Schedule RI, Income Statement, and particularly in item 5.h, "Insurance commissions and fees." In general, banks should report in Schedule RI, item 5.h, all income from insurance and reinsurance underwriting and from sales of insurance (including credit life insurance), reinsurance, and annuities. However, commissions and fees on sales of annuities by a bank's trust department (or consolidated trust company subsidiary) that are executed in a fiduciary capacity should be reported in Schedule RI, item 5.a, "Income from fiduciary activities." In addition, commissions and fees that a bank earns from sales of annuities to bank customers by securities brokerage firms should be reported in Schedule RI, item 5.d., "Investment banking, advisory, brokerage, and underwriting fees and commissions."

Standby Letters of Credit Issued by a Federal Home Loan Bank

The instructions for Schedule RC-L, item 9, "All other off-balance sheet liabilities," indicate that this item includes standby letters of credit issued by a Federal Home Loan Bank (FHLB) on behalf of the reporting bank. On these letters of credit, because the reporting bank is the account party, it is obligated to reimburse the issuing Federal Home Loan Bank for all payments made under the standby letters of credit. A bank should include its FHLB standby letters of credit in Schedule RC-L, item 9, if the aggregate amount of these letters of credit exceeds 10 percent of the bank's equity capital. If the aggregate amount exceeds 25 percent of equity capital, these standby letters of credit must be identified and disclosed in item 9.c, 9.d., or 9.e.

Although FHLB standby letters of credit should be reported in Schedule RC-L, item 9, if they exceed the 10 percent reporting threshold, these letters of credit are not subject to the risk-based capital requirements. Accordingly, FHLB standby letters of credit should *not* be reported in Schedule RC-R, Regulatory Capital, item 52, column A, "All other off-balance sheet liabilities." A bank's FHLB standby letters of credit are not covered by the risk-based capital guidelines because the FHLB will have a claim on the bank, rather than the bank having a claim on the FHLB, if the standby letter of credit issued by the FHLB is drawn upon by the beneficiary of the letter of credit.

Proper Reporting of Brokered Deposits

As defined in Section 29 of the Federal Deposit Insurance Act and in the Call Report instructions, a "deposit broker," in general, is "any person engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with insured depository institutions." The term "deposit broker" also includes a bank that is not well capitalized, and any employee of such a bank, which engages, directly or indirectly, in the solicitation of deposits by offering rates of interest significantly higher than prevailing rates on deposits offered in the bank's normal market area. Brokered deposits are deposits obtained, directly or indirectly, by or through a deposit broker.

In their May 11, 2001, Joint Agency Advisory on Brokered and Rate-Sensitive Deposits, the banking agencies advised institutions that make use of significant amounts of such deposits to ensure that proper risk management practices are in place. These risk management practices include having management information systems that identify non-relationship or higher cost funding sources, such as brokered deposits, and allow the bank to manage and monitor these funds and report them properly on the Call Report. In some cases, brokered deposits are issued in the name of the depositor whose funds have been placed in a bank by a deposit broker. In other cases, a bank's deposit account records may indicate that the funds have been deposited in the name of a third party custodian for the benefit of others (e.g., "XYZ Corporation as custodian for the benefit of others," or "Custodial account of XYZ Corporation"). Unless the custodian meets one of the specific exemptions from the "deposit broker" definition in Section 29 and the Call Report instructions, these custodial accounts should be reported as "brokered deposits" in Call Report Schedule RC-E, Deposit Liabilities.

A deposit listing service whose only function is to provide information on the availability and terms of accounts is not facilitating the placement of deposits and therefore is not a deposit broker per se. However, if a deposit broker uses a deposit listing service to identify an institution offering a high rate on deposits and then places its customers' funds at that institution, the deposits would be "brokered deposits" and the institution should report them as such in the Call Report. This classification of the deposits is based not on the broker's use of the listing service but on the placement of the deposits in the institution by the deposit broker.

In items 1 through 7 of Schedule RC-E, banks report separate breakdowns of their transaction and nontransaction accounts by category of depositor. When reporting brokered deposits in these items, the funds should be categorized based on the beneficial owners of the funds that the broker has placed in the bank. The business structure of the deposit broker (i.e., whether the broker is, for example, a bank, an individual, a partnership, or a nonbank corporation) should have no bearing on the categorization of the deposit. Thus, deposits placed in a bank by a deposit broker that is a nonbank corporation should not be reported in their entirety as

deposits of "individuals, partnerships, and corporations" when in fact the beneficial owners of the deposits are, for example, individuals, local governments, and other commercial banks. Instead, the bank should report these deposits in Schedule RC-E according to the appropriate beneficial owner categories as deposits of "Individuals, partnerships, and corporations," "States and political subdivisions in the U.S.," and "Commercial banks and other depository institutions in the U.S." based on the proportionate amount of funds from each category of depositor included in the brokered deposits the bank has received.

Investments in Trust Preferred Securities

A number of banks have invested in trust preferred securities, which are hybrid instruments possessing characteristics typically associated with debt obligations. Although each issue of these securities may involve minor differences in terms, under the basic structure of trust preferred securities a corporate issuer, such as a bank holding company, first organizes a business trust or other special purpose entity. This trust issues two classes of securities: common securities, all of which are purchased and held by the corporate issuer, and trust preferred securities, which are sold to investors. The business trust's only assets are deeply subordinated debentures of the corporate issuer, which the trust purchases with the proceeds from the sale of its common and preferred securities. The corporate issuer makes periodic interest payments on the subordinated debentures to the business trust, which uses these payments to pay periodic dividends on the trust preferred securities to the investors. The subordinated debentures have a stated maturity and may also be redeemed under other circumstances. Most trust preferred securities are subject to a mandatory redemption upon the repayment of the debentures.

Trust preferred securities meet the definition of a security in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Because of the mandatory redemption provision in the typical trust preferred security, investments in trust preferred securities would normally be considered debt securities for financial accounting purposes. Accordingly, regardless of the authority under which a bank is permitted to invest in trust preferred securities, banks should report these investments as debt securities for Call Report purposes (unless, based on the specific facts and circumstances of a particular issue of trust preferred securities, the securities would be considered equity rather than debt securities under Statement No. 115). If not held for trading purposes, trust preferred securities issued by U.S. business trusts should be reported in Schedule RC-B, item 6.a, "Other domestic debt securities."

Optional Tax Worksheet

For assistance in calculating 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. For a copy of this worksheet, state member banks should contact their Federal Reserve District Bank. National and FDIC-supervised banks should telephone the FDIC's Reports Analysis and Quality Control Section in Washington, D.C., toll free at (800) 688-FDIC or call (202) 898-6607. The optional tax worksheet for December 31, 2001, also is expected to be available on the FDIC's Web site by that date.

Call Report Software Vendors

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

DBI Financial Systems, Inc.
P.O. Box 90360
Santa Barbara, California
93190
Telephone: (800) 774-3279
www.e-dbi.com

Financial Architects US
35 Corporate Drive, 4th Floor
Burlington, Massachusetts
01803
Telephone: (781) 685-4956
www.finarch.com

FRS, an S1 Corporation
Business
2815 Coliseum Centre Drive,
Suite 300
Charlotte, North Carolina 28217
Telephone: (704) 423-0394
frs.s1.com

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

The InterCept Group
27200 Agoura Road, Suite 100
Calabasas Hills, California
91301
Telephone: (800) 825-3772
www.intercept.net

Jack Henry & Associates, Inc.
Banker-II Data Center
2405 Schneider Avenue, Suite
A
Menomonie, Wisconsin 54751
Telephone: (715) 235-8420

Milas LLC
2936 Graceland Way
Glendale, California 91206
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