FFIEC
Federal Financial Institutions Examination Council
Washington, D.C. 20006

CALL REPORT DATE: December 31, 2003

Financial Institution Letter

FIL-95-2003
December 18, 2003

SUPPLEMENTAL INSTRUCTIONS

December 2003 Call Report Materials

A sample set of the December 31, 2003, 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/ffiec_report_forms.htm) and the FDIC's Web site (www.fdic.gov/regulations/resources/call/index.html). 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, 2003, 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; IDOM, Inc.; 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.

Call Report Central Data Repository

The FFIEC has contracted with the Unisys Corporation to build a Central Data Repository (CDR) for the collection, validation, and distribution of Call Report data submitted by banks. The FFIEC anticipates that implementation of the new CDR system will start with the Call Reports for September 30, 2004. Under this new system, all institutions will be required to file their Call Reports via the Internet using software that contains the FFIEC edits for validating Call Report data prior to submission. Call Report software vendors are currently modifying their software to incorporate these edits.

As part of the CDR development process, a CDR Focus Group has been established to serve as a collaboration bridge for communication about the project with those institutions that file Call Reports. The Focus Group has representatives from bank trade groups, financial institutions, and the banking agencies. The Focus Group plans to provide information about the CDR project to the banking industry through the FFIEC's Web site and other means.

Amending Previously Submitted Reports

Should your bank find that it needs to revise certain Call Report information in a previously submitted report, an amended Call Report data file may be electronically submitted to EDS. Otherwise, contact your Call Report analyst at the FDIC (for national and FDIC-supervised banks) or at your Federal Reserve District Bank (for state member banks) and arrange to provide the amended data by telephone, fax, or electronic mail.

FFIEC Instruction Books

The most recent update to your Call Report instruction book was distributed with the June 2003 Call Report materials. 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.

GNMA Mortgage Loan Optional Repurchase Program

Government National Mortgage Association (GNMA) mortgage-backed securities are backed by residential mortgage loans that are insured or guaranteed by the Federal Housing Administration (FHA), the Department of Veterans Affairs/Veterans Administration (VA), or the Farmers Home Administration (FmHA). GNMA programs allow financial institutions to buy back individual delinquent mortgage loans that meet certain criteria from the securitized loan pool for which the institution provides servicing. At the servicer's option and without GNMA's prior authorization, the servicer may repurchase such a delinquent loan for an amount equal to 100 percent of the remaining principal balance of the loan. Under FASB Statement No. 140, this buy-back option is considered a conditional option until the delinquency criteria are met, at which time the option becomes unconditional.

When the loans backing a GNMA security are initially securitized, Statement No. 140 permits the issuer of the security to treat the transaction as a sale for accounting purposes because the conditional nature of the buy-back option means that the issuer does not maintain effective control over the loans. The loans are removed from the issuer's balance sheet. When individual loans later meet GNMA's specified delinquency criteria and are eligible for repurchase, the issuer (provided the issuer is also the servicer) is deemed to have regained effective control over these loans and, under Statement No. 140, the loans can no longer be reported as sold. The delinquent GNMA loans must be brought back onto the issuer-servicer's books as assets and initially recorded at fair value, regardless of whether the issuer intends to exercise the buy-back option. An offsetting liability also would be recorded. Whether or not these rebooked delinquent loans are repurchased, the issuer-servicer should report them as loans on the Call Report balance sheet (Schedule RC) and related schedules. These loans should be reported as held for sale (Schedule RC, item 4.a) or held for investment (Schedule RC, item 4.b), based on facts and circumstances, in accordance with generally accepted accounting principles. These loans should not be reported as "Other assets" (Schedule RC, item 11). The offsetting liability should be reported as "Other borrowed money" (Schedule RC, item 16).

For risk-based capital purposes, these rebooked loans should be risk-weighted in the same manner as all other FHA, VA, and FmHA loans, i.e., at 20 percent to the extent of the conditional guarantee. For leverage capital purposes, these rebooked loans should be included in the bank's average total assets.

Accounting for Indexed Retirement Plans

Banks that have agreements with individual employees to provide retirement benefits often fund the benefit obligation with the proceeds from bank-owned life insurance (BOLI). Some of these agreements are referred to as indexed retirement plans because retirement benefits are based upon the difference between the actual earnings on the BOLI and a predefined index ("excess spread"). If the agreements with individual employees, taken together, are equivalent to a postretirement income plan, then FASB

Statement No. 87, Employers' Accounting for Pensions, governs the accounting. Otherwise, each agreement should be accounted for individually on an accrual basis in accordance with the terms of the underlying contract as required by the provisions of Accounting Principles Board Opinion No. 12, Omnibus Opinion, addressing deferred compensation contracts.

Many employee agreements provide for future benefit payments from the excess spread that accrues before and after retirement on the related BOLI. Opinion No.12, as amended by FASB Statement No. 106, requires employer obligations under deferred compensation contracts to be accrued over the required service periods until the date the employee is fully eligible for the benefits ("full eligibility date"). However, some institutions have failed to record a liability for the estimated cost of benefit payments related to the excess spread that the employee will be entitled to receive after retirement. In addition, some institutions have failed to accrue the present value of the expected future benefit payments by the full eligibility date.

The failure to record a liability for the postretirement excess spread or to appropriately consider the impact of vesting provisions on the full eligibility date represents an accounting error. If an institution has made an error that is deemed material, it should make an adjustment to correct this accounting error and report the effect of the adjustment on retained earnings as of the beginning of the year in Schedule RI-A, item 2. The effect of the adjustment on earnings since the beginning of the year should be reflected in the appropriate income statement (Schedule RI) account on a year-to-date basis. The institution also should contact its primary federal supervisor to determine whether prior Call Reports should be amended.

Revisions to the estimated cost of future benefits because of changes in assumptions (e.g., changes in interest rates) should be accounted for as a change in accounting estimate and not as an accounting error.

FASB Statement No. 149 and Loan Commitments That Must Be Accounted for as Derivatives

FASB Statement No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities, provides guidance on the circumstances in which a loan commitment must be accounted for as derivative. This guidance applies to commitments issued after June 30, 2003. Commitments issued before July 1, 2003, are addressed by FASB Statement No. 133 Implementation Issue No. C13. Banks must follow the guidance in Statement No. 149 and Issue No. C13 for Call Report purposes. Statement No. 149 differs somewhat from Issue No. C13. For further information on Issue No. C13, please refer to the reporting guidance on loan commitments in the Call Report Supplemental Instructions for September 30, 2003. These Supplemental Instructions can be accessed via the FFIEC's Web site (www.ffiec.gov/PDF/FFIEC_forms/FFIEC031_041_suppinst0903.pdf).

Under Statement No. 149, loan commitments that relate to the origination of mortgage loans that will be held for sale, commonly referred to as interest rate lock commitments, must be accounted for as derivatives by the issuer of the commitment. Commitments to originate mortgage loans that will be held for investment purposes and commitments to originate other types of loans are not considered derivatives. However, for commitments to purchase or sell existing loans, the definition of a derivative in FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, (see page A-26 of the Glossary section of the Call Report instructions) should be applied to these commitments to determine whether they meet this definition and are subject to the provisions of Statement No. 133.

Interest rate lock commitments are considered over-the-counter written interest rate options. Therefore, because they are derivatives, these commitments should not be reported as unused commitments in item 1 of Schedule RC-L, Derivative and Off-Balance Sheet Items. Instead, interest rate lock commitments must be reported on the balance sheet (Schedule RC) at fair value. In addition, the par value of the mortgage loans to be originated under these commitments must be reported in Schedule RC L, item 12.d.(1), column A, and in Schedule RC-L, item 14, column A. Banks must also report the fair value of these interest rate lock commitments in the appropriate subitem of Schedule RC-L, item 15.b. As written options, interest rate lock commitments are outside the scope of the credit conversion process that applies to derivatives under the agencies' risk-based capital standards. However, if the fair value of these commitments is positive and therefore reported as an asset, this positive fair value is subject to the risk-based capital standards and must be risk weighted as an on-balance sheet asset.

The unused portion of loan commitments that are not considered derivatives should continue to be reported in Schedule RC-L, item 1. Unused commitments with an original maturity exceeding one year are subject to the risk-based capital standards and must be reported in Schedule RC-R, item 53.

FASB Interpretation No. 46

The FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities, in January 2003. This interpretation explains how to identify a “variable interest entity” (previously referred to as a “special purpose entity”) and how an institution should assess its interests in a variable interest entity to decide whether to consolidate that entity. Variable interest entities often are created for a single specified purpose, for example, to facilitate securitization, leasing, hedging, research and development, and reinsurance. Most small banks are unlikely to have any “variable interests” in variable interest entities.

In general, a variable interest entity is an entity in which either the controlling financial interests are not voting interests or the equity investors do not bear the entity’s residual economic risks. A variable interest is a contractual or ownership interest in an entity that changes when the value of the entity’s net assets changes. An organization that has a variable interest (or a combination of variable interests) that will absorb a majority of a variable interest entity’s expected losses if they occur, receive a majority of the entity’s expected residual returns if they occur, or both, is the “primary beneficiary” of the variable interest entity and must consolidate it.

For Call Report purposes, banks with variable interests in variable interest entities created after January 31, 2003, must apply the provisions of Interpretation No. 46 to those entities immediately. As announced in FASB Staff Position No. FIN 46-6 on October 9, 2003, a bank that is a public company, or a subsidiary of a public company, and has a variable interest in a variable interest entity created before February 1, 2003, need not apply the provisions of Interpretation No. 46 to its variable interest until the end of the first interim or annual reporting period ending after December 15, 2003, as long as the public company has not issued financial statements reporting that variable interest entity in accordance with the recognition and measurement provisions of the interpretation. A bank that is neither a public company nor a subsidiary of a public company, but has a variable interest in a variable interest entity created before February 15, 2003, must apply the provisions of Interpretation No. 46 to that entity no later than the end of the first annual reporting period beginning after June 15, 2003.

The assets and liabilities of a consolidated variable interest entity should be reported on the Call Report balance sheet (Schedule RC) on a line-by-line basis according to the asset and liability categories shown on the balance sheet. This reporting treatment also carries over to the other schedules in both the Report of Condition and the Report of Income.

Reporting Asset-Backed Commercial Paper Conduits in Schedules RC-L, RC-R, and RC-S

For purposes of Memorandum item 3 of Schedule RC-S, Servicing, Securitization, and Asset Sale Activities, banks must report the requested information on credit enhancements and liquidity facilities provided to asset-backed commercial paper conduits regardless of their accounting treatment for the conduit. Thus, whether or not a bank must consolidate the conduit for reporting purposes in accordance with FASB Interpretation No. 46, the bank must report its maximum credit exposure arising from and its unused commitments to conduit structures in Memorandum items 3.a and 3.b, respectively.

The banking agencies have issued an interim final rule that sets forth a temporary risk-based capital treatment for assets in asset-backed commercial paper conduits that sponsoring banks are required to consolidate in accordance with Interpretation No. 46. This interim capital treatment allows sponsoring banks to exclude the consolidated asset-backed commercial paper program assets from their risk weighted asset bases when they calculate their risk-based capital ratios. However, sponsoring banks must continue to hold risk-based capital against all exposures arising in connection with these programs, including direct credit substitutes, recourse obligations, residual interests, long-term liquidity facilities, and loans. Furthermore, any minority interests in consolidated asset-backed commercial paper programs are not eligible for inclusion in Tier 1 capital (or total risk-based capital). This interim risk-based capital treatment will be in effect only for the December 31, 2003, and March 31, 2004, Call Report dates. In addition, the interim risk-based capital treatment does not alter the accounting rules for balance sheet consolidation under Interpretation No. 46, nor does it affect the denominator of the Tier 1 leverage capital ratio calculation, which continues to be based primarily on on-balance sheet assets as reported under generally accepted accounting principles.

Under the agencies' interim rule, bank sponsors of any consolidated asset-backed commercial paper programs should include the consolidated assets in the appropriate balance sheet asset categories when completing items 34 through 43, column A, in Schedule RC-R, Regulatory Capital. The amounts of these consolidated assets should also be reported in items 34 through 43, column B, "Items not Subject to Risk-Weighting." However, sponsoring banks must continue to hold risk-based capital against all exposures arising in connection with these programs, whether or not the programs are consolidated, including direct credit substitutes, recourse obligations, residual interests, long-term liquidity facilities, and loans. These exposures should be reported in the appropriate items of Schedule RC-R. Any minority interests in consolidated asset-backed commercial paper programs should not be included in Schedule RC-R, item 6, “Qualifying minority interests in consolidated subsidiaries.”

For those asset-backed commercial paper programs that a bank consolidates, any credit enhancements and liquidity facilities the bank provides to the conduit should not be reported in Schedule RC-L, Derivatives and Off-Balance Sheet Items. In contrast, for programs that are not consolidated, the bank should report the credit enhancements and liquidity facilities it provides to the programs in the appropriate items of Schedule RC-L.

Reporting Gains and Losses from Extinguishments of Debt, Including Prepayment Penalties

Until it was rescinded by FASB Statement No. 145 in April 2002, FASB Statement No. 4 required gains and losses from the extinguishment (repayment or retirement) of debt to be aggregated and, if material, reported as extraordinary items. Under Statement No. 145, such gains and losses should be classified as extraordinary items only if they meet the criteria in Accounting Principles Board Opinion No. 30. For Call Report purposes, except for those unusual and infrequent gains and losses that qualify as extraordinary, banks should aggregate their gains and losses from the extinguishment of debt, including losses resulting from the payment of prepayment penalties on borrowings such as Federal Home Loan Bank advances, and consistently report the net amount in item 7.d, "Other noninterest expense," of the income statement (Schedule RI). Only if a bank's debt extinguishments normally result in net gains over time should the bank consistently report its net gains (losses) in Schedule RI, item 5.l, "Other noninterest income."

In addition, under FASB Emerging Issues Task Force (EITF) Issue No. 96-19, “Debtor’s Accounting for a Modification or Exchange of Debt Instruments,” the accounting for the gain or loss on the modification or exchange of debt depends on whether the original and the new debt instruments are substantially different. If they are substantially different, the transaction is treated as an extinguishment of debt and the gain or loss on the modification or exchange is reported immediately in earnings as discussed above. If the original and new debt instruments are not substantially different, the gain or loss on the modification or replacement of the debt is deferred and recognized over time as an adjustment to the interest expense on the new borrowing. EITF Issue No. 96-19 provides guidance on how to determine whether the original and the new debt instruments are substantially different.

Deposit Accounts on Which the Interest Rate Has Been Reduced to Zero

Many banks offer deposit products, such as money market deposit accounts or NOW accounts, on which they periodically adjust the interest rate paid on the accounts in response to changes in market interest rates and other factors. If a bank's rate adjustments on certain deposit accounts have reduced the interest rate to zero, but the interest rate paid on these accounts can be increased as market conditions change, the bank should continue to report the deposits as interest-bearing accounts in item 13 of Schedule RC, Balance Sheet, and include them in the appropriate deposit items in Schedule RC K, Quarterly Averages.

Equity-Indexed Certificates of Deposit

Under FASB Statement No. 133, a certificate of deposit (CD) that pays "interest" based on changes in an equity securities index is a hybrid instrument with an embedded derivative that must be accounted for separately from the host contract, i.e., the CD. Examples of equity-indexed CDs include the "Index Powered® CD" and the “Dow Jones Industrials Indexed Certificate of Deposit.”

Banks that either issue or invest in equity-indexed CDs should continue to follow the accounting and reporting guidance provided on this subject in the Call Report Supplemental Instructions for June 30, 2003. These Supplemental Instructions can be accessed via the FFIEC’s Web site (www.ffiec.gov/PDF/FFIEC_forms/FFIEC031_041_suppinst0603.pdf).

FASB Interpretation No. 45

For Call Report purposes, banks must follow FASB Interpretation No. 45, Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. Among the types of guarantee contracts to which Interpretation No. 45 applies are both financial and performance standby letters of credit. For further information, please refer to Interpretation No. 45 and to the Call Report Supplemental Instructions for June 30, 2003, which can be accessed via the FFIEC’s Web site (www.ffiec.gov/PDF/FFIEC_forms/FFIEC031_041_suppinst0603.pdf).

Reporting of Funds Invested Through Bentley Financial Services, Inc.

Banks should continue to follow the guidance provided on this subject in the Call Report Supplemental Instructions for June 30, 2003. These Supplemental Instructions can be accessed via the FFIEC’s Web site (www.ffiec.gov/PDF/FFIEC_forms/FFIEC031_041_suppinst0603.pdf).

Call Report Software Vendors

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

DBI Financial Systems, Inc.
P.O. Box 14027
Bradenton, Florida 34280
Telephone: (800) 774-3279
www.e-dbi.com

Financial Architects US
12040 Provincetowne Drive
Charlotte, North Carolina 28277
Telephone: (800) 763-7070
www.finarch.com

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

IDOM, Inc.
One Gateway Center, Third Floor
Newark, New Jersey 07102
Telephone: (973) 648-0900
www.idomusa.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
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