FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

NEWS RELEASE

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FDIC ADOPTS FINAL RULE IMPLEMENTING STATUTORY REQUIREMENTS FOR OUTSIDE AUDITS OF INSURED BANKS AND THRIFTS, OTHER SAFETY MEASURES

The FDIC Board of Directors today adopted a final rule implementing statutory requirements for outside audits of insured banks and thrifts and other measures to help detect and prevent problems in an institution's financial management.

The final rule implements Section 112 of the FDIC Improvement Act of 1991 (Section 36 of the Federal Deposit Insurance Act). The rule requires each insured institution over the threshold set by the FDIC -- total assets of $500 million or more -- to file an annual report with the agency, starting with fiscal years beginning after December 31, 1992. Section 36 also requires each institution subject to the audit requirements to establish an audit committee composed entirely of outside directors who must review the annual audit findings with management and the outside accountant. The law mandates that "large institutions," defined by the FDIC as those having $3 billion or more in total assets, have more stringent requirements for their audit committees. Any change in an outside auditor also by law must be brought to the attention of the FDIC by the institution.

The final rule adopted today is a mix of regulatory requirements and interpretive guidelines. The regulation mirrors the explicit requirements of Section 36 and is fully enforceable. The guidelines elaborate on those requirements but give discretion to bank managers and government examiners. FDIC officials noted that while the guidelines do not carry the same penalties as regulatory requirements, the agency has other enforcement tools at its disposal if an institution is acting recklessly. These protections

-more-include FDIC regulations that enforce safe and sound banking practices and safeguard the insurance funds.

FDIC Chairman Andrew C. Hove said: "The audit rule adopted today follows the letter of the law but also places on the banking system no greater regulatory burden than absolutely necessary. As such, the FDIC Board finds this to be a reasonable, balanced approach toward promoting safe and sound banking operations."

Chairman Hove added that the use of the guidelines "gives the FDIC the opportunity to field test this part of the regulation, and to adjust the guidelines as circumstances and conditions demand."

The new audit and reporting requirements will apply to about 1,000 of the approximately 14,000 FDIC-insured banks and thrifts, with about 75 percent of combined industry assets. As specified in the law, the required annual report must contain: an assessment by the institution's management of the effectiveness of its internal controls for financial reporting and its compliance with safety and soundness laws and regulations; financial statements audited by an independent public accountant; and the accountant's report on management's assertions regarding the institution's internal controls for financial reporting. The accountant also must report on the institution's compliance with designated safety and soundness laws and rules.

While all banks and thrifts covered by the rule will be required to have an independent audit committee comprised of outside directors, the FDIC expects that about 240 institutions with more than half the combined industry assets will be subject to the more stringent requirements. Those are: the audit committee must include at least two members with banking or related financial management expertise; "large customers" with significant credit or other relationships are prohibited from serving on the audit committee; and the committee must have access to its own outside counsel independent of management. The guidelines elaborate on what the FDIC recommends for complying with the law's requirements.

The FDIC decided to impose the regulation only on institutions with $500 million or more in assets because of concerns that many smaller institutions, especially those in small communities, would have problems attracting and retaining qualified outside directors to serve on their audit committee.

FDIC officials noted that about 96 percent of the institutions with $500 million or more in assets are known to already engage an independent public accountant to perform annual audits, while the rest use independent accountants for more limited audit work. Therefore, they said, the new rule and the use of the guidelines approach should not impose undue burdens on the affected institutions. The FDIC Board also agreed to include in its rulemaking a statement urging all insured institutions to voluntarily have audits by independent public accountants and establish audit committees.

The final rule is scheduled to go into effect 30 days after it is published in the Federal Register.

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