DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

FEDERAL RESERVE SYSTEM

FEDERAL DEPOSIT INSURANCE CORPORATION

Proposed Agency Information Collection Activities; Comment Request

AGENCIES: Office of the Comptroller of the Currency (OCC), Treasury; Board of Governors of the Federal Reserve System (Board); and Federal Deposit Insurance Corporation (FDIC).

ACTION: Joint notice and request for comment.

SUMMARY: In accordance with the requirements of the Paperwork Reduction Act of 1995 (44 U.S.C. chapter 35), the OCC, the Board, and the FDIC (the ''agencies'') may not conduct or sponsor, and the respondent is not required to respond to, an information collection unless it displays a currently valid Office of Management and Budget (OMB) control number. The Federal Financial Institutions Examination Council (FFIEC), of which the agencies are members, has approved the agencies' publication for public comment of a proposal to extend, with revision, the Consolidated Reports of Condition and Income (Call Report), which are currently approved collections of information. At the end of the comment period, the comments and recommendations received will be analyzed to determine the extent to which the FFIEC and the agencies should modify the proposed revisions prior to giving final approval. The agencies will then submit the revisions to OMB for review and approval.

DATES: Comments must be submitted on or before October 19, 2009.

ADDRESSES: Interested parties are invited to submit written comments to any or all of the agencies. All comments, which should refer to the OMB control number(s), will be shared among the agencies.

OCC: You should direct all written comments to: Communications Division, Office of the Comptroller of the Currency, Public Information Room, Mailstop 2–3, Attention: 1557–0081, 250 E Street, SW., Washington, DC 20219. In addition, comments may be sent by fax to (202) 874–5274, or by electronic mail to *regs.comments@occ.treas.gov*. You may personally inspect and photocopy comments at the OCC, 250 E Street, SW., Washington, DC 20219. For security reasons, the OCC requires that visitors make an appointment to inspect comments. You may do so by calling (202) 874–4700. Upon arrival, visitors will be required to present valid government-issued photo identification and to submit to security screening in order to inspect and photocopy comments.

Board: You may submit comments, which should refer to ''Consolidated Reports of Condition and Income, 7100–0036,'' by any of the following methods:

- *Agency Web site: http://www.federalreserve.gov*. Follow the instructions for submitting comments on the *http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm*.
- *Federal eRulemaking Portal: http://www.regulations.gov*. Follow the instructions for submitting comments.
- *E-mail: regs.comments@federalreserve.gov*. Include the OMB control number in the subject line of the message.
- *Fax:* 202–452–3819 or 202–452–3102.
- *Mail:* Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments are available from the Board's Web site at *http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm* as submitted, unless modified for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper in Room MP–500 of the Board's Martin Building (20th and C Streets, NW.) between 9 a.m. and 5 p.m. on weekdays.

FDIC: You may submit comments, which should refer to ''Consolidated Reports of Condition and Income, 3064–0052,'' by any of the following methods:

- *Agency Web site: http://www.fdic.gov/regulations/laws/federal/propose.html*. Follow the instructions for submitting comments on the FDIC Web site.
- *Federal eRulemaking Portal: http://www.regulations.gov*. Follow the instructions for submitting comments.
- *E-mail: comments@FDIC.gov*. Include ''Consolidated Reports of Condition and Income, 3064–0052'' in the subject line of the message.
- *Mail:* Herbert J. Messite (202–898–6834), Counsel, Attn: Comments, Room F–1052, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.
- *Hand Delivery:* Comments may be hand delivered to the guard station at the rear of the 550 17th Street Building (located on F Street) on business days between 7 a.m. and 5 p.m.

Public Inspection: All comments received will be posted without change to *http://www.fdic.gov/regulations/laws/federal/propose.html* including any personal information provided. Comments may be inspected at the FDIC Public Information Center, Room E–1002, 3501 Fairfax Drive, Arlington, VA 22226, between 9 a.m. and 5 p.m. on business days.

Additionally, commenters may send a copy of their comments to the OMB desk officer for the agencies by mail to the Office of Information and Regulatory Affairs, U.S. Office of Management and Budget, New Executive Office Building, Room 10235, 725 17th Street, NW., Washington, DC 20503, or by fax to (202) 395–6974.

FOR FURTHER INFORMATION CONTACT: For further information about the revisions discussed in this notice, please contact any of the agency clearance officers whose names appear below. In addition, copies of the Call Report forms can be obtained at the FFIEC's Web site (*http://www.ffiec.gov/ffiec_report_forms.htm*).

OCC: Mary Gottlieb, OCC Clearance Officer, (202) 874–5090, Legislative and Regulatory Activities Division, Office of the Comptroller of the Currency, 250 E Street, SW., Washington, DC 20219.

Board: Michelle Shore, Federal Reserve Board Clearance Officer, (202) 452–3829, Division of Research and Statistics, Board of Governors of the Federal Reserve System, 20th and C Streets, NW., Washington, DC 20551. Telecommunications Device for the Deaf (TDD) users may call (202) 263–4869.

FDIC: Herbert J. Messite, Counsel, (202) 898–6834, Legal Division, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.

SUPPLEMENTARY INFORMATION: The agencies are proposing to revise and extend for three years the Call Report, which is currently an approved collection of information for each agency.

Report Title: Consolidated Reports of Condition and Income (Call Report).

Form Number: Call Report: FFIEC 031 (for banks with domestic and foreign offices) and FFIEC 041 (for banks with domestic offices only).

Frequency of Response: Quarterly.

Affected Public: Business or other for-profit.

OCC

OMB Number: 1557–0081.

Estimated Number of Respondents: 1,569 national banks.

Estimated Time per Response: 49.33 burden hours.

Estimated Total Annual Burden: 309,595 burden hours.

Board

OMB Number: 7100–0036.

Estimated Number of Respondents: 861 state member banks.

Estimated Time per Response: 55.08 burden hours.

Estimated Total Annual Burden: 189,696 burden hours.

FDIC

OMB Number: 3064–0052.

Estimated Number of Respondents: 5,032 insured state nonmember banks.

Estimated Time per Response: 39.15 burden hours.

Estimated Total Annual Burden: 788,011 burden hours.

The estimated time per response for the Call Report is an average that varies by agency because of differences in the composition of the institutions under each agency's supervision (*e.g.,* size distribution of institutions, types of activities in which they are engaged, and existence of foreign offices). The average reporting burden for the Call Report is estimated to range from 16 to 655 hours per quarter, depending on an individual institution's circumstances.

General Description of Reports

These information collections are mandatory: 12 U.S.C. 161 (for national banks), 12 U.S.C. 324 (for state member banks), and 12 U.S.C. 1817 (for insured state nonmember commercial and savings banks). At present, except for selected data items, these information collections are not given confidential treatment.

Abstract

Institutions submit Call Report data to the agencies each quarter for the agencies' use in monitoring the condition, performance, and risk profile of individual institutions and the industry as a whole. Call Report data provide the most current statistical data available for evaluating institutions' corporate applications, for identifying areas of focus for both on-site and off-site examinations, and for monetary and other public policy purposes. The agencies use Call Report data in evaluating interstate merger and acquisition applications to determine, as required by law, whether the resulting institution would control more than ten percent of the total amount of deposits of insured depository institutions in the United States. Call Report data are also used to calculate institutions' deposit insurance and Financing Corporation assessments and national banks' semiannual assessment fees.

Current Actions

I. Overview

The agencies are proposing to implement certain changes to the Call Report requirements in 2010 that are intended to provide data needed for reasons of safety and soundness or other public purposes. These proposed revisions respond, for example, to a change in accounting standards, a temporary increase in the deposit insurance limit, and credit availability concerns.

The proposed Call Report changes that are the subject of this proposal would take effect as of March 31, 2010, unless otherwise indicated. These revisions, which are discussed in detail in Sections II.A. through J. of this notice, include:

- New items identifying total other-than-temporary impairment losses on debt securities, the portion of the total recognized in other comprehensive income, and the net losses recognized in earnings, consistent with the presentation requirements of a recent accounting standard;
- Clarification of the instructions for reporting unused commitments;
- Breakdowns of the existing items for unused credit card lines and other unused commitments, with the former breakdown required only for certain institutions, and a related breakdown of the existing item for other loans;
- New items pertaining to reverse mortgages that would be collected annually as of December 31;
- A breakdown of the existing item for time deposits of $100,000 or more (in domestic offices);
- Revisions of existing items for brokered deposits;
- New items for the interest expense and quarterly averages for fully insured brokered time deposits and other brokered time deposits;
- A change in the reporting frequency for small business and small farm lending data from annually to quarterly;
- A change in the reporting frequency for the number of certain deposit accounts from annually to quarterly; and
- The elimination of the item for internal allocations of income and expense from the schedule for income from foreign offices.

The agencies seek to establish reporting thresholds for the collection of Call Report information where practicable to limit the reporting burden imposed on banking institutions. In establishing such thresholds, the agencies weigh the characteristics of the institutions involved in the activity that would be subject to the reporting requirements, the number of institutions affected by the reporting requirements, the type of information being collected, how that information will be used by the agencies, and banks' costs associated with gathering and reporting the requested information. The agencies solicit comments from banking institutions related to the proposals described in this notice. Are there appropriate reporting thresholds for specific proposed changes that will enable the agencies to collect meaningful information without creating undue burden for institutions? Please provide specific feedback regarding the amount of burden created by the proposed amendments as well as suggestions for thresholds that would reduce this burden without compromising the usefulness of the data.

For the March 31 and December 31, 2010 report dates, banks may provide reasonable estimates for any new or revised Call Report item initially required to be reported as of that date for which the requested information is not readily available. The specific wording of the captions for the new or revised Call Report data items discussed in this proposal and the numbering of these data items should be regarded as preliminary.

Type of Review: Revision and extension of currently approved collections.

II. Discussion of Proposed Call Report Revisions

A. Other-Than-Temporary Impairment Losses on Debt Securities

On April 9, 2009, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) No. 115–2 and 124–2, *Recognition and Presentation of Other-Than-Temporary Impairments* (FSP FAS 115–2).[1] This FSP amended the other-than-temporary impairment guidance in other accounting standards that applies to investments in debt securities. Under FSP FAS 115–2, if a bank intends to sell a debt security or it is more likely than not that it will be required to sell the debt security before recovery of its amortized cost basis, an other-than-temporary impairment has occurred and the entire difference between the security's amortized cost basis and its fair value at the balance sheet date must be recognized in earnings. FSP FAS

[1] Under the FASB Accounting Standards Codification™, see Topic 320, Investments—Debt and Equity Securities.

115–2 also provides that if the present value of cash flows expected to be collected on a debt security is less than its amortized cost basis, a credit loss exists. In this situation, if a bank does not intend to sell the security and it is not more likely than not that the bank will be required to sell the debt security before recovery of its amortized cost basis less any current-period credit loss, an other-than-temporary impairment has occurred. The amount of the total other-than-temporary impairment related to the credit loss must be recognized in earnings, but the amount of the total impairment related to other factors must be recognized in other comprehensive income, net of applicable taxes.

For other-than-temporary impairment losses on held-to-maturity and available-for-sale debt securities, banks report the amount of the other-than-temporary impairment losses that must be recognized in earnings in items 6.a and 6.b of the Call Report income statement (Schedule RI), respectively. Other-than-temporary impairment losses that are to be recognized in other comprehensive income, net of applicable taxes, are reported in Schedule RI–A, Changes in Bank Equity Capital, item 10, ''Other comprehensive income.'' However, because items 6.a and 6.b of Schedule RI also include other amounts such as gains (losses) on sales of held-to-maturity and available-for-sale securities, the agencies currently are not able to determine the effect on the net income of banks, individually and in the aggregate, of other-than-temporary impairment losses that must be recognized in earnings. Similarly, because item 10 of Schedule RI–A includes all of the other components of a bank's other comprehensive income, the agencies cannot identify the portion of other comprehensive income attributable to other-than-temporary impairment losses for banks individually and in the aggregate.

According to FSP FAS 115–2, in a period in which a bank determines that a debt security's decline in fair value below its amortized cost basis is other than temporary, the bank must present the total other-than-temporary impairment loss in the income statement with an offset for the amount of the total loss that is recognized in other comprehensive income. This new presentation provides additional information about the amounts that a bank does not expect to collect related to its investments in debt securities held for purposes other than trading. Therefore, to enhance the agencies' ability to evaluate the factors affecting bank earnings, the agencies propose to add three Memorandum items to the Call Report income statement that would mirror the presentation requirements of FSP FAS 115–2. In these new Memorandum items, banks would report total other-than-temporary impairment losses on debt securities for the calendar year-to-date reporting period, the portion of these losses recognized in other comprehensive income, and the net losses recognized in earnings

B. Clarification of the Instructions for Reporting Unused Commitments

Banks report unused commitments in item 1 of Schedule RC–L, Derivatives and Off-Balance Sheet Items. The instructions for this item identify various arrangements that should be reported as unused commitments, including but not limited to commitments for which the bank has charged a commitment fee or other consideration, commitments that are legally binding, loan proceeds that the bank is obligated to advance, commitments to issue a commitment, and revolving underwriting facilities. However, the agencies have found that some banks have not reported commitments that they have entered into until they have signed the loan agreement for the financing that they have committed to provide. Although the agencies consider these arrangements to be commitments to issue a commitment and, therefore, within the scope of the existing instructions for reporting commitments in Schedule RC–L, they believe that these instructions may not be sufficiently clear. Therefore, the agencies originally proposed to revise the instructions for Schedule RC–L, item 1, ''Unused commitments,'' as one of the proposed Call Report changes for implementation as of March 31, 2009.[2] More specifically, with respect to commitments to issue a commitment at some point in the future, the agencies proposed to add language to the instructions for this item explicitly stating that such commitments include those that have been entered into even though the related loan agreement has not yet been signed.

In response to the agencies' request for comment on Call Report revisions for 2009, three commenters specifically addressed the proposed instructional clarification pertaining to unused commitments. One commenter agreed that clarification is needed, but recommended that commitments to issue a commitment in the future, including those entered into even though the related loan agreement has not yet been signed, should be removed from the list of types of arrangements that the instructions would direct banks to report as unused commitments. A second commenter expressed concern about reporting ''commitments that contain a relatively high level of uncertainty until a loan agreement has been signed or the loan has been funded with a first advance'' and the reliability of data on such commitments. The third commenter stated that because some banks do not have systems for tracking such arrangements, the instructions should in effect permit banks to exclude commitment letters with an expiration date of 90 days or less. Finally, the first commenter also recommended that the instructions for reporting unused commitments should state that amounts conveyed or participated to others that the conveying or participating bank is not obligated to fund should not be reported as unused commitments by the conveying or participating bank.

After evaluating these comments, the agencies have refined their approach to identifying commitments to issue a commitment in a manner that is intended to address the commenters' concerns by focusing on a point in the commitment process when the agencies believe that banks' systems should be tracking their commitments. Thus, the instructions would state that commitments to issue a commitment at some point in the future are those where the bank has extended terms and the borrower has accepted the offered terms, even though the related loan agreement has not yet been signed. In addition, the agencies agree with the commenter's recommendation concerning commitments that have been conveyed or participated to others and are proposing to modify the instructions accordingly.

The proposed revised instructions for Schedule RC–L, item 1, would read as follows:

Report in the appropriate subitem the unused portions of commitments. Unused commitments are to be reported gross, *i.e.,* include in the appropriate subitem the unused amount of commitments acquired from and conveyed or participated to others. However, exclude commitments conveyed or participated to others that the bank is not legally obligated to fund even if the party to whom the commitment has been conveyed or participated fails to perform in accordance with the terms of the commitment.

For purposes of this item, commitments include:

[2] 73 FR 54811, September 23, 2008.

(1) Commitments to make or purchase extensions of credit in the form of loans or participations in loans, lease financing receivables, or similar transactions.

(2) Commitments for which the bank has charged a commitment fee or other consideration.

(3) Commitments that are legally binding.

(4) Loan proceeds that the bank is obligated to advance, such as:

(a) Loan draws;

(b) Construction progress payments; and

(c) Seasonal or living advances to farmers under prearranged lines of credit.

(5) Rotating, revolving, and open-end credit arrangements, including, but not limited to, retail credit card lines and home equity lines of credit.

(6) Commitments to issue a commitment at some point in the future, where the bank has extended terms and the borrower has accepted the offered terms, even though the related loan agreement has not yet been signed.

(7) Overdraft protection on depositors' accounts offered under a program where the bank advises account holders of the available amount of overdraft protection, for example, when accounts are opened or on depositors' account statements or ATM receipts.

(8) The bank's own takedown in securities underwriting transactions.

(9) Revolving underwriting facilities (RUFs), note issuance facilities (NIFs), and other similar arrangements, which are facilities under which a borrower can issue on a revolving basis short-term paper in its own name, but for which the underwriting banks have a legally binding commitment either to purchase any notes the borrower is unable to sell by the rollover date or to advance funds to the borrower.

Exclude forward contracts and other commitments that meet the definition of a derivative and must be accounted for in accordance with FASB Statement No. 133, which should be reported in Schedule RC–L, item 12. Include the amount (not the fair value) of the unused portions of loan commitments that do not meet the definition of a derivative that the bank has elected to report at fair value under a fair value option. Also include forward contracts that do not meet the definition of a derivative. The unused portions of commitments are to be reported in the appropriate subitem regardless of whether they contain ''material adverse change'' clauses or other provisions that are intended to relieve the issuer of its funding obligations under certain conditions and regardless of whether they are unconditionally cancelable at any time.

In the case of commitments for syndicated loans, report only the bank's proportional share of the commitment.

For purposes of reporting the unused portions of revolving asset-based lending commitments, the commitment is defined as the amount a bank is obligated to fund—as of the report date—based on the contractually agreed upon terms. In the case of revolving asset-based lending, the unused portions of such commitments should be measured as the difference between (a) the lesser of the contractual borrowing base (*i.e.,* eligible collateral times the advance rate) or the note commitment limit, and (b) the sum of outstanding loans and letters of credit under the commitment. The note commitment limit is the overall maximum loan amount beyond which the bank will not advance funds regardless of the amount of collateral posted. This definition of ''commitment'' is applicable only to revolving asset-based lending, which is a specialized form of secured lending in which a borrower uses current assets (*e.g.,* accounts receivable and inventory) as collateral for a loan. The loan is structured so that the amount of credit is limited by the value of the collateral.

C. Additional Categories of Unused Commitments and Loans

The extent to which banks are reducing the supply of credit during the current financial crisis has been of great interest to the agencies and to Congress. Also, bank lending plays a central role in any economic recovery and the agencies need data to better determine when credit conditions have eased. One way to measure the supply of credit is to analyze the change in total lending commitments by banks, considering both the amount of loans outstanding and the volume of unused credit lines. These data are also needed for safety and soundness purposes because draws on commitments during periods when banks face significant funding pressures, such as during the fall of 2008, can place significant and unexpected demands on the liquidity and capital positions of banks. Therefore, the agencies propose breaking out in further detail two categories of unused commitments on Schedule RC–L, Derivatives and Off-Balance Sheet Items. The agencies also propose to break out in further detail one new loan category on Schedule RC–C, part I, Loans and Leases. These new data items would improve the agencies' ability to obtain timely and accurate readings on the supply of credit available to households and businesses. These data would also be useful in determining the effectiveness of the government's economic stabilization programs.

Unused commitments associated with credit card lines are reported in Schedule RC–L, item 1.b. This data item is not sufficiently meaningful for monitoring the supply of credit because it mixes consumer credit card lines with credit card lines for businesses and other entities. As a result of this aggregation, it is not possible to fully monitor credit available specifically to households. Furthermore, bank supervisors would benefit from the split, because the usage patterns, profitability, and evolution of credit quality through the business cycle are likely to differ for consumer credit cards and business credit cards. Therefore, the agencies propose to split Schedule RC–L, item 1.b, into unused consumer credit card lines and other unused credit card lines. This breakout would be reported by institutions with either $300 million or more in total assets or $300 million or more in unused credit card commitments. Draws from these credit lines that have not been sold are already reported on Schedule RC–C, part I. For example, banks must report draws on credit cards issued to nonfarm nonfinancial businesses as commercial and industrial (C&I) loans in Schedule RC–C, part I, item 4, and draws on personal credit cards as consumer loans in Schedule RC–C, part I, item 6.a.

Schedule RC–L, item 1.e, aggregates all other unused commitments, and includes unused commitments to fund C&I loans (other than credit card lines to commercial and industrial enterprises, which are reported in item 1.b, and commitments to fund commercial real estate, construction, and land development loans not secured by real estate, which are reported in item 1.c.(2)). Separating these C&I lending commitments from the other commitments included in other unused commitments would considerably improve the agencies' ability to analyze business credit conditions. A very large percentage of banks responding to the Federal Reserve's Senior Loan Officer Opinion Survey on Bank Lending Practices (FR 2018; OMB No. 7100–0058) reported having tightened lending policies for C&I loans and credit lines during 2008; however, C&I loans on banks' balance sheets expanded through the end of October 2008, reportedly as a result of substantial draws on existing credit lines. In contrast, other unused commitments reported on the Call Report contracted, but without the proposed breakouts of such commitments, it was not possible to

know how total business borrowing capacity had changed. The FR 2018 data are qualitative rather than quantitative and are collected only from a sample of institutions up to six times per year. Having the additional unused commitment data reported separately on the Call Report, along with the proposed changes to Schedule RC–C described below, would have indicated more clearly whether there was a widespread restriction in new credit available to businesses.

Therefore, the agencies propose to split Schedule RC–L, item 1.e, into three categories: Unused commitments to fund commercial and industrial loans (which would include only commitments not reported in Schedule RC–L, items 1.b and 1.c.(2), for loans that, when funded, would be reported in Schedule RC–C, item 4), unused commitments to fund loans to financial institutions (defined to include depository institutions and nondepository financial institutions, *i.e.*, real estate investment trusts, mortgage companies, holding companies of other depository institutions, insurance companies, finance companies, mortgage finance companies, factors and other financial intermediaries, short-term business credit institutions, personal finance companies, investment banks, the bank's own trust department, other domestic and foreign financial intermediaries, and Small Business Investment Companies), and all other unused commitments. With respect to Schedule RC–C, part I, the agencies also propose to revise item 9, ''Other loans,'' by breaking out a new category for loans to nondepository financial institutions (as defined above). Banks already report data on loans to depository institutions in Schedule RC–C, part I, item 2.

Lending by nondepository financial institutions was a key characteristic of the recent credit cycle and many such institutions failed; however, little information existed on the exposure of the banking system to those firms as this information was obscured by the current structure of the Call Report's loan schedule. The proposed addition of separate items for unused commitments to financial institutions and loans to nondepository financial institutions, together with the existing data on loans to depository institutions, will allow supervisors and other interested parties to more closely monitor the exposure of individual banks to financial institutions and to assess the impact that changes in the credit availability to this sector have on the economy.

D. Reverse Mortgage Data

Reverse mortgages are complex loan products that leverage equity in homes to provide lump sum cash payments or lines of credit to borrowers. These products are typically marketed to senior citizens who own homes. The agencies are currently unable to effectively identify and monitor institutions that offer these products due to a lack of reverse mortgage data.

The reverse mortgage market currently consists of two basic types of products: Proprietary products designed and originated by financial institutions and a federally-insured product known as a Home Equity Conversion Mortgage (HECM). Some reverse mortgages provide for a lump sum payment to the borrower at closing, with no ability for the borrower to receive additional funds under the mortgage at a later date. Other reverse mortgages are structured like home equity lines of credit in that they provide the borrower with additional funds after closing, either as fixed monthly payments, under a line of credit, or both. There are also reverse mortgages that provide a combination of a lump sum payment to the borrower at closing and additional payments to the borrower after the closing of the loan.

The volume of reverse mortgage activity is expected to dramatically increase in the coming years as the U.S. population ages. A number of consumer protection related risks and safety and soundness related risks are associated with these products and the agencies need to collect information from banks involved in the reverse mortgage activities to monitor and mitigate those risks. For example, proprietary reverse mortgages structured as lines of credit, which are not insured by the federal government, expose borrowers to the risk that the lender will be unwilling or unable to meet its obligation to make payments due to the borrower. Additionally, in those circumstances in which housing prices are declining, there is the risk that the reverse mortgage loan balance may exceed the value of the underlying collateral value of the home.

As stated above, access to data regarding loan volumes, dollar amounts outstanding, and the institutions offering reverse mortgages or participating in reverse mortgage activity is severely limited. The U.S. Department of Housing and Urban Development provides a monthly report for reverse mortgages endorsed for federal insurance, by fiscal year, for those loans that are part of the federally-sponsored HECM program. While this monthly report provides information such as average expected interest rates, average property values, average age of the borrower, and the number of active insured accounts, there is no aggregate monthly data nor is there institution-specific information that identifies the institutions participating in the program. For proprietary reverse mortgage loans, there is no known data on the volume of reverse mortgages, dollar amounts outstanding, or the institutions offering these products.

The agencies propose that new items be added to the Call Report to collect reverse mortgage data on an annual basis beginning on December 31, 2010. Collecting this information will provide the agencies the necessary information for policy development and the management of risk exposures posed by institutions' involvement with reverse mortgages. First, a new Memorandum item would be added to Schedule RC–C, part I, Loans and Leases, for ''Reverse mortgages outstanding that are held for investment.'' In this Memorandum item, banks would separately report the amount of HECM reverse mortgages and the amount of proprietary reverse mortgages that are held for investment and included in Schedule RC–C, part I, item 1.c, Loans ''Secured by 1–4 family residential properties.'' Additionally, new items would be added to Schedule RC–L, Derivatives and Off-Balance Sheet Items, to collect the amounts of ''Unused commitments for HECM reverse mortgages outstanding that are held for investment'' and ''Unused commitments for proprietary reverse mortgages outstanding that are held for investment.'' Because these reverse mortgages have been structured in whole or in part like home equity lines of credit, the unused commitments associated with these mortgages are also reportable in existing item 1.a, ''Revolving, open-end lines secured by 1–4 family residential properties,'' of Schedule RC–L. The proposed new unused commitment items would be subsets of item 1.a.

In many instances, institutions do not underwrite and fund reverse mortgages, but refer borrowers to other reverse mortgage lenders. These institutions receive a fee for referring customers to the reverse mortgage lender and they may be involved in (although their involvement may not be limited to) the following activities: Marketing the reverse mortgage loan product, providing information on or answering questions about the reverse mortgage loan, selling products in conjunction with reverse mortgages, and/or accepting an application for a reverse mortgage from the potential borrower. This model enables consumers to deal

first with their local institutions without the institutions having to build an entirely new lending function. It also provides an economy of scale for a specialized lender because they will not necessarily need a large physical branch network when they can partner with existing lenders. The banking agencies propose adding a new Memorandum item to Schedule RC–C, part I, to annually collect the estimated number of fee-paid referrals during the year from each bank making referrals beginning on December 31, 2010. Banks would report separately the estimated number of fee-paid referrals for HECM reverse mortgages and proprietary reverse mortgages.

The agencies request specific feedback from reporting institutions on their ability to provide fee-paid referral information for reverse mortgages. Do banks maintain the data necessary to provide an estimate of the number of fee paid referrals they have made during the year? Would it be less burdensome for banks to report an estimated number of fee-paid referrals for reverse mortgages that falls within specified ranges of numbers? Is there alternative information that the agencies could collect in order to better understand the extent of banks' reverse mortgage referral activities?

Finally, many banks that originate reverse mortgages routinely sell their funded mortgages in the secondary market. As a result, these loans will not remain on the originating banks' balance sheets for long periods of time and, therefore, the proposed items for reverse mortgages outstanding that are held for investment will not capture the extent of banks' reverse mortgage activity when it involves the origination and sale of these loans. Thus, the agencies propose to add Memorandum items to Schedule RC–C, part I, in which banks would report the principal amount of reverse mortgages originated for sale that have been sold during the year. HECM and proprietary reverse mortgages sold would be reported separately. These items are distinct and separate from the items for the estimated number of referrals because the referring bank is not funding the loan, but is merely taking an application or conducting another service in order to refer the borrower to another institution that ultimately funds the reverse mortgage. The information on loans sold during the year also would be collected annually beginning on December 31, 2010.

E. Time Deposits of $100,000 or More

On October 3, 2008, the Emergency Economic Stabilization Act of 2008 temporarily raised the standard maximum deposit insurance amount (SMDIA) from $100,000 to $250,000 per depositor. Under this legislation, the SMDIA was to return to $100,000 after December 31, 2009. However, on May 20, 2009, the Helping Families Save Their Homes Act extended this temporary increase in the SMDIA to $250,000 per depositor through December 31, 2013, after which the SMDIA is scheduled to return to $100,000.

At present, banks report a two-way breakdown of their time deposits (in domestic offices) in Schedule RC–E, Deposit Liabilities, distinguishing between time deposits of less than $100,000 and time deposits of $100,000 or more. In response to the extension of the temporary increase in the limit on deposit insurance coverage, the agencies understand that time deposits with balances in excess of $100,000, but less than or equal to $250,000, have been growing and can be expected to increase further. However, given the existing Schedule RC–E reporting requirements, the agencies are unable to monitor growth in banks' time deposits with balances within the temporarily increased limit on deposit insurance coverage.

Therefore, the agencies are proposing to replace Schedule RC–E, Memorandum item 2.c, ''Total time deposits of $100,000 or more,'' with a revised Memorandum item 2.c, ''Total time deposits of $100,000 through $250,000,'' and a new Memorandum item 2.d, ''Total time deposits of more than $250,000.'' Existing Memorandum item 2.c.(1), ''Individual Retirement Accounts (IRAs) and Keogh Plan accounts included in Memorandum item 2.c, 'Total time deposits of $100,000 or more,' above,'' would be renumbered and recaptioned as Memorandum item 2.e, ''Individual Retirement Accounts (IRAs) and Keogh Plan accounts of $100,000 or more included in Memorandum items 2.c and 2.d above,'' but the scope of this Memorandum item would not change.

F. Revisions of Brokered Deposit Items

As mentioned in Section I*I.E.* above, the SMDIA has been increased temporarily from $100,000 to $250,000 through year-end 2013. However, the data that banks currently report in the Call Report on fully insured brokered deposits in Schedule RC–E, Memorandum items 1.c.(1) and 1.c.(2), is based on the $100,000 insurance limit (except for brokered retirement deposit accounts for which the deposit insurance limit was already $250,000). Therefore, in response to the temporary increase in the SMDIA, the agencies are proposing to revise the reporting of fully insured brokered deposits in Schedule RC–E. Furthermore, given the linkage between the deposit insurance limits and the Memorandum items on fully insured brokered deposits in Schedule RC–E, the scope of these items needs to be changed whenever deposit insurance limits change. To ensure that the scope of these Memorandum items, including the dollar amounts cited in the captions for these items, changes automatically as a function of the deposit insurance limit in effect on the report date, Memorandum item 1.c, ''Fully insured brokered deposits,'' would be footnoted to state that the specific dollar amounts used as the basis for reporting fully insured brokered deposits in Memorandum items 1.c.(1) and 1.c.(2) reflect the deposit insurance limits in effect on the report date. The instructions for Memorandum item 1.c would be similarly clarified.[3]

In addition, consistent with the reporting of time deposits in other items of Schedule RC–E, brokered deposits would be reported based on their balances rather than the denominations in which they were issued.

Accordingly, Memorandum items 1.c.(1) and 1.c.(2) of Schedule RC–E and their instructions would be revised as follows:

- Memorandum item 1.c.(1), ''Brokered deposits of less than $100,000'': Report in this item brokered deposits with balances of less than $100,000. Also report in this item time deposits issued to deposit brokers in the form of large ($100,000 or more) certificates of deposit that have been participated out by the broker in shares with balances of less than $100,000. For brokered deposits that represent retirement deposit accounts (as defined in Schedule RC–O, Memorandum item 1) eligible for $250,000 in deposit insurance coverage, report such brokered deposits in this item only if their balances are less than $100,000.
- Memorandum item 1.c.(2), ''Brokered deposits of $100,000 through $250,000 and certain brokered retirement deposit accounts'': Report in this item brokered deposits (including brokered retirement deposit accounts) with balances of $100,000 through

[3] The proposed linkage of the scope of the Memorandum items on fully insured brokered deposits in Schedule RC–E to the deposit insurance limits in effect on the report date is consistent with an existing linkage between the deposit insurance limits in effect on the report date and the Memorandum items in Schedule RC–O, Other Data for Deposit Insurance and FICO Assessments, on the amount and number of deposit accounts within the insurance limit and in excess of the insurance limit.

$250,000. Also report in this item brokered deposits that represent retirement deposit accounts (as defined in Schedule RC–O, Memorandum item 1) eligible for $250,000 in deposit insurance coverage that have been issued by the bank in denominations of more than $250,000 that have been participated out by the broker in shares of $100,000 through exactly $250,000.

The proposed revisions to Schedule RC–E, Memorandum items 1.c.(1) and 1.c.(2), that relate to the temporary increase in the SMDIA would remain in effect during this increase, after which the dollar amounts used as the basis for reporting fully insured brokered deposits in these items would revert to the amounts in effect prior to the temporary increase.

The agencies are not proposing to revise the existing requirements for the reporting of maturity data on brokered deposits in Memorandum items 1.d.(1) and 1.d.(2) of Schedule RC–E.

G. Interest Expense on and Quarterly Averages for Brokered Deposits

Under Section 29 of the Federal Deposit Insurance Act (12 U.S.C. 1831f), an insured depository institution that is less than well capitalized generally may not pay a rate of interest that significantly exceeds the prevailing rate in the institution's ''normal market area'' and/or the prevailing rate in the ''market area'' from which the deposit is accepted. In the case of an adequately capitalized institution with a waiver to accept brokered deposits, the institution may not pay a rate of interest on brokered deposits accepted from outside the bank's ''normal market area'' that significantly exceeds the ''national rate'' as defined by the FDIC. On May 29, 2009, the FDIC's Board of Directors adopted a final rule making certain revisions to the interest rate restrictions under Section 337.6 of the FDIC's regulations. Under the final rule, the ''national rate'' is a simple average of rates paid by U.S. depository institutions as calculated by the FDIC.[4] When evaluating compliance with the interest rate restrictions in Section 337.6 by an institution that is less than well capitalized, the FDIC generally will deem the national rate to be the prevailing rate in all market areas. The final rule is effective January 1, 2010.

At present, the agencies are unable to evaluate the level and trend of the cost of brokered time deposits to institutions that have acquired such funds, nor can the agencies compare the cost of such deposits across institutions with brokered time deposits. Data on the cost of brokered deposits would also assist the agencies in evaluating the overall cost of institutions' time deposits, for which data have long been collected in the Call Report. Furthermore, many of the banks that have failed since the beginning of 2008 have relied extensively on brokered deposits to support their asset growth. Therefore, to enhance the agencies' ability to evaluate funding costs and the impact of brokered time deposits on these costs, the agencies are proposing to add two Memorandum items to both Schedule RC–K, Quarterly Averages, and Schedule RI, Income Statement. In these Memorandum items, banks would report the interest expense and quarterly averages for ''fully insured brokered time deposits'' and ''other brokered time deposits.'' The definition of ''fully insured brokered time deposits'' would be based on the definitions of ''fully insured brokered deposits'' and ''time deposits'' in Schedule RC–E, Deposit Liabilities. ''Other brokered time deposits'' would consist of all brokered time deposits that are not ''fully insured brokered deposits.''

H. Change in Reporting Frequency for Loans to Small Businesses and Small Farms

Section 122 of the Federal Deposit Insurance Corporation Improvement Act requires the banking agencies to collect from insured institutions annually the information the agencies ''may need to assess the availability of credit to small businesses and small farms.'' To implement these requirements, the banking agencies added Schedule RC–C, Part II—Loans to Small Businesses and Small Farms to the Call Report effective June 30, 1993. This schedule requests information on the number and amount currently outstanding of ''loans to small businesses'' and ''loans to small farms,'' as defined in the Call Report instructions, which all banks must report annually as of June 30.

With the United States now more than a year into a recession, the current administration ''firmly believes that economic recovery will be driven in large part by America's small businesses,'' but ''small business owners are finding it harder to get the credit necessary to stay in business.''[5] Because ''[c]redit is essential to economic recovery,'' Treasury Secretary Geithner stated on March 16, 2009, that ''we need our nation's banks to go the extra mile in keeping credit lines in place on reasonable terms for viable businesses.''[6] Accordingly, Secretary Geithner asked the banking agencies ''to call for quarterly, as opposed to annual reporting of small business loans, so that we can carefully monitor the degree that credit is flowing to our nation's entrepreneurs and small business owners.''[7] In response to Secretary Geithner's request and to improve the agencies' own ability to assess the availability of credit to small businesses and small farms, the agencies propose to change the frequency with which banks must submit Call Report Schedule RC–C, Part II, from annually to quarterly beginning March 31, 2010. The agencies are not proposing to make any revisions to the information that banks are required to report on this schedule.

I. Change in Reporting Frequency for the Number of Certain Deposit Accounts

In Call Report Schedule RC–O—Other Data for Deposit Insurance and FICO Assessments, banks report the number of deposit accounts based on whether the amount of the account is within the deposit insurance limit or is in excess of this limit. Information is reported separately for retirement deposit accounts and all other deposit accounts. At present, for deposit accounts for which the amount of the account exceeds the deposit insurance limit, the number of accounts is reported quarterly (Schedule RC–O, Memorandum items 1.b.(2) and 1.d.(2)). However, for deposit accounts for which the amount of the account is within this limit, the number of accounts is reported annually as of June 30 (Schedule RC–O, Memorandum items 1.a.(2) and 1.c.(2)).

Data on the number of deposit accounts are used to estimate average deposit account balances and changes therein as well as insured and uninsured deposits. These data also assist the FDIC in its planning efforts as it seeks to resolve potential failures of insured institutions. As a consequence, the difference in reporting frequency for deposit accounts with balances within and in excess of the deposit insurance limit hinders the effectiveness of these analyses. Therefore, the agencies are proposing to require all of the existing Call Report items on the number of deposit accounts to be reported quarterly beginning March 31, 2010. The agencies note that savings associations already report the number of all deposit accounts quarterly in the

[4] The FDIC publishes a weekly schedule of national rates and national interest-rate caps by maturity, which can be accessed at *http://www.fdic.gov/regulations/resources/rates/*.

[5] *http://www.financialstability.gov/roadtostability/smallbusinesscommunity.html*.

[6] *http://www.financialstability.gov/latest/tg58-remarks.html*.

[7] Ibid.

Thrift Financial Report (OMB No. 1550–0023). Thus, this proposed change in reporting frequency in the Call Report would conform the reporting requirements in this area for banks and savings associations.

J. Internal Income and Expense Allocations Applicable to Foreign Offices

In Schedule RI–D, Income from Foreign Offices, banks are to report in item 11 their best estimate of all appropriate internal allocations of income and expense applicable to foreign offices, whether or not ''booked'' that way in the bank's formal accounting records. This estimate includes, for example, allocations of income and expense in domestic offices applicable to foreign offices and allocations of income and expense in foreign offices applicable to domestic offices. A review of Schedule RI–D data indicates that few banks report any amount for these internal allocations and the usefulness of the amounts that are reported appears to be limited. Accordingly, the agencies propose to eliminate item 11, ''Internal allocations of income and expense applicable to foreign offices,'' from Schedule RI–D.

III. Other Matters

A. Effect of New Accounting Standards on Schedule RC–S, Servicing, Securitization, and Asset Sale Activities

On June 12, 2009, the Financial Accounting Standards Board (FASB) issued Statements of Financial Accounting Standards Nos. 166 and 167, which revise the existing standards governing the accounting for financial asset transfers and the consolidation of variable interest entities.[8] Statement No. 166 eliminates the concept of a ''qualifying special-purpose entity,'' changes the requirements for derecognizing financial assets, and requires additional disclosures. Statement No. 167 changes how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. This consolidation determination is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance.[9] In general, the revised standards take effect January 1, 2010. The standards are expected to cause a substantial volume of assets in bank-sponsored entities associated with securitization and structured finance activities to be brought onto bank balance sheets.

The agencies currently collect data on banks' securitization and structured finance activities in Schedule RC–S, Servicing, Securitization, and Asset Sale Activities. The agencies will continue to collect Schedule RC–S after the effective date of Statements Nos. 166 and 167 and banks should continue to complete this schedule in accordance with its existing instructions, taking into account the changes in accounting brought about by these two FASB statements. In this regard, items 1 through 8 of Schedule RC–S involve the reporting of information for securitizations that the reporting bank has accounted for as sales. Therefore, after the effective date of Statements Nos. 166 and 167, a bank should report information in items 1 through 8 only for those securitizations for which the transferred assets qualify for sale accounting or are otherwise not carried as assets on the bank's consolidated balance sheet. Thus, if a securitization transaction that qualified for sale accounting prior to the effective date of Statements Nos. 166 and 167 must be brought back onto the reporting bank's consolidated balance sheet upon adoption of these statements, the bank would no longer report information about the securitization in items 1 through 8 of Schedule RC–S.

Items 11 and 12 of Schedule RC–S are applicable to assets that the reporting bank has sold with recourse or other seller-provided credit enhancements, but has not securitized. In Memorandum item 1 of Schedule RC–S, a bank reports certain transfers of small business obligations with recourse that qualify for sale accounting. The scope of these items will continue to be limited to such sold financial assets after the effective date of Statements Nos. 166 and 167. In Memorandum item 2 of Schedule RC–S, a bank currently reports the outstanding principal balance of loans and other financial assets that it services for others when the servicing has been purchased or when the assets have been originated or purchased and subsequently sold with servicing retained. Thus, after the effective date of Statements Nos. 166 and 167, a bank should report retained servicing for those assets or portions of assets reported as sold as well as purchased servicing in Memorandum item 2. Finally, Memorandum item 3 of Schedule RC–S collects data on asset-backed commercial paper conduits regardless of whether the reporting bank must consolidate the conduit in accordance with FASB Interpretation No. 46(R). This will continue to be the case after the effective date of Statement No. 167, which amended this FASB interpretation.

The agencies plan to evaluate the disclosure requirements in Statements Nos. 166 and 167 and the disclosure practices that develop in response to these requirements. This evaluation will assist the agencies in determining the need for revisions to Schedule RC–S that will improve their ability to assess the nature and scope of banks' involvement with securitization and structured finance activities, including those accounted for as sales and those accounted for as secured borrowings. Such revisions, which would not be implemented before March 2011, would be incorporated into a formal proposal that the agencies would publish with a request for comment in accordance with the requirements of the Paperwork Reduction Act of 1995.

In addition, should new Call Report data items pertaining to securitization and structured finance transactions be necessary for regulatory capital calculation purposes after the effective date of Statements No. 166 and 167, a proposal to collect these data items would be incorporated into any notice of proposed rulemaking to amend the agencies regulatory capital standards that the agencies would publish for comment in the **Federal Register**.

B. Trading Assets That Are Past Due or in Nonaccrual Status

In the proposed Call Report revisions for 2009, which were issued for comment on September 23, 2008,[10] the agencies proposed to replace Schedule RC–N, Past Due and Nonaccrual Loans, Leases, and Other Assets, item 9, for ''Debt securities and other assets'' that are past due 30 days or more or in nonaccrual status with two separate items: item 9.a, ''Trading assets,'' and item 9.b, ''All other assets (including available-for-sale and held-to-maturity securities).'' The agencies also proposed to expand the scope of Schedule RC–D, Trading Assets and Liabilities, Memorandum item 3, ''Loans measured at fair value that are past due 90 days

[8] Statement of Financial Accounting Standards No. 166, *Accounting for Transfers of Financial Assets*, amends Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. Statement of Financial Accounting Standards No. 167, *Amendments to FASB Interpretation No. 46(R)*, amends FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities*. In general, under the FASB Accounting Standards Codification™, see Topics 860, Transfers and Servicing, and 810, Consolidation.

[9] FASB News Release, June 12, 2009, *http://www.fasb.org/cs/ContentServer?c=FASBContent_C&pagename=FASB/FASBContent_C/NewsPage&cid=1176156240834&pf=true*.

[10] 73 FR 54807.

or more,'' to include loans held for trading and measured at fair value that are in nonaccrual status. The agencies proposed to collect this information to improve their ability to assess the quality of assets held for trading purposes and generally enhance surveillance and examination planning efforts. One commenter on these proposed reporting changes questioned the meaningfulness of delinquency and nonaccrual data for trading assets because they are accounted for at fair value through earnings. After fully considering this commenter's views, the agencies have decided not to implement the proposed revisions to Schedule RC–N, item 9, and Schedule RC–D, Memorandum item 3. These items will remain in their current form.

C. Unpaid Premiums on Certain Credit Derivatives

The agencies' proposed Call Report revisions for 2009 also included the addition of new Memorandum items 3.a and 3.b to Schedule RC–R, Regulatory Capital, to collect the present value of unpaid premiums on credit derivatives for which the bank is the protection seller that are defined as covered positions under the agencies' market risk capital guidelines. This present value information was to be reported by remaining maturity and with a breakdown between investment grade and subinvestment grade for the rating of the underlying reference asset. One commenter on this proposed credit derivative data requested clarification of the impact of the reporting requirement on a bank's risk-based capital calculations. The agencies have reconsidered this proposed reporting change and have decided not to add these new Memorandum items to Schedule RC–R.

IV. Request for Comment

Public comment is requested on all aspects of this joint notice. Comments are invited specifically on:

(a) Whether the proposed revisions to the Call Report collections of information are necessary for the proper performance of the agencies' functions, including whether the information has practical utility;

(b) The accuracy of the agencies' estimates of the burden of the information collections as they are proposed to be revised, including the validity of the methodology and assumptions used;

(c) Ways to enhance the quality, utility, and clarity of the information to be collected;

(d) Ways to minimize the burden of information collections on respondents, including through the use of automated collection techniques or other forms of information technology; and

(e) Estimates of capital or start up costs and costs of operation, maintenance, and purchase of services to provide information.

Comments submitted in response to this joint notice will be shared among the agencies and will be summarized or included in the agencies' requests for OMB approval. All comments will become a matter of public record.

Dated: August 12, 2009.

Michele Meyer,

Assistant Director, Legislative and Regulatory Activities Division, Office of the Comptroller of the Currency.

Board of Governors of the Federal Reserve System, August 13, 2009.

Jennifer J. Johnson,

Secretary of the Board.

Dated at Washington, DC, this 11th day of August 2009.

Federal Deposit Insurance Corporation.

Robert E. Feldman,

Executive Secretary.

[FR Doc. E9–19911 Filed 8–18–09; 8:45 am]

BILLING CODE 4810–33–P; 6210–01–P; 6714–01–P

DEPARTMENT OF THE TREASURY

Office of Thrift Supervision

Proposed Agency Information Collection Activities; Comment Request—Thrift Financial Report: Schedules SC, RM, CC, DI, and SB

AGENCY: Office of Thrift Supervision (OTS), Treasury.

ACTION: Notice and request for comment.

SUMMARY: The Department of the Treasury, as part of its continuing effort to reduce paperwork and respondent burden, invites the general public and other federal agencies to comment on proposed and continuing information collections, as required by the Paperwork Reduction Act of 1995, 44 U.S.C. 3507. Today, the Office of Thrift Supervision within the Department of the Treasury solicits comments on proposed changes to the Thrift Financial Report (TFR), Schedule SC—Consolidated Statement of Condition, Schedule CC—Consolidated Commitments and Contingencies, Schedule DI—Consolidated Deposit Information, Schedule SB—Consolidated Small Business Loans, and on a proposed new schedule, Schedule RM—Annual Supplemental Consolidated Data on Reverse Mortgages. The changes are proposed to become effective in March 2010 except for the proposed new schedule RM which would become effective in December 2010.

At the end of the comment period, OTS will analyze the comments and recommendations received to determine if it should modify the proposed revisions prior to giving its final approval. OTS will then submit the revisions to the Office of Management and Budget (OMB) for review and approval.

DATES: Submit written comments on or before October 19, 2009.

ADDRESSES: Send comments to Information Collection Comments, Chief Counsel's Office, Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552; send facsimile transmissions to FAX number (202) 906–6518; send e-mails to *infocollection.comments@ots.treas.gov;* or hand deliver comments to the Guard's Desk, east lobby entrance, 1700 G Street, NW., on business days between 9 a.m. and 4 p.m. All comments should refer to ''TFR Revisions—2010, OMB No. 1550–0023.'' OTS will post comments and the related index on the OTS Internet Site at *http://www.ots.treas.gov.* In addition, interested persons may inspect comments at the Public Reading Room, 1700 G Street, NW., by appointment. To make an appointment, call (202) 906–5922, send an e-mail to *publicinfo@ots.treas.gov,* or send a facsimile transmission to (202) 906–7755.

FOR FURTHER INFORMATION CONTACT: You can access sample copies of the proposed 2010 TFR forms on OTS's Web site at *http://www.ots.treas.gov* or you may request them by electronic mail from *tfr.instructions@ots.treas.gov.* You can request additional information about this proposed information collection from James Caton, Director, Financial Monitoring and Analysis Division, (202) 906–5680, Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552.

SUPPLEMENTARY INFORMATION:

Title: Thrift Financial Report.

OMB Number: 1550–0023.

Form Number: OTS 1313.

Abstract: OTS is proposing to revise and extend for three years the TFR, which is currently an approved collection of information.

All OTS-regulated savings associations must comply with the information collections described in this notice. OTS collects this information each calendar quarter or less frequently if so stated. OTS uses this information to monitor the condition, performance, and risk profile of individual

DataLine
A look at current financial reporting issues

PricewaterhouseCoopers

2009–23
April 30, 2009

FASB's New Model for the Impairment of Debt Securities

Questions and Interpretive Responses

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Overview

New accounting guidance revises the recognition and reporting requirements for other-than-temporary impairments of debt securities.

The Financial Accounting Standards Board (FASB) issued FASB Staff Position FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments* (the FSP or FSP 115-2) to address concerns about evaluating and recognizing other-than-temporary impairments of investments in debt securities. For an overview of the provisions of FSP 115-2, refer to DataLine 2009-20, *FASB's New Guidance on Other-Than-Temporary Impairments*.

FSP 115-2 establishes a new method of recognizing and reporting other-than-temporary impairments of debt securities. The FSP also contains additional disclosure requirements. It is effective for interim and annual periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009 if certain conditions are met.

The issuance of FSP 115-2 has generated a number of implementation questions. The Questions and Interpretive Responses in this DataLine may be helpful as companies evaluate the requirements and implications of the FSP.

In this DataLine, the abbreviation "OTTI" is used to mean "other-than-temporarily impaired" and "other-than-temporary impairment." Reference to a debt security means any security representing a creditor relationship with an enterprise as defined by FAS 115, *Accounting for Certain Investments in Debt and Equity Securities* (FAS 115).

In addition to the Questions and Interpretive Responses below, the following guidance may be helpful when assessing investments in debt securities for potential OTTI.

- FAS 115, *Accounting for Certain Investments in Debt and Equity Securities*
- FSP 115-1/124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*
- FSP 115-2/124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*
- EITF 99-20, *Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets*
- FSP EITF 99-20-1, *Amendments to the Impairment Guidance of EITF Issue 99-20*

- SOP 03-3, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*
- PwC DataLine 2009-20, *FASB's New Guidance on Other-Than-Temporary Impairments*
- PwC DataLine 2008-22, *Accounting Considerations Related to Other-Than-Temporary Impairment of Certain Investments in Debt and Equity Securities*
- PwC Guide, *Accounting for Transfers and Servicing of Financial Assets*

Questions

Clients of PricewaterhouseCoopers that have questions about this DataLine should contact their engagement partner. Engagement teams that have questions about the DataLine should contact a member of the Financial Services / Financial Instruments team in the National Professional Services Group (973-236-7803).

Questions and Interpretive Responses

Transition effect

Question 1

Should the transition adjustment for an individual debt security be based on cash flows expected to be collected as of the transition date or as of the date the last impairment was taken?

Interpretive Response

According to the FSP, the transition adjustment should be based on cash flow expected to be collected as of the beginning of the interim period in which the FSP is adopted (the transition date). This is unlike other cumulative effect calculations that evaluate the impact on retained earnings as if the new guidance were applied historically. As a result, if an entity recorded a credit-related OTTI in the past, and there has been an increase in expected cash flows to be collected since that date, the transition adjustment would be based on the more favorable cash flow expectations.

Question 2

Is the cumulative effect of adopting the FSP just a reclassification of the noncredit portion of previously recognized OTTI losses, net of related taxes, from retained earnings to accumulated other comprehensive income (AOCI)?

Interpretive Response

Not necessarily. In accordance with FASB Statement No. 154, *Accounting Changes and Error Corrections*, the cumulative effect of a retroactive application of a change in accounting principle should include the direct effects, as defined, of that change, including any related income tax effects. Adjustments for items such as the application of EITF Topic D-41, *Adjustments in Assets and Liabilities for Holding Gains and Losses as Related to the Implementation of FASB Statement No.115* (discussed further in the Interpretive Response to Question 4), and for the reassessment of a deferred tax valuation allowance (discussed in the Interpretive Response to Question 3) would be considered direct effects of the retroactive application of the FSP under FAS 154. We do not believe that the language in paragraph 45 of the FSP which notes that the cumulative effect of initially applying this FSP should be recorded as an adjustment to the opening balance of retained earnings with a "corresponding adjustment" to accumulated other comprehensive income is meant to limit the transition adjustment to the noncredit portion of previously recognized OTTI losses (net of related income tax effects). In accordance with the FSP, the cumulative effect adjustment should not impact earnings.

Question 3

Will adoption of the FSP always result in a reclassification within shareholders' equity balances with no net impact on overall shareholders' equity?

Interpretive Response

Not necessarily. For example, adoption of the FSP may have an impact on an entity's deferred tax asset (DTA) valuation allowance, which would result in a change to overall

shareholders' equity[1]. Assume an entity has adopted an accounting policy to separately evaluate the recoverability of DTAs related to unrealized losses on available-for-sale (AFS) debt securities under the Alternative View discussed in the Interpretive Response to Question 15 of DataLine 2008-22, *Accounting Considerations Related to Other-Than-Temporary Impairment of Certain Investments in Debt and Equity Securities*. Under the Alternative View, realizability of DTAs relating to unrealized losses on AFS debt securities recorded in accumulated other comprehensive income (AOCI) is assessed differently than for DTAs related to OTTI losses recognized in earnings. If a valuation allowance had been provided for DTAs related to OTTI losses previously recognized in the income statement, the adoption of the FSP may enable an entity to reverse the portion of the valuation allowance related to the OTTI losses being reclassified to AOCI, assuming the entity can assert the intent and ability to hold to recovery (maturity, if necessary). In this circumstance, the release of the valuation allowance should not be included in income from continuing operations; rather, it should be recorded as part of the cumulative effect of adopting the FSP.

Question 4

Will adoption of the FSP result in adjustments to assets and liabilities in accordance with EITF Topic No. D-41, *Adjustments in Assets and Liabilities for Holding Gains and Losses as Related to the Implementation of FASB Statement No. 115*?

Interpretive Response

No. EITF Topic D-41 requires that certain assets and liabilities, such as noncontrolling interests, certain life insurance policyholder liabilities, deferred acquisition costs, and the present value of future profits, be adjusted to the extent that unrealized gains or losses from debt securities classified as AFS would result in adjustments of those assets and liabilities if those gains or losses had actually been realized (sometimes referred to as "shadow" adjustments). When such adjustment is recorded, a corresponding entry is made to AOCI. Adoption of the FSP will result in recognition in AOCI of certain amounts previously recognized in earnings, and may result in corresponding shadow adjustments for the items discussed in D-41. However, as the shadow adjustment is meant to adjust these items as if the unrealized gains and losses have been realized, adoption of the FSP should not materially impact the amount at which the assets and liabilities discussed above are recorded.

Question 5

Will the FSP's transition provisions impact the comparability of reported earnings between periods?

Interpretive Response

Yes. The cumulative effect of adopting the FSP is recorded within shareholders' equity as of the adoption date, essentially restating opening retained earnings. Because prior income statements are not restated, the FSP may impact the comparability between current and prior period financial statements. The FSP requires reclassification of amounts previously recognized in income (i.e., noncredit-related OTTI) from retained earnings to AOCI. A subsequent sale (or certain subsequent OTTI) will result in income statement recognition of these noncredit-related losses in the period of sale. For example, an entity may recognize an

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[1] The FASB has added a project to its agenda to consider the issues related to recoverability of DTAs on available-for-sale debt securities expected to be held to recovery. The outcome of that project could impact the accounting in this area.

OTTI in the first quarter of 2009. Upon adoption of the FSP in the second quarter of 2009, the cumulative effect entry would effectively reclassify the noncredit portion of the previously recognized loss from retained earnings to AOCI. When the debt security is sold, the loss in AOCI will be recognized, which results in that charge being recorded in income twice. In addition, the FSP may have a significant impact on reported investment yields on OTTI debt securities (generally reducing these yields). Because prior financial statements are not restated, disclosure of these comparability considerations should be considered.

Evaluation of OTTI for a debt security

Question 6

What indicators are relevant in determining whether an entity has an "intent to sell" an AFS or held-to-maturity (HTM) debt security for purposes of applying the FSP?

Interpretive Response

If an entity has the "intent to sell" an AFS or HTM debt security that is impaired, the entity is required to recognize OTTI on that debt security. The FSP indicates that an intent to sell exists when an entity has decided to sell a debt security. The FSP does not provide guidance for determining when such a decision is deemed to have been made. Judgment will be required and consideration should be given to all available evidence. For example, a decision to sell that is contingent upon the occurrence of a future event may not be evidence of a present intent to sell that would result in an OTTI. The following indicators, though not all-inclusive, may assist in making determinations about the point at which an entity has the intent to sell a security:

- An entity (or its agent) has decided to sell a security with approval by an authorized representative of the entity, subject only to terms that are usual and customary for sales of such securities

- The security is being actively marketed for sale at a price that is reasonable in relation to its current fair value

In general, we would expect a relatively short period of time to elapse between an entity's assertion about an intent to sell and an actual sale. An entity should update its financial reporting systems and related internal controls to determine in a timely and consistent manner when an intent to sell a security exists. This determination should be made each financial reporting period and on a security-by-security basis.

Question 7

When performing its OTTI analysis, what information should an entity consider in determining whether it is more likely than not that it will be required to sell the debt security before recovery of its amortized cost basis?

Interpretive Response

The criteria that an OTTI must be recognized if it is "more likely than not" (MLTN) that the entity will be required to sell an impaired debt security involves an assessment of two factors:

- the conditions or events that might require the entity to sell a security, and

- the likelihood of such conditions or events occurring.

Implicit in these criteria is the notion that not all potential sales of impaired debt securities that are considered MLTN will result in OTTI. In general, only sales that involve a level of legal,

regulatory or operational compulsion should be considered "required" sales, consistent with the FSP's guidance that an entity should consider "its cash or working capital requirement or contractual or regulatory obligations that indicate that the security will be required to be sold before a forecasted recovery occurs." Once the conditions or events that may require the sale of an impaired debt security are identified, an entity should determine whether it is considered MLTN that these conditions or events will occur. If it is considered MLTN, judgment may be needed to determine which debt securities would be sold if the events or conditions actually do occur, and an OTTI must be recognized on these debt securities. We believe that the potential sale of an impaired debt security, even if considered MLTN, would not result in an OTTI if that sale is not a "required" sale as contemplated by the FSP. Other criteria must still be considered to determine whether OTTI should be recognized, including whether a decision to sell has been made at the balance sheet date (see the Interpretive Response to Question 6).

Question 8

If an OTTI is recognized because it is more likely than not that the entity will be required to sell the debt security before recovery of its amortized cost basis, may a portion of the OTTI be recognized in OCI?

Interpretive Response

In circumstances where OTTI is recognized because it is MLTN that the entity will be required to sell the debt security, the noncredit portion of the OTTI may be recognized in OCI if it is not MLTN that the entity will be required to sell the debt security before recovery of its amortized cost basis, less any current period credit loss. This involves determining the timing of a required sale, the adjusted amortized cost at that date, and projecting the fair value/sales price at that date. Essentially, if the noncredit portion of the OTTI and all expected cash flows would be recovered by the date of the MLTN required sale, only the credit portion of OTTI would be recognized in income. Because of the subjectivity involved in estimating the date of a required sale and of projecting recovery of noncredit elements (which are based on changes in various market factors such as risk-free interest rates, liquidity premiums, etc.) it may be difficult for entities to provide persuasive evidence to support recognizing only the credit portion in OTTI. As a result, we generally expect that entities will recognize OTTI in income equal to the difference between the debt security's fair value and its amortized cost.

Question 9

Does the FSP change the threshold for recognizing an impairment loss for investments in debt securities when there is a decrease in expected future cash flows?

Interpretive Response

Yes. Prior to the FSP, FAS 115 required that an OTTI be considered to have occurred if it was probable that the investor would be unable to collect all amounts due according to the contractual terms of a debt security not impaired at acquisition. The FSP eliminates this threshold and requires that a credit loss be recognized when the present value of the cash flows expected to be collected from the debt security are less than the security's amortized cost. The term "cash flows expected to be collected" is defined as "the cash flows that the entity is likely to collect after a careful assessment of all available information." As a result, a decrease in cash flows that the entity is likely to collect will now result in OTTI (if in an unrealized loss position), even if non-collection of cash flows is not considered probable. The Board described their rationale for this change as an attempt to clarify that an entity should not wait until an event of default has occurred to recognize an impairment loss.

Question 10

When determining whether a credit loss exists for a debt security not accounted for under EITF 99-20, *Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets* (EITF 99-20), must an entity use the methodology described in FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan* (FAS 114), to determine its best estimate of the present value of cash flows expected to be collected from the debt security?

Interpretive Response

No. The methodology in FAS 114 is one way of estimating the present value of cash flows expected to be collected from the debt security. Other methods may be appropriate. Any method for measuring a credit loss should be consistent with the Board's intent that "cash flows expected to be collected should represent the cash flows that an entity is likely to collect after a careful assessment of all available information." Methodologies that implicitly or explicitly recognize changes in cash flows that are not due to credit would generally not be consistent with this standard. For debt securities that are within the scope of EITF 99-20, the present value of cash flows expected to be collected should be determined in accordance with that standard, resulting in the cash flows estimated at the current reporting date being discounted at the current yield used to accrete the debt security.

Question 11

Is it appropriate for an entity to determine the cash flows expected to be collected from the debt security using either a probability-weighted measure or a single best estimate?

Interpretive Response

Yes. We believe that the decision to use either a single best estimate or a probability-weighted measure is a policy election. The term "cash flows expected to be collected" is not necessarily an "expected cash flow measure" as defined in FASB Concept Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements* (CON 7) or as described in Appendix B of FASB Statement No. 157, *Fair Value Measurements* (FAS 157). CON 7 defines expected cash flow as the "sum of probability weighted amounts in a range of possible estimated amounts; the estimated mean or average." Consistent with the Board's objective of aligning the requirements for recognition and measurement of impairment losses for investments in debt securities with those for loans, we believe that the term "present value of cash flows expected to be collected" used in the FSP may be viewed similar to the "present value of expected future cash flows" described in FAS 114. Although some believe FAS 114 implies that a single best estimate should be used, paragraph 59 of CON 7 notes that cash flow under FAS 114 can be determined using an expected cash flow approach. Thus, while a single "best estimate" measure may be used, an approach that determines a probability-weighted measure would also be appropriate for FAS 114 purposes and, by analogy, for purposes of applying the FSP. Management should document and disclose its policy decision in this regard. In practice, a best estimate approach is typically used for purposes of applying FAS 114 to investments in impaired loans.

Question 12

For debt securities within the scope of EITF 99-20 should *cash flows expected to be collected* be based on a single best estimate or a probability-weighted measure of expected cash flows?

Interpretive Response

The FSP amends EITF 99-20 by replacing the term *estimated cash flows* with *cash flows expected to be collected.* As a result, the cash flows used in the EITF 99-20 model now

conform to the cash flows used in the SOP 03-3, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer* (SOP 03-3), model and to the cash flows used in the FSP's impairment model. Refer to the Interpretive Response to Question 11 regarding our view that management may make a policy election to apply either a single best estimate or a probability-weighted measure when estimating cash flows. Regardless of which measure is used, both the amount and timing of future cash flows based on current information and events should be considered and the policy should be consistently applied.

Question 13

If a probability-weighted measure of cash flows is used to determine the cash flows expected to be collected, can the present value be determined using the effective interest rate implicit in the debt security at the date of acquisition?

Interpretive Response

No. The effective interest rate implicit in the debt security at the date of acquisition represents the contractual interest rate adjusted for any costs, premium or discount that exist at the acquisition date, and is essentially comprised of a risk-free rate adjusted for a credit spread and liquidity premium. This rate equates the cost of the debt security to the debt security's expected cash flows over its remaining term. By its nature, this rate reflects expectations about potential future defaults. It would, therefore, not be appropriate to use it to discount a probability-weighted measure of cash flows because the cash flow projections already reflect assumptions about future defaults.

Question 14

Must a detailed cash flow analysis be performed on every impaired debt security to determine whether a credit loss exists?

Interpretive Response

Not necessarily. Management is required to determine whether the present value of cash flows expected to be collected is less than the amortized cost of an impaired debt security (i.e., whether a credit loss exists). Under certain circumstances, a qualitative determination of whether a credit loss exists may be made based on an evaluation of all available information, including the conditions outlined in paragraph 25 of the FSP (as described in DataLine 2009-20). If, based on this qualitative assessment, a credit loss is determined to exist, such loss should be measured in accordance with the FSP's guidance (i.e., the FAS 114 model or another acceptable approach).

Question 15

May an entity recognize a credit loss in excess of the unrealized loss on an impaired debt security?

Interpretive Response

Yes, but unlikely. If the OTTI is being recognized because (1) the entity intends to sell the debt security, or (2) because it is MLTN that the entity will be required to sell the debt security before recovery and the conditions in Question 8 have not been met, the amount of OTTI recognized in the income statement will equal the unrealized loss on the impaired debt security. However, in all other cases, it is possible for a debt security's amortized cost to be written down below fair value. In these other instances, a portion of the credit loss recognized in the income statement is offset by an unrealized gain in comprehensive income such that the carrying value of the debt security will always be its fair value. This could occur even if a market participant's view of future expected cash flows is consistent with management's expectations because other factors affect fair value and changes in fair value

due to those factors may offset the decline in fair value due to a decrease in expected future cash flows. For example, a decrease in risk-free interest rates would result in an offsetting increase to fair value even when future estimated cash flows have declined. This decrease in risk-free interest rates would not be reflected in the determination of the credit loss in accordance with a FAS 114 methodology (which would be computed using the effective interest rate implicit in the debt security at the date of acquisition). Although recognition of a credit loss in excess of the pre-OTTI unrealized loss is possible, we believe that conditions in current debt securities markets, including historically high liquidity premiums and credit spreads, make such a result unlikely upon adoption of the FSP.

Question 16

Paragraphs 24 of the FSP and revised paragraph 14E of FSP 115-1 state that "a decrease in cash flows expected to be collected on an asset-backed security that results from an increase in prepayments on the underlying assets shall be considered in the estimate of the present value of cash flows expected to be collected." How do contractual prepayments affect the determination of credit losses?

Interpretive Response

We understand that the FSP's guidance about the treatment of prepayments was intended to provide clarification for determining the "cash flows expected to be collected" on interest-only securities and other similar securities that can be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of the investment. These securities are generally accounted for in accordance with EITF 99-20 if they are not considered derivatives within the scope of FAS 133, *Accounting for Derivative Instruments and Hedging Activities*. EITF 99-20 requires that an entity estimate cash flows expected to be collected based on all available information, including prepayments. We do not believe that the FSP changes the accounting for prepayments under existing accounting models, including FAS 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*, EITF 99-20 or SOP 03-3, or that decreases in expected cash flows as a result of contractual prepayments that were typically considered yield adjustments under those models should now be considered potential credit losses.

Question 17

Must an entity use the same inputs and assumptions regarding estimated cash flows to measure fair value under FAS 157 and credit losses under the FSP?

Interpretive Response

No. Neither the FSP nor FAS 115 require that an entity place exclusive reliance on market participant assumptions of future cash flows. However, management is required to consider all relevant facts and circumstances when evaluating OTTI, and the market's view of the likelihood and amount of future cash flows which is embedded in a current fair value measure under FAS 157 is one important source of evidence that should be considered. The implied yield approach discussed in DataLine 2008-22 may be helpful in estimating expected future cash flows. As declines in fair value increase in severity and duration, and in the absence of any explicit evidence to the contrary, the level of analysis and objective evidence needed to support a difference between management's estimate of cash flows expected to be collected and the cash flows implied in a current fair value measure also increases.

Question 18

May an entity use the fair value of an impaired debt security purely as a "practical expedient" to determine the credit loss under the FSP?

Interpretive Response

No. The practical expedient in FAS 114 allows a creditor to measure impairment of a loan based on the loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. Because the FSP refers to the methodology described in FAS 114 as one way of estimating the amount of credit loss on a debt security, some believe that the FSP also permits a similar practical expedient to be used. However, the FSP does not incorporate the entire FAS 114 impairment model, including the condition that a loan is not impaired unless it is considered probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement.

We do not believe it is appropriate to assume that the FASB intended for the practical expedient granted in FAS 114 to be applied when determining a credit loss under the FSP. More importantly, one of the main objectives of the FSP is to provide financial statement users with sufficient information about the amount of cash an entity expects to collect by holding a debt security. The use of a fair value, which includes assumptions regarding interest rate, liquidity and other market risks in addition to perceived credit risk would not isolate the credit-related decrease in estimated cash flows. As a result, use of fair value as a practical expedient for determining the credit loss on a debt security would, in most cases, be inconsistent with the FSP's underlying objective. However, in certain limited circumstances, the fair value of a debt security may represent an entity's best estimate of the present value of cash flows expected to be collected within acceptable materiality limits.

While fair value cannot be used as a practical expedient to determine a credit loss under the FSP, this does not affect the requirement to measure OTTI as the difference between a debt security's fair value and its amortized cost if the entity intends to sell the debt security or more likely than not will be required to sell the debt security before recovery of its amortized cost basis (less any current period credit loss).

Accounting for a debt security after an OTTI

Question 19

In periods subsequent to a recognized credit loss, how should an entity account for the debt security and the estimated cash flows it expects to collect?

Interpretive Response

For debt securities that are not accounted for in accordance with EITF 99-20, a significant increase in cash flows expected to be collected or actual cash flows significantly greater than cash flows previously expected, should be treated as prospective yield adjustments in accordance with SOP 03-3. For these securities, subsequent declines in estimated cash flows generally will not result in a yield adjustment, but may result in additional OTTI (if the debt security is impaired). This essentially conforms the accounting for securities that are not within the scope of EITF 99-20 with the accounting in SOP 03-3 subsequent to an OTTI.

If the debt security is within the scope of EITF 99-20, changes in cash flows expected to be collected should be accounted for in accordance with that guidance. The FSP does not address when a holder of a debt security would place a debt security on nonaccrual status or how to subsequently report income on a debt security that is placed on nonaccrual status.

Question 20

If an OTTI is recognized because the entity intends to sell the debt security or it is more likely than not it will be required to sell the debt security before recovery of its amortized cost, must a credit loss be computed for post-OTTI accounting purposes?

Interpretive Response

An OTTI is not limited to credit loss when an entity intends to sell an impaired debt security or when it is more likely than not the entity will be required to sell the impaired debt security before recovery of its amortized cost basis, except as discussed in the Interpretive Response to Question 8. Other than that circumstance, the amount of OTTI is equal to the difference between the debt security's fair value and its amortized cost, and the credit loss is not required to be separately presented in the financial statements. Regardless, however, of the reason an OTTI is recognized, the FSP requires that the difference between the new amortized cost basis and the cash flows expected to be collected be accreted as interest income in accordance with existing guidance. As a result, the analysis of future expected cash flows is technically required for all securities for which an OTTI is recognized. However, given that a sale is generally expected to occur within a reasonably short time period after a decision to sell has been made, subsequent accretion may not be material, depending on an entity's particular facts and circumstances. As noted in the Interpretive Response to Question 19, the FSP does not address when a holder of a debt security would place a debt security on nonaccrual status or how to subsequently report income on a debt security that is placed on nonaccrual status.

Tainting of an available for sale debt security portfolio

Question 21

Does subsequent sale at a loss after an entity's assertion that it does not intend to sell a debt security or that it is MLTN that it will not be required to sell a security before recovery, call into question management's assertion on other securities for which noncredit-related impairments have not been recognized?

Interpretive Response

Perhaps, depending on the specific reasons for the subsequent sale at a loss. Prior to the FSP, a pattern of sales of AFS debt securities at a loss for which the entity had previously asserted the ability and intent to hold until recovery could "taint" or call into question the entity's assertion about its ability and intent to hold any remaining impaired debt securities in the AFS portfolio until recovery. Although the "intent to sell" and "more likely than not will be required to sell" criteria under the FSP constitute different thresholds for recognizing OTTI than the previous "intent and ability to hold” thresholds, subsequent sales at a loss may still call into question the validity of an entity's assertions under the FSP. In general, however, although an entity must still assess their specific facts and circumstances, we expect fewer sales will raise questions about an entity's prior assertions. This is primarily due to the fact that an entity's assertion regarding its intent to sell is made at a point in time and that intent may change over time. The historical assertion regarding management's intent to hold to recovery contemplated a longer term outlook that generally was not expected to change except as a result of certain unique or unforeseen circumstances. In addition, even though it may not be considered MLTN that the sale of an impaired debt security will be required, such a sale may still be possible. A sale at a loss in these circumstances would not necessarily call into question the entity's prior assertion, unless it was determined that the entity incorrectly concluded that such a sale was not MLTN. Entities should document why recent sales do not impact their OTTI assertions.

Perpetual preferred stock

Question 22

How does the FSP impact the impairment guidance for equity securities with debt-like features (e.g., perpetual preferred stock)?

Interpretive Response

The FSP does not address the application of existing OTTI requirements to securities that are structured in equity form but possess significant 'debt-like' characteristics. However, consistent with the guidance previously issued in the SEC staff letter dated October 19, 2008 (refer to Interpretive Response to Question 14, in DataLine 2008-22), an entity may evaluate OTTI for equity instruments with debt-like features in accordance with the FSP unless there is evidence of deterioration in credit quality of the issuer (e.g., a decline in the cash flows from the investment or a downgrade of the rating of the perpetual preferred stock below investment grade). We believe that a decrease in expected cash flows below amortized cost (i.e., a credit loss under the FSP) is also "evidence of a deterioration in credit quality of the issuer." When performing an OTTI assessment for these types of securities, entities should first determine whether there is evidence of a deterioration in credit quality of the issuer. If evidence of a deterioration exists, the perpetual preferred stock should be evaluated for OTTI as an equity security and not as a debt security. As a result, an OTTI loss on a perpetual preferred security with debt-like features would not be separated into its credit and noncredit portions as prescribed by the FSP.

Investments in debt securities managed by a third party

Question 23

How does the elimination of the requirement to assert an ability to hold a debt security for a period of time sufficient to allow for an anticipated recovery in its fair value to its amortized cost affect the OTTI assessment relating to investments in debt securities managed by third-party investment managers (e.g., nuclear decommissioning trust funds)?

Interpretive Response

While not specifically addressed by the FSP, we believe that, in certain circumstances, debt securities managed by third-party investment managers which were previously considered OTTI solely because of the entity's lack of ability to control the manager's sale of the debt security may no longer require an OTTI. This view is premised on the concept that, because of the change in the indicators of OTTI, application of the FSP should result in consistent treatment for managed assets, whether management is performed by a third-party investment manager or an internal function. A third-party investment manager typically acts as an agent for the entity and performs a function that the entity itself could legally perform. Although the contractual arrangement between the entity and the asset manager may provide the asset manager with discretion regarding which assets to buy and sell, this discretion is typically defined within the parameters of a given investment strategy that is approved by the entity. Effectively, the operation of the third-party asset manager is not dissimilar to the operation of the entity's internal asset managers who must comply with internal investment guidelines.

In the situation described above, management must still be able to assert that it does not intend to sell the debt security and that it is not MLTN that the entity will be required to sell the debt security. We believe management may be able to make such an assertion by obtaining evidence regarding the intent of the third party investment manager. And, although management may not be able to prevent a third-party investment manager from selling an impaired debt security, were such a sale to occur, it would not necessarily be the same as a "required sale" as contemplated by the FSP. As discussed in the Interpretive Response to

Question 7, only sales that involve a level of legal, regulatory or operational compulsion should be considered "required" sales. If the assets managed by the third-party investment manager are not needed to fund current operating needs or to satisfy other legal or regulatory requirements, the fact that the entity may not be able to prevent the manager from making sales would not prevent management from asserting that it is not MLTN that the entity would be required to sell these securities. In addition, the fact that a third-party investment manager may sell a debt security does not necessarily mean that the likelihood of that sale is MLTN.

It would also be acceptable to consider all sales by the third-party investment manager to be "required" due to the fact that, by contract, the entity must sell the debt security once a manager has decided to do so. This view assumes that an entity's lack of ability to prevent the asset manager from selling an impaired debt security also prevents the entity from asserting that it is MLTN that these sales will not occur. Therefore, under this view, the lack of ability contemplated under pre-FSP OTTI guidance would continue to result in OTTI for impaired securities managed by a third-party investment manager.

Until additional clarification is provided by the SEC or the FASB on these types of relationships, we believe that either view expressed above is acceptable. However, since the FSP applies only to investments in debt securities, and since the OTTI guidance for investments in equity securities has not changed, entities should continue to apply the historical OTTI model for investments in equity securities managed by third-party investment managers. To the extent that a third-party investment manager manages both debt and equity securities, this may result in the application of different OTTI models for different securities managed by the same investment manager.

Disclosures

Question 24

How does the FSP affect the presentation and disclosure of amounts within other comprehensive income (OCI) and accumulated other comprehensive income (AOCI) for impaired debt securities?

Interpretive Response

The FSP amends FAS 130*, Reporting Comprehensive Income*, to require presentation of unrealized gains and losses on AFS securities for which an OTTI has been recognized separately from unrealized gains and losses on AFS securities for which an OTTI has not been recognized. The unrealized gains and losses on AFS debt securities for which an OTTI has been recognized is determined by comparing the current amortized cost basis with the current fair value. That is, the noncredit component of OTTI as well as all subsequent changes in fair value relating to a previously impaired debt security should be reported in a single line item where the components of OCI and AOCI are disclosed. The FSP also requires disclosure of the unamortized unrealized loss relating to impaired HTM securities within OCI and AOCI.

Additionally, as part of the revised disclosures required by paragraph 19 of FAS 115, an entity must separately disclose the total OTTI recognized in AOCI by major security type.

The following example illustrates these requirements (all amounts presented before tax impacts for simplicity).

Facts:

2009

- Debt security with a $100 amortized cost basis and fair value of $60
- Impairment is determined to be other than temporary
- OTTI is comprised of a $10 credit-related component recognized in earnings and a $30 noncredit component recognized in OCI

1st Quarter 2010

- Fair value of the debt security has increased to $64
- No further OTTI

Conclusions:

A debit (charge) of $30 would be included in the OTTI-related component of OCI for the period ending March 31, 2009. For the year ending December 31, 2010, a $4 credit would be included in the OTTI-related component of OCI. The disclosure of the components of AOCI as required by paragraph 26 of FAS 130 would show a $30 debit balance in the OTTI-related component of AOCI at December 31, 2009. At March 31, 2010, the AOCI disclosure would show a $26 debit balance in the OTTI-related component of AOCI for the debt security.

Separately, in accordance with the disclosure required by paragraph 19 of FAS 115, the total OTTI impairment recognized in AOCI would be $30 at December 31, 2009 and March 31, 2010.

Question 25

How would a subsequent increase in the fair value of a previously other-than-temporarily impaired AFS debt security, accompanied by an increase in expected credit losses for that debt security, be presented in equity and OCI in the current period?

Interpretive Response

While an additional OTTI has not occurred in the current period because the debt security's fair value is greater than the prior period's fair value, a charge to income would be recognized for the increased credit loss, offset by a corresponding reduction in the previous noncredit OTTI recognized in OCI. That is, while, on a comprehensive income basis, there is no additional impairment, the nature of the impairment has changed between the credit loss portion and the noncredit loss portion of the total other than temporary impairment.

Consider the following example (all amounts presented before tax impacts for simplicity).

Facts:

2009

- Debt security with a $100 amortized cost basis and fair value of $60
- Impairment is determined to be other than temporary
- OTTI is comprised of a $10 credit-related component recorded in earnings and a $30 noncredit component recognized in OCI
- The new amortized cost basis of the debt security, after the credit loss, is $90.

1st Quarter 2010

- The debt security has increased in fair value to $64
- The credit loss has increased by $5, resulting in a new amortized cost basis of $85.

Conclusions:

In accordance with paragraph 36 of FSP 115-2, the income statement presentation for the quarter ended March 31, 2010 would be as follows:

Total other than temporary impairment losses	$0
Portion of loss recognized in OCI	($5) credit
Net impairment loss recognized in earnings	$5 debit

Comprehensive income would consist of the following activity for the period ending March 31, 2010, comprised of a $5 reclassification to earnings and $4 increase in fair value of the debt security:

Change in OTTI-related component of unrealized gain/loss	$9 credit

AOCI balances would consist of the following component at March 31, 2010:

OTTI-related component of unrealized gain/loss	($21)* debit

* Calculated as 2009 $30 noncredit component of OTTI less $5 reclass from OCI to earnings in 2010 and less $4 unrealized gain recognized in 2010.

Question 26

What is the objective of the tabular rollforward in each interim and annual reporting period of the amount related to credit losses recognized in earnings that is required by paragraph 43 of the FSP?

Interpretive Response

We understand that this disclosure was suggested by investors who wanted additional information regarding management's expectations of credit losses, how those expectations develop over time, and how actual experience compares to prior expectations. The item being rolled forward is not an actual financial statement balance. Rather, it represents a

memo account relating to cumulative credit loss activity recorded in income on impaired debt securities for which a portion of the impairment was recorded in OCI. One of the focus areas for investors is likely to be the disclosure of additional credit losses recognized on securities for which a credit loss had previously been recognized, as this may provide some indication of management's ability to accurately estimate credit losses on a timely basis.

Question 27

The rollforward requires disclosure of reductions for increases in cash flows expected to be collected over the remaining life of the debt security. Should the amount included in the rollforward reflect the entire expected increase in future cash flows or the amount recognized in the income statement in the period that relates to the expected increase in cash flows?

Interpretive Response

Subsequent increases in expected cash flows on a previously OTTI debt security are recognized as a yield adjustment on a prospective basis. We understand that the intent of the FASB was to require disclosure in the rollforward of the amount recognized in income in the current period that relates to the expected increase in cash flows. However, the components of the rollforward are identified as a "minimum" disclosure, suggesting that supplemental disclosure of the entire increase in expected cash flows would not be precluded.

Question 28

The rollforward does not require disclosure of the accretion of discounted expected cash flows recognized in the period. May this amount be included in the rollforward?

Interpretive Response

Yes. Consistent with the Interpretive Response to Question 27, the components of the rollforward are identified as a "minimum" disclosure, suggesting that additional disclosure would not be precluded.

Question 29

How should the duration of the unrealized loss be determined for disclosure purposes for securities for which a portion of an OTTI has been recognized in earnings? Should the duration be calculated from the original impairment date or from the date when OTTI is recognized in earnings?

Interpretive Response

FSP FAS 115-1 requires disclosure of the duration of the unrealized loss on AFS debt and equity securities and states that the reference point for determining how long an investment has been in a continuous loss position is the balance sheet date of the reporting period in which the impairment (i.e., amortized cost exceeding fair value) first exists. Prior to the FSP, recognition of OTTI would eliminate the entire unrealized loss (i.e., by recognizing it in the income statement) and effectively "restart the clock" for purposes of determining the duration of any subsequent impairment. When a portion of an OTTI is not recognized in earnings in accordance with the FSP, the duration of that unrealized loss continues after the OTTI. For disclosure purposes, the duration of the remaining impairment should be based on the end date of the reporting period during which the debt security first had a fair value less than amortized cost. This will likely result in comparatively more disclosures of securities in an unrealized loss position for 12 months or greater than were made prior to the FSP. Additional disclosures may be useful in explaining the increased amount of securities with longer-duration unrealized losses for which an OTTI has already been recognized.

Question 30

What is the reference point (as described in the Interpretive Response to Question 29) for determining the duration of an unrealized loss for disclosure purposes for debt securities for which a reclassification was made between retained earnings and AOCI at the transition date?

Interpretive Response

The FSP does not provide specific guidance for determining the reference point for aging the newly computed unrealized loss which results from application of the new OTTI model. As a result, a variety of methods may be acceptable, and judgment will be needed to determine whether the resulting disclosures reasonably portray the nature of the unrealized loss position of debt securities. We believe that acceptable alternatives include using the reference point for each debt security for aging any AOCI amount that existed prior to the transition date as the reference point for aging the post-transition AOCI amount, or, if there was no amount in AOCI at the transition date, using the transition date as the reference point. The latter approach effectively treats the AOCI that results from adoption of the FSP as if the unrealized loss first arose at the transition date. Although such a result would be unlikely if the FSP had been applied in all prior periods, this approach is consistent with the FSP's transition guidance which does not require retroactive restatement or computation of a debt security's amortized cost based on cash flow expectations prior to the transition date.

We do not believe it is appropriate to use the transition date as the reference point when AOCI existed prior to the transition date, as this approach would effectively ignore the duration of the AOCI that existed at the transition date.

For example, assume the FSP is adopted by a calendar year company for the quarter ended June 30, 2009 and the pre-tax cumulative effect reclassification from retained earnings to AOCI for a particular debt security is $30. Assume also that the debt security had an existing AOCI amount of $5 at the transition date with a reference date of June 30, 2008. The reference point for aging the $35 total AOCI amount for the June 30, 2009 unrealized loss duration disclosure could be June 30, 2008. However, if the debt security instead had no existing AOCI amount at the transition date, the reference date for the $30 OCI transition amount could be April 1, 2009.

Deferred Tax

Question 31

How does the FSP's threshold for determining whether an OTTI exists affect the assertions made regarding recoverability of related DTAs under FAS 109, *Accounting for Income Taxes*?

Interpretive Response

Although the FSP changes the threshold for determining whether an OTTI loss exists, an entity would continue to need to assert that it has the intent and ability to hold its AFS debt securities to recovery (maturity, if necessary) to support its related DTAs. While practice in this area is still evolving, we believe that such assertion would be necessary for:

- An entity for which a capital loss, if triggered, would otherwise require a valuation allowance absent a source of capital gains;
- An entity that is placing reliance on recovery of the contractual cash flows of debt securities as an incremental objective source of future taxable income; and

- An entity that follows the Alternative View discussed in Question 15 of DataLine 2008-22.

Historically, given the similarity of assertions made for OTTI purposes and DTA realizability, little additional work was required to assess the reasonableness of the assertion made for tax purposes. Consideration may now need to be given to address the assertions made in the DTA realizabilty assessment that, while similar to those required for determining whether an OTTI loss exists, are not the same. In addition, companies should be aware that although subsequent sales of AFS debt securities may not necessarily call into question prior assertions that allowed losses to remain in OCI, such actions may nevertheless call into question assertions relating to DTAs where realizability was dependent on a strategy of holding securities to recovery (maturity, if necessary).

DataLine
2009-23

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PRICEWATERHOUSECOOPERS

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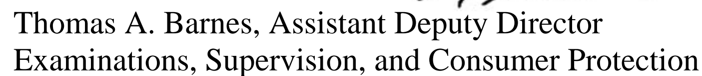
September 3, 2009

MEMORANDUM FOR: **CHIEF EXECUTIVE OFFICERS**



FROM: Thomas A. Barnes, Assistant Deputy Director
Examinations, Supervision, and Consumer Protection

SUBJECT: **Accounting Considerations Related to Other-Than-Temporary Impairment of Securities**

On August 28, 2009, OTS issued guidance to the examiner and supervisory staff regarding accounting considerations related to other-than-temporary impairment of securities. The guidance issued to OTS staff is attached for your information.

If you have any questions about this or other matters, please do not hesitate to contact your OTS Regional office.

Attachment

OTS Guidance to Examination Staff
Accounting Considerations Related to Other-Than-Temporary Impairment of Securities (Subsequent to adoption of FASB Staff Position FAS 115-2 and 124-2)

Executive summary

The global financial crisis has seen the fair value[1] of many securities decline below their amortized cost basis[2] and thus those securities are impaired under *U.S. generally accepted accounting principles* (**GAAP**). Consequently, thrift management must assess whether the fair value decline represents a temporary or *other-than-temporary impairment* (**OTTI**). This assessment is important as it can directly affect the accounting treatment, impacting earnings and regulatory capital. In certain circumstances for *debt* securities, OTTI is separated into two components: (1) the credit loss amount, recognized in earnings; and (2) the amount related to all other factors (**non-credit loss**) recognized in other comprehensive income (**OCI**), net of applicable taxes.

- Under GAAP**,** when the fair value of an available-for-sale (**AFS**) or held-to-maturity (**HTM**) security is less than its amortized cost basis, it is impaired. The impairment is either temporary or other than temporary. Other than temporary does **not** mean permanent.
- At each TFR reporting date, thrift management, not the external auditor[3], must assess securities for impairment.
- Assessing OTTI is complex and involves significant judgment. There are no "bright lines"; each assessment depends on the specific facts and circumstances associated with the individual security and the thrift.
- The greater the decline in fair value and the longer the period of time the security has been impaired (commonly referred to as **severity and duration**), the more difficult it will be to support a conclusion that the impairment is not OTTI. Other important factors to consider are discussed later.
- Management of different thrifts might come to different OTTI conclusions for the same security as the fact patterns could differ for individual thrifts. Accordingly, examiners must evaluate all of the available evidence when reviewing management's documented OTTI conclusions.

[1] Under GAAP Fair Value Measurements and Disclosures (FASB ASC 820), fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

[2] Amortized cost basis includes adjustments made to the cost of an investment for accretion, amortization, collection of cash, previous other-than-temporary impairments recognized in earnings (less any cumulative-effect adjustments recognized in accordance with the transition provisions of FASB ASC 320-10-65), and fair value hedge accounting adjustments.

[3] The thrift's financial statements, which will reflect the results of the OTTI assessment, are the responsibility of management. The external auditor opines as to whether the financial statements (the financial position, results of operations, and cash flows) are fairly presented, in all material respects, in accordance with GAAP.

2009 FASB issuances

The most significant 2009 issuances from the *Financial Accounting Standards Board* (**FASB**) include the following impairment standards:

- January 12, 2009 – *FASB Staff Position* (**FSP**) Emerging Issues Task Force (**EITF**) 99-20-1, *Amendments to the Impairment Guidance of EITF Issue No. 99-20 (***FSP EITF 99-20-1***)*; and
- April 9, 2009 – FSP *Financial Accounting Standards* (**FAS**) 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments* (**FSP FAS 115-2**).

On June 3, 2009, the FASB approved the *FASB Accounting Standards Codification*™ (**FASB ASC**) effective for financial statements for interim or annual reporting periods ending after September 15, 2009. OTTI accounting standards are in *FASB ASC 320 Investments – Debt and Equity Securities, 10 Overall, 35 Subsequent Measurement* (FASB ASC 320-10-35); and *FASB ASC 325 Investments – Other, 40 Beneficial Interests in Securitized Financial Assets* (FASB ASC 325-40). Both the superseded and codified accounting standard references are provided below for convenience.

The above standards substantially amends the two accounting models used for assessing OTTI:

A. *FSP FAS 115-1/FASB ASC 320-10-35* **(Investment security model)** is the general model that applies to debt and equity securities, as well as cost method investments[4].

B. *EITF 99-20/FASB ASC 325-40* **(Beneficial interest model)** is the specialized model that is applied to a subset of debt securities which are beneficial interests in securitized financial assets that: (1) are *not* of "high credit quality" (with high credit quality interpreted as included in the rating agencies' top two investment grades, e.g. AAA or AA), **or** (2) can be contractually prepaid in such a manner that substantially all of the recorded investment would not be recovered. Examples include interest-only strips or the residual interest in a securitization. Note that these investments are **also** subject to the Investment security model.

Simplified example of a debt security

Thrift A and Thrift B each purchase $100 of debt security XYZ at the same time and unit price. Subsequently, Thrift A decides to sell the security, while Thrift B has no intent to sell the security nor is it "more likely than not" that Thrift B will be required to sell the security. At the June 30, 2009 reporting date, the security is impaired by $40 (amortized cost basis equals $100 less fair value of $60). The $40 total impairment consists of $10 of estimated credit loss and $30 of estimated non-credit loss. For reporting purposes, Thrift A recognizes the entire impairment of $40 in earnings as management "intends to sell" the security. Thrift B recognizes the credit loss of $10 in earnings and the non-credit loss of $30 in OCI. So, although both thrifts have impairment of the security that is considered OTTI, the accounting treatment differs because the facts and circumstances differ for each thrift.

[4] "Cost-method investments" are equity securities that are not subject to the scope of FASB ASC 320 (Investments – Debt and Equity Securities) and FASB ASC 958 (Not-For-Profit Entities) and not accounted for under the equity method pursuant to FASB ASC 323 (Investments – Equity-Method and Joint Ventures) and related interpretations.

OTTI matrix **(prepared by the Office of Thrift Supervision)**

The OTS matrix below outlines the key questions to assess OTTI whenever the fair value of a security is less than its amortized cost basis.

DEBT SECURITY

Investment security model

(1) Intends to sell or (2) "more likely than not" will be required to sell before recovery of its amortized cost basis?	Are credit losses expected? (i.e., Is the PV of CF expected to be collected < the amortized cost basis?)	Impairment: Temporary or OTTI?	Accounting
No	**No**	**Temporary**	**Report AFS at fair value through OCI and HTM at cost**
No	**Yes**	**OTTI**	**OTTI separated:** • credit loss in earnings • non-credit loss in OCI
Yes	**N/A**	**OTTI**	**Recognize entire impairment loss in earnings.**

Beneficial interest model[5]

Does holder (1) intend to sell or (2) is it "more likely than not" holder will be required to sell before recovery of its amortized cost basis?	Answer	Accounting
	Yes	**Recognize entire impairment loss in earnings.**
	No	**Follow assessment under the Beneficial interest model below.**

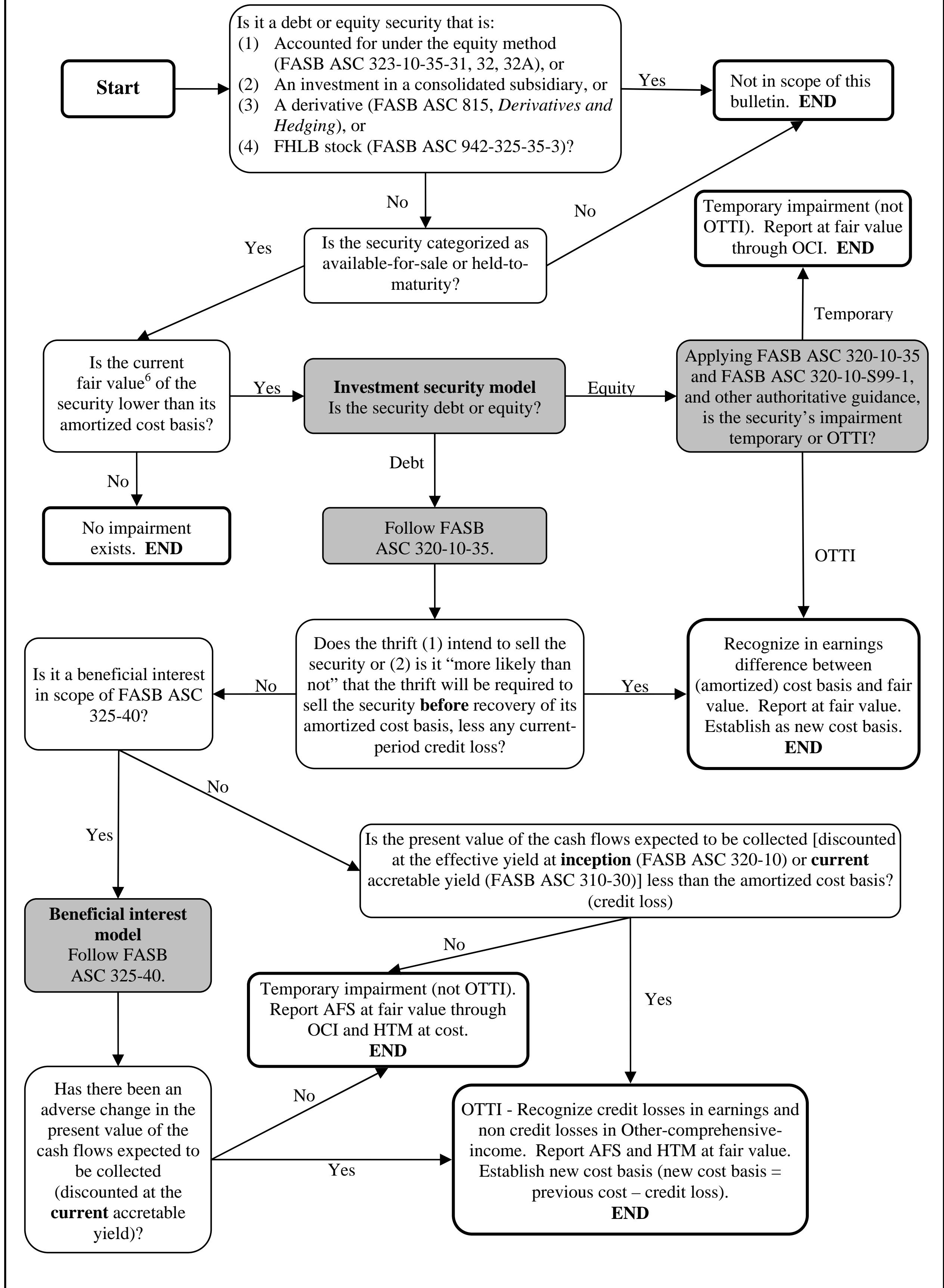
Is there an adverse change in the timing or amount of cash flows expected to be collected? (May indicate expected credit loss.)	Impairment: Temporary or OTTI?	Accounting
No	**Temporary**	**Report AFS at fair value through OCI and HTM at cost**
Yes	**OTTI**	**OTTI separated:** • credit loss in earnings • non-credit loss in OCI

EQUITY SECURITY

Investment security model

Intent and ability to hold to recovery of cost basis?	Impairment: Temporary or OTTI?	Accounting
Yes	**Temporary**	**Report AFS at fair value through OCI**
No	**OTTI**	**Recognize entire impairment loss in earnings**

[5] Only used for certain beneficial interests in securitized financial assets within scope of FASB ASC 325-40 model (see page 2, item B).


OTTI flowchart - Investment security & Beneficial interest models (debt & equity securities)
(Prepared by the Office of Thrift Supervision)
Start
Is it a debt or equity security that is:
(1) Accounted for under the equity method (FASB ASC 323-10-35-31, 32, 32A), or
(2) An investment in a consolidated subsidiary, or
(3) A derivative (FASB ASC 815, Derivatives and Hedging), or
(4) FHLB stock (FASB ASC 942-325-35-3)?
Yes
Not in scope of this bulletin. END
No
No
Temporary impairment (not OTTI). Report at fair value through OCI. END
Yes
Is the security categorized as available-for-sale or held-to-maturity?
Temporary
Is the current fair value[6] of the security lower than its amortized cost basis?
Yes
Investment security model
Is the security debt or equity?
Equity
Applying FASB ASC 320-10-35 and FASB ASC 320-10-S99-1, and other authoritative guidance, is the security's impairment temporary or OTTI?
No
Debt
No impairment exists. END
Follow FASB ASC 320-10-35.
OTTI
Is it a beneficial interest in scope of FASB ASC 325-40?
No
Does the thrift (1) intend to sell the security or (2) is it "more likely than not" that the thrift will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss?
Yes
Recognize in earnings difference between (amortized) cost basis and fair value. Report at fair value. Establish as new cost basis. END
No
Yes
Is the present value of the cash flows expected to be collected [discounted at the effective yield at inception (FASB ASC 320-10) or current accretable yield (FASB ASC 310-30)] less than the amortized cost basis? (credit loss)
Beneficial interest model
Follow FASB ASC 325-40.
No
Temporary impairment (not OTTI). Report AFS at fair value through OCI and HTM at cost. END
Yes
Has there been an adverse change in the present value of the cash flows expected to be collected (discounted at the current accretable yield)?
No
Yes
OTTI - Recognize credit losses in earnings and non credit losses in Other-comprehensive-income. Report AFS and HTM at fair value. Establish new cost basis (new cost basis = previous cost – credit loss). END

This bulletin covers the following topics:
A. Assessing OTTI of investment securities;
B. Supervisory expectations;
C. Authoritative references; and
D. Appendix.
- Application of GAAP with different types of securities;
- Scope of FASB ASC 325-40 (*Beneficial Interests in Securitized Financial Assets*); and
- Forward contracts and purchased options.

A. Assessing OTTI of investment securities

There are 3 key steps in assessing OTTI:
Step 1 - Determine whether an investment is impaired.
Step 2 - Evaluate whether impairment is temporary or other than temporary.
Step 3 - If impairment is other than temporary, recognize an impairment loss.

Step 1: Determine whether an investment is impaired.

If the fair value of the security is less than its amortized cost basis, it is impaired. A thrift shall determine whether an AFS, HTM, or cost-method investment[6] is impaired at the end of each quarter (TFR reporting period). A thrift should **not** "look through" the form of its investment; for example, an investment in a mutual fund that invests only in debt securities is assessed for OTTI as an equity security, not as a debt security.

Impairment shall be assessed at the individual security level. Individual security level means the level and method of aggregation used by the thrift to measure realized and unrealized gains and losses on its debt and equity securities. For example, equity securities of an issuer bearing the same Committee on Uniform Security Identification Procedures [CUSIP] number that were purchased in separate trade lots may be aggregated by a thrift on an average cost basis if that corresponds to the basis used to measure realized and unrealized gains and losses for these securities.

If the investment is impaired, proceed to Step 2.

[6] If the thrift **has** estimated the fair value of a cost-method investment, the estimated fair value shall be used to determine if the investment is impaired for the reporting periods in which the thrift estimates fair value. If the thrift has **not** estimated the fair value of a cost-method investment, evaluate whether an event or change in circumstances has occurred in that reporting period which may have a significant adverse effect on the fair value of the investment (an "impairment indicator") (FASB ASC 320-10-35-25). If an impairment indicator is present, then estimate the fair value of the investment, and if less than its cost basis, the investment is impaired; proceed to Step 2 of Section A in body of text. Impairment indicators (FASB ASC 320-10-35-27) include, but are not limited to, the following:
a. A significant deterioration in the earnings performance, credit rating, asset quality, or business prospects of the investee.
b. A significant adverse change in the regulatory, economic, or technological environment of the investee.
c. A significant adverse change in the general market condition of either the geographic area or the industry in which the investee operates.
d. A bona fide offer to purchase (whether solicited or unsolicited), an offer by the investee to sell, or a completed auction process for the same or a similar security for an amount less than the cost of the investment.
e. Factors that raise significant concerns about the investee's ability to continue as a going concern, such as negative cash flows from operations, working capital deficiencies, or noncompliance with statutory capital requirements or debt covenants.

Step 2: Evaluate whether the impairment is temporary or other than temporary.

The impairment is either temporary or other than temporary as determined through evaluation under the two accounting models, investment security or beneficial interest model, as appropriate. The evaluation is discussed below.

Debt securities

Investment security model

- ***Scope*** – This model applies to any investment security classified as HTM or AFS that meets the definition of a debt security under GAAP. These securities represent a creditor relationship and generally include:
  - U.S. Treasury securities, U.S. government agency securities, municipal securities, corporate bonds, convertible debt, commercial paper, all securitized instruments (e.g., CMOs, REMICs, CDOs), interest-only strips, and principal-only strips.
  - Trust preferred securities and pooled trust preferred securities (CDOs).
  - Certain *non-security* financial instruments accounted for under FASB ASC Transfers and servicing (FASB ASC 860.) Examples include interest only strips, retained interests in securitizations, loans, and other receivables or other financial assets that can be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment.
- ***Impairment*** (e.g., decline in fair value below amortized cost basis, which might occur as a result of a change in interest rates, market illiquidity, or credit quality) is OTTI if:
  (1) Management intends to sell the security, or
  (2) It is "more likely than not" that the thrift will be required to sell the security before recovery of its amortized cost basis, or
  (3) The thrift does not expect to recover its entire amortized cost basis in the investment security (credit loss).
- ***Severity and duration*** - The time horizon for recovery of a debt security's cost basis may be as far out as maturity, provided it is expected that all the cash flows will be received according to the contractual terms of the agreement. Under FASB ASC 320-10-35 "the length of time and the extent to which the fair value has been less than the amortized cost basis" needs to be considered (i.e., severity and duration) when evaluating whether a security is OTTI. Generally, the longer the period of time and greater the amount of decline in value, the more likely a security is OTTI. However, a decline in value due to expected credit losses may occur within a short period of time if the issuer of the security or underlying collateral of an asset-backed investment has experienced significant credit or value deterioration, with or without a payment default. On the other hand, a security that has a decline in value for more than a year may fully recover (e.g., pull to par at maturity). Any decision to sell a depreciated security prior to full recovery of its cost basis results in the recognition of an immediate loss at the time the *decision to sell* is made. Each security should be assessed based on its individual facts and circumstances as well as the plans and requirements of the thrift.

- There are numerous ***additional factors*** to be considered when estimating whether a credit loss exists and the period over which the debt security is expected to recover. The FASB ASC 320-10-35-33F list is not meant to be all inclusive. All of the following factors shall be considered:
    a. The length of time and the extent to which the fair value has been less than the amortized cost basis (see severity and duration discussion above).
    b. Adverse conditions specifically related to the security, an industry, or geographic area; for example, changes in the financial condition of the issuer of the security, or in the case of an asset-backed debt security, changes in the financial condition of the underlying loan obligors. Examples of those changes include any of the following:
        1. Changes in technology.
        2. The discontinuance of a segment of the business that may affect the future earnings potential of the issuer or underlying loan obligors of the security.
        3. Changes in the quality of the credit enhancement.
    c. The historical and implied volatility of the fair value of the security.
    d. The payment structure of the debt security and the likelihood of the issuer being able to make payments that increase in the future.
    e. Failure of the issuer of the security to make scheduled interest or principal payments.
    f. Any changes to the rating of the security by a rating agency.
    g. Recoveries or additional declines in fair value after the balance sheet date.
- A ***credit loss*** exists if the thrift determines that the present value of the cash flows expected to be collected is lower than the amortized cost basis.
    - For FASB ASC 320-10 debt securities one way of estimating the credit loss is to use the methodology applicable to receivables as described in FASB ASC 310-10-35. Under this methodology, a thrift discounts the cash flows management expects to collect at the effective interest rate implicit in the debt security when acquired. The OTS also will permit other reasonable measurement methodologies for the determination of credit loss that are consistent with GAAP. Any shortfall between the present value calculation and the debt security's amortized cost basis is a credit loss recognized through earnings.
    - For debt securities acquired with deteriorated credit quality within FASB ASC 310-30, credit losses (if any) are estimated as the excess of the amortized cost basis over the present value of cash flows management expects to collect, discounted at the accretable yield rate.
- For securities in the scope of the Beneficial interest model:
    - If the investor intends to sell the security or it is "more likely than not" it will be required to sell:
        - The security is OTTI (under the Investment security model) and should be written down to fair value through earnings.
    - If the investor does not intend to sell the security and it is not "more likely than not" it will be required to sell:
        - The securities should be evaluated for OTTI under the Beneficial interest model below.
- If OTTI, then proceed to Step 3.

Beneficial interest model

- ***Scope***
  - For securities in the scope of the Beneficial interest model where the investor does not intend to sell and it is not more likely than not that the investor will be required to sell, then evaluate using this model.
  - This model is used for beneficial interests classified as HTM or AFS that are either:
    - Not "high credit quality" ("high credit quality" is interpreted as included in the rating agencies' top two investment grades, e.g. AAA or AA), or
    - Can be contractually prepaid such that the thrift would not recover substantially all of its recorded investment.
- Determine whether there has been an adverse change in cash flows expected to be collected, when compared to the cash flows previously projected.
- Using management's best estimate of cash flows expected to be collected, ***if*** (a) the present value of the *original* estimate of remaining future cash flows expected to be collected at the initial transaction date (or the last date previously revised) ***is greater than*** (b) the present value of the *current* estimate of future cash flows expected to be collected, (with both (a) and (b) discounted at the current yield used to accrete income on the beneficial interest), ***then*** the change is considered adverse and the impairment is OTTI; proceed to Step 3.

Equity securities

Scope – This model applies to any investment security classified as AFS[7] that meets the definition of an equity security under GAAP. These securities represent an ownership interest and generally include:

- Common, preferred, or other capital stock,
- The right to acquire (for example, warrants, rights, and call options) or dispose of (for example, put options) an ownership interest in an entity at fixed or determinable prices, and
- Mutual funds, including mutual funds who invest only in debt securities.

The term equity security does not include any of the following:

- Written equity options (because they represent obligations of the writer, not investments),
- Cash-settled options on equity securities or options on equity-based indexes (because those instruments do not represent ownership interests in an entity), or
- Convertible debt or preferred stock that by its terms either must be redeemed by the issuing entity or is redeemable at the option of the investor.

Stock in the Federal Home Loan Banks (FHLB) is an equity security; however, the assessment of impairment[8] is outside the scope of this bulletin (FASB ASC 942-325-35-3).

[7] Equity securities have no stated maturity and therefore may not be classified as HTM.

[8] Several white papers on considerations for evaluating OTTI of FHLB stock have been produced and are available at OTS intranet: Other-than-temporary impairment guidance.

Both public and non-public thrifts shall apply SEC guidance codified as FASB ASC 320-10-S99-1, *Other Than Temporary Impairment of Certain Investments in Equity Securities*; and other applicable authoritative literature in assessing impairment. Factors to be considered include:

- "intent and ability to hold for any anticipated recovery in [fair value]," and
- "the length of time and extent to which the [fair] value has been less than cost" (i.e., severity and duration).

In assessing whether an equity security is OTTI, all available evidence should be considered, both positive and negative. The following facts and guidelines may assist in determining whether an OTTI exists:

- When a large number of negative factors exist and they outweigh positive factors, this would indicate that OTTI exists.
- If positive factors, which are cited as reasons that an OTTI does not exist, are more objectively verifiable than negative factors, the evidence may support a conclusion that the impairment is temporary.

The longer and the more severe the decline in fair value of the security, the more persuasive the evidence that is needed to support the premise that it is not OTTI. While there are no bright lines, it is difficult to conclude that an impairment of an equity security is not OTTI when the security has been impaired for a period of time longer than 6 to 9 months, the amount of the impairment is significant, and, importantly, market information indicates the prospects for recovery in the near-term are unlikely. For example, reliance on a 24-month recovery period may be overly speculative as it relies principally on the thrift's ability to predict the future direction of market prices for an equity security over an extended period of time. For an equity security, if the near-term (i.e., the next 6 to 9 months) prospects for recovery are unlikely, persuasive, but not conclusive, evidence exists that the impairment is generally considered OTTI.

When a thrift decides to sell an impaired available-for-sale equity security and the thrift does not expect the fair value of the equity security to fully recover prior to the expected time of sale, the security is deemed OTTI at the time that the *decision to sell* is made. If OTTI, proceed to Step 3.

SEC letter on impairment testing of perpetual preferred securities

Perpetual preferred securities are generally classified as equity securities on the issuer's balance sheet, as they do not have a contractual maturity date (note that the fact that a security may be "called" at the option of the issuer does not provide a basis to assert that the call provision is the same as a contractual cash flow at maturity). However, in a U.S. Securities and Exchange Commission (SEC) staff letter[9] to industry, the SEC staff concluded that:

- *Provided* that there has been no evidence of a deterioration of credit of the issuer (for example, a decline in the cash flows from holding the investment or a downgrade of the rating of the security below investment grade),
- The SEC would not object to an investor, only for purposes of impairment tests subsequent to October 14, 2008, applying an impairment model (including an anticipated recovery period) similar to a **debt** security until this matter can be further addressed[10] by the FASB.

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[9] Letter from Conrad Hewitt, SEC Chief Accountant, to Robert Herz, FASB Chairman, concerning the assessment of declines in fair value for perpetual preferred securities under the existing other-than-temporary impairment model in FAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. (October 14, 2008).http://www.sec.gov/info/accountants/staffletters/fasb101408.pdf

[10] As of the issuance of this bulletin the SEC and the FASB have not further addressed this issue. Examiners should contact their Regional Accountant if they have questions on this matter.

Step 3: If OTTI, recognize an impairment loss as follows:

Debt security

Investment security model

- If a thrift (1) does **not** intend to sell the debt security, **and** (2) it is **not** "more likely than not" that the thrift will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the OTTI shall be divided into two elements and reported as follows:
  a. The credit loss amount (the excess of amortized cost over the present value of cash flows expected to be collected) shall be recognized in earnings using an appropriate calculation methodology:
     - For FASB ASC 320-10 debt securities, discount the cash flows expected to be collected at the *original* effective interest rate at the date of acquisition (described in FASB ASC 310-10-35-20 through 35-29).
     - For FASB ASC 310-30 debt securities acquired with deteriorated credit quality, discount the cash flows expected to be collected at the *current* accretable yield (described in FASB ASC 310-30-35-8).

     For FASB ASC 325-40 Beneficial Interests refer to the Beneficial interest model section below.

  b. The amount related to other factors (non-credit loss) shall be recognized as a component of OCI, net of applicable taxes.

  Note: For financial reporting purposes, the OTTI amounts are presented in the statement of earnings as follows (amounts are for illustrative purposes only):

Total other-than-temporary impairment losses	($10,000) (total FV loss)
Portion of loss recognized in other comprehensive income (before taxes)	$4,000 (non-credit loss)
Net impairment losses recognized in earnings	($ 6,000) (credit loss)

- However, if a thrift (1) intends to sell the security or (2) it is "more likely than not" will be required to sell the security before recovery of its amortized cost basis less any current-period losses, the OTTI shall be recognized in earnings equal to the entire difference between the security's amortized cost basis and its fair value at the balance sheet date.

Beneficial interest model

- Similar to impairment recognition in the Investment security model, except the credit loss amount is determined based on discounting the cash flows expected to be collected using the yield currently used to accrete the beneficial interest (described in FASB ASC 325-40-35-4b), rather than the original effective interest rate (described in 310-10-35-20 through 35-29).

Equity security

Investment security model

- Recognize an impairment loss in earnings equal to the entire difference between the security's amortized cost basis and its fair value.

B. Supervisory expectations

Thrift management is responsible for assessing and documenting quarterly, whether each impaired security is OTTI under GAAP. The thrift's Board of Directors is ultimately responsible for ensuring that the assessment has been completed in a timely manner and that the assessment is reasonable. Reporting systems should be in place which monitor the severity and duration of securities impaired on an instrument-by-instrument basis. Management should have detailed written policies which state the criteria that lead to the rebuttable presumption that OTTI exists. Robust, documented evidence should support conclusions that impaired securities are not OTTI. Thrift management is also responsible for ensuring that there are robust processes for ensuring that security valuations are consistent with FASB ASC 820, *Fair Value Measurements and Disclosures* (FASB ASC 820).

Examiners should review and conclude on the adequacy, timeliness, and accuracy of the following practices:

- The fair value methodology and compliance with FASB ASC 820.
- The process used to evaluate individual securities in accordance with FASB ASC 320-10-35, and FASB ASC 325-40, as applicable.
- Management's policies and procedures to identify securities with potential OTTI.
- Documentation supporting temporary or OTTI determinations.

Thrift management may deem it appropriate to use pre-determined parameters, for example, based on the relationship of current fair value to cost basis, as a management tool to assist with prioritizing and determining the extent of the analysis to be performed to determine whether impairments are considered other than temporary. All securities with unrealized losses should be systematically reviewed each reporting period to determine whether an OTTI should be recognized. Declines in fair value that are significant but of short duration, or less significant but of a longer duration, may be indicators of OTTI. Note that the two examples of pre-determined parameters below are included <u>for illustration purposes only</u> and are not intended to be either requirements or safe harbors. Securities that fall within the predetermined parameters should be reviewed in greater detail to assess whether based on the facts and circumstances they are OTTI or not OTTI.

- Any security that is impaired by 7 percent or more for two consecutive quarters or any amount for twelve consecutive months.
- Any debt security, other than one backed by the full faith and credit of the U.S. government, that is impaired by greater than 10 percent or impaired by any amount for six consecutive months.

Appropriate documentation for examiners to review should include, but is not limited to:
Internal
- An analysis of the security's cost basis and fair value.
- The severity (dollar amount and percentage) and duration of the impairment.
- Investments as a percentage of assets, when considering examination scope.
- Impairment as a percentage of regulatory capital, when considering examination scope.
- Key components in the security's terms or structure that affect its fair value.
- Internal auditors OTTI review, if any.

External
- The financial performance of the issuer.
- The financial performance of the underlying collateral.
- The security's or issuer's credit rating, as applicable.
- Trends in the issuer's industry or underlying asset classes.
- Analyst reports, if available.
- External auditors OTTI review.

Disclosures
- The FASB ASC 825-10-50, *Financial Instruments, Overall, Disclosure.*
- The FASB ASC 320-10-50, *Investments – Debt and Equity Securities, Overall, Disclosure*.

Thrift management support includes its:
- Accounting and reporting policy for OTTI.
- OTTI analysis and the date performed.
- Expectations about the security's future performance based on the information available.
- Representations (preferably in writing) that they do not intend to sell and will not "more likely than not" be required to sell impaired securities prior to expected recovery, where appropriate.

Examiners should consider the thrift's business and liquidity plans as well as prior and contemplated transactions when assessing management's representations.

The determination that an investment security is OTTI has the following impact on GAAP equity and regulatory capital:

Debt (HTM and AFS)	**GAAP equity**	**Regulatory capital**
Losses in earnings	Reduces	Reduces
Non-credit losses in other comprehensive income	Reduces	*No impact/ "neutralized"*
Equity (AFS and cost method investments)	**GAAP equity**	**Regulatory capital**
Losses recorded in earnings	Reduces	Reduces
Losses in other comprehensive income	Reduces	Reduces

OTTI and Regulatory Capital – Illustration			
Assume investment security with:			
Amortized cost			$500
Credit losses		$30	
Non-credit losses		$20	
Total impairment		$50	($50)
Fair value			$450

Note: Credit and non-credit losses only apply to debt securities.

		Debt	
		Intend to sell?	
	Equity	Yes	No
GAAP capital, before OTTI	$1,000	$1,000	$1,000
Deduct total OTTI impairment	($50)	($50)	($50)
GAAP capital, after OTTI	$950	$950	$950
Add non-credit OTTI losses*	N/A	N/A	$20
Regulatory capital subtotal	$950	$950	$970

**In OCI and AOCI*

Examiners should advise management of any weaknesses or deficiencies in its OTTI policies and procedures and encourage management to consult with its external auditors, as necessary, in order to cure the identified weaknesses and deficiencies. Unresolved material differences between examiners and thrift management on OTTI assessments should be communicated to thrift senior management and/or board of directors, external auditors, OTS caseload supervisors, and the Regional Accountant, as appropriate.

C. References

- FASB ASC 320, *Investments-Debt and Equity Securities 10 Overall 35 Subsequent Measurement (***FASB ASC 320-10-35***)*, formerly:
  - FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities* (**FAS 115**),
  - FASB Staff Position FAS 115-1 and FAS 124-1, *The Meaning of Other Than Temporary Impairment and Its Application to Certain Investments* (**FSP FAS 115-1**) and
  - FASB Staff Position FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments* (**FSP FAS 115-2**)
- FASB ASC 325-40, *Beneficial Interests in Securitized Financial Assets* (**FASB ASC 325-40**), formerly:
  - EITF 99-20, *Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets* (**EITF 99-20**) and
  - FASB Staff Position EITF 99-20-1, *Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets* (**FSP EITF 99-20-1**)
- FASB ASC 820, *Fair Value Measurements and Disclosures* (**FASB ASC 820**), formerly:
  - FASB Statement No. 157, *Fair Value Measurements* (**FAS 157**)
- FASB ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality* (**FASB ASC 310-30**)*,* formerly*:*
  - Statement of Position 03-3, *Accounting for Certain Loans and Debt Securities* (**SOP 03-3**)
- SEC Staff Accounting Bulletin SAB Topic 5.M, *Other than Temporary Impairment of Certain Investments in Equity Securities* (**FASB ASC 320-10-S99-1**), also know as
  - SEC Staff Accounting Bulletin No. 111 (Topic 5M) *Other Than Temporary Impairment of Certain Investments in Equity Securities* (**SAB 111**) http://www.sec.gov/interps/account/sab111.htm
- SEC Office of the Chief Accountant and FASB Staff – *SEC Office of the Chief Accountant and FASB Staff Clarifications on Fair Value Accounting*. Refer to section titled: *What factors should be considered in determining whether an investment is other-than-temporarily impaired?* http://www.fasb.org/news/2008-FairValue.pdf
- *AICPA Statement on Auditing Derivative Instruments, Hedging Activities, and Investments in Securities* (**SAS 92**) http://www.aicpa.org/download/members/div/auditstd/AU-00332.PDF
- AICPA TPA# 21.30 *Application of SOP 03-3* (**TPA 03-3**) http://www.aicpa.org/download/acctstd/TPA_03-3.pdf
- 2004 *Uniform Agreement on the Classification of Assets and of Securities Held by Banks and Thrifts* (**CEO Letter # 200**) http://files.ots.treas.gov/25200.pdf
- Audit firms other-than-temporary impairment literature. OTS intranet: Other-than-temporary impairment guidance

D. Appendix

The table below illustrates the application of GAAP for different types of securities:

Type	FASB ASC 320-10-35 In Scope?	FASB ASC 325-40 In Scope?	Model(s)
DEBT SECURITIES			
All investments in AFS and HTM debt securities	Yes	No	1. Investment security model
Certain non-consolidated beneficial interests not of "high credit quality" or pre-payable at less than cost basis	Yes	Yes	1. Investment security model 2. Beneficial interest model, if do not intend to sell or not "more likely than not" will be required to sell
EQUITY SECURITIES			
Most investments with readily determinable fair values (excludes cost method investments)	Yes	No	1. Investment security model
Cost-method investments[6]	Yes	No	

Scope of FASB ASC 325-40, *Beneficial Interest in Securitized Financial Assets*

Included in the scope are all asset backed securities (ABS), collateralized debt obligations (CDOs) and residential and commercial mortgage-backed securities (RMBS or CMBS) **not** guaranteed by the U.S. government or its agencies, or **not** sufficiently collateralized to ensure that there is a remote possibility of credit loss (i.e., principal and/or interest).

Excluded from the scope are securities that meet both of the following criteria:

- The security is of "high credit quality" (interpreted as included in the rating agencies' top two investment grades, e.g. AAA or AA); **and**
- The security cannot be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment.

The SEC has indicated that it is acceptable to determine whether a security is within this scope: (1) at acquisition only, or (2) at acquisition and on an ongoing basis, i.e. evaluate at each period end. These are the two most common approaches. For example, a thrift could consider a debt security that was AAA rated at acquisition as scoped out even upon a subsequent credit rating downgrade to BBB because the scope determination was made at acquisition only. Alternatively, a thrift could evaluate each security at each quarter-end to determine if it currently would be within the scope based upon its current credit rating. Thrifts should specify in their accounting policies which scope determination method is used.

Forward contracts and purchased options

Changes in the fair value of forward contracts and purchased options to acquire investment securities (under FASB ASC 320) that are not derivatives (under FASB ASC 815), such as one that is not readily convertible to cash, must be recognized immediately in earnings or OCI, subject to an OTTI assessment. The determination of where to record changes in fair value (in earnings or OCI) is based on the designation of the underlying asset as HTM, AFS, or Trading (FASB ASC 815-10-35-5).