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Financial Restatements: Observations from the
Federal Reserve

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Presentation Topics

- Federal Reserve Views on Financial Restatements
- Federal Reserve Review of Recent Public Restatements of Banking Organizations
 - Top Ten Causes of Banking Organization Restatements
 - Supervisory Responses to Banking Organization Restatements
- Federal Reserve Review of Recent Restatements of Regulatory Reports

Federal Reserve Views on Financial Restatements

- The Federal Reserve is a significant user of financial data and collects more than 90 reporting series including:
 - Financial statement reporting series
 - Applications and structure reporting series
 - Monetary policy reporting series
 - FFIEC reporting series
 - Business and consumer credit reporting series
 - Research reporting series
- The Federal Reserve also collects securities filings from certain banks under delegated authority from the SEC

Federal Reserve Views on Financial Restatements

- Accurate, reliable public financial statements promote financial stability and foster market discipline
 - Restatements can gradually erode market confidence
- Public financial statements and regulatory reports are critical elements to our supervisory program
 - Restatements may require supervisors to spend more time in institutions
- Preparers, auditors, investors and supervisors all benefit from high quality financial statements

Federal Reserve Review of Recent Banking Organization Restatements

Scope:

- Banking organizations included in the U.S. GAO Financial Restatement Database
 - Covers restatements of previously reported public financial information due to financial reporting fraud and accounting errors
 - Public announcements of restatement from July 1, 2002 through June 30, 2006
 - <http://www.gao.gov/cgi-bin/getrpt?GAO-06-1079SP>

Federal Reserve Review of Recent Banking Organization Restatements

Scope:

- Banking organizations were defined as entities with the following Standard Industrial Classification (SIC) Codes
 - 6021 - NATIONAL COMMERCIAL BANKS
 - 6022 - STATE COMMERCIAL BANKS
 - 6029 - COMMERCIAL BANKS
 - 6035 - SAVINGS INSTITUTION, FEDERALLY CHARTERED
 - 6036 - SAVINGS INSTITUTIONS, NOT FEDERALLY CHARTERED
 - 6099 - FUNCTIONS RELATED TO DEPOSITORY BANKING

Federal Reserve Review of Recent Banking Organization Restatements

Review:

- Public filings to identify the reason for the restatement
- Supervisory materials to determine the degree of awareness and involvement of the banking supervisors in the restatement process
- Supervisory actions following a restatement, including requiring amendments to regulatory reports



Top Ten Reasons Given for Restatements

1. Misapplication of various aspects of FAS 140
2. Misapplication of the accounting rules for derivatives, primarily the inappropriate use of the “short-cut” method
3. Circumstances governing the determination of securities impairment and asset valuations
4. Clarification of the accounting rules for employee compensation and benefits

Top Ten Reasons Given for Restatements

Con't

5. Changes in the facts, circumstances and judgment in the estimation of the allowance for loan lease losses, provision for loan and lease losses and charge-offs
6. Misapplication of the facts and circumstances in business combinations and sales of business units
7. Inappropriate application of FAS 91, improper fee recognition, and premium/discount amortization errors
8. Errors in the calculation of income taxes

Top Ten Reasons Given for Restatements

Con't

9. Errors in the reporting of stockholders' equity transactions or the presentation of transactions in the statement of cash flows
10. Other, including:
 - Fraud
 - Lease Accounting
 - FAS 5 Gain/Loss Contingencies

Supervisory Involvement in Restatements

- Supervisors are generally aware of restatements at banking organizations with onsite supervision during the deliberative stages of the decision to restate
 - Likely change the supervisory plan to scope in additional areas or more fully explore areas where weaknesses are suspected
- Supervisors are often not aware of restatements at banking organizations with no onsite supervision until, or near, the time the restatement is made public
 - Likely will impact the scoping process for full scope inspections/examinations under risk focused supervision

Supervisory Responses to Restatements

- Restatements do not automatically result in a downgrade of either the organization's RFI/CD (formerly BOPEC) or CAMELS ratings
 - However, as previously mentioned, restatements impact the inspection/examination process
- Supervisors generally require management to take corrective measures with regard to deficient accounting policies and internal controls over financial reporting
 - Management is likely already focused on this because of Sarbanes-Oxley section 404 or FDICIA section 112

Supervisory Responses to Restatements (Con't)

- Supervisors generally require the organization to file amended regulatory reports consistent with the restatement
 - Particularly, in cases where the restatement would be material to regulatory capital or asset quality measures
 - However, the timing of the filing of the amended regulatory reports varies based on the views of the primary banking regulator of the entity responsible for recording the restatement

Federal Reserve Review of Recent Restatements of Regulatory Reports

Scope:

- Banking organizations amending holding company FR Y-9C reports or bank Call Reports after the filing deadline for the June 30, 2007 and March 31, 2007 report dates

Review:

- Identify the most frequently amended items
- Determine whether a supervisory action was the source of the amendment

FR Y-9C Restatements

	# of FR Y-9C Filers	# of Filers with Restatements	# of Data Items Revised
June 30, 2007 Filers			
Total assets > \$1 billion	444	12	158
Total assets ≤ \$1 billion	536	15	58
March 31, 2007 Filers			
Total assets > \$1 billion	441	147	1,742
Total assets ≤ \$1 billion	547	144	1,360

Top FR Y-9C Restatements

1. Schedule HC-R, Risk-Based Capital - Various items
2. Schedule HI, Income Statement – Various noninterest income and noninterest expense items
3. Schedule HC-E, Deposit Liabilities – Time deposit items
4. Schedule HC-C, Loans and Leases – Loans secured by nonfarm nonresidential properties and 1-4 family construction loans
5. Schedule HC-L, Off-balance sheet – Loan commitments

Bank Call Report Restatements

	# of Call Report Filers	# of Filers Restating ¹	# of Data Items Revised
June 30, 2007 Filers			
Total assets > \$1 billion	557	48	959
Total assets ≤ \$1 billion	7,305	208	4,024
March 31, 2007 Filers			
Total assets > \$1 billion	548	45	2,368
Total assets ≤ \$1 billion	7,348	208	9,252

1 – Data reflects filers restating 6 or more items for the June report date and 24 or more items for the March report date.

Top Call Report Restatements

1. Schedule RC-R, Risk-Based Capital - Various items
2. Schedule RC-E, Deposit Liabilities – Time deposit items and maturity information
3. Schedule RC-K, Quarterly Averages – Time deposit items
4. Schedule RI, Income Statement – Various noninterest income and noninterest expense items
5. Schedule RC-C, Loans and Leases – Loans secured by nonfarm nonresidential properties and 1-4 family construction loans

Questions

