
**Update from the Division of Corporation
Finance
*AICPA National Conference on Banks & Savings
Institutions*
September 12, 2012**

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U.S. Securities and Exchange Commission



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Speaker Biography

Stephanie J. Ciboroski
U.S. Securities and Exchange Commission

Stephanie Ciboroski is a Senior Assistant Chief Accountant in the SEC's Division of Corporation Finance office that is responsible for resolving technical accounting, financial reporting and disclosure issues related to the large financial institutions. Prior to January 2011, Stephanie was an Associate Chief Accountant in the Chief Accountant's Office of the Division of Corporation Finance where her responsibilities primarily included consultation with registrants and Commission staff on accounting and reporting matters in the Financial Services industry. Stephanie joined the Commission staff in 2002 as a staff accountant in the Division of Corporation Finance. Prior to that, Stephanie was an audit manager with Ernst & Young.

Stephanie graduated summa cum laude from the University of Maryland at College Park.

Speaker Biography

Mark Shannon

U.S. Securities and Exchange Commission

Mark Shannon is an associate chief accountant in the Division of Corporation Finance's Chief Accountant's Office (CF-OCA) of the Securities and Exchange Commission. He currently serves as a liaison for the Division's Financial Services I and Consumer Products disclosure operations groups. Mark also previously served in various positions in the Division's disclosure operations group, including in the Office of Natural Resources and the Office of Information Technologies and Services.

Prior to joining the SEC in July 2007, Mark worked in the Houston office of PwC where he served clients primarily in the financial services sector. He attended the University of Houston where he majored in Accounting. He is licensed as a CPA in the state of Texas.

Agenda

- **Organization of the Division of Corporation Finance**
- **Frequent Areas of Staff Comment on Accounting & Disclosure Matters**
- **Resource Links**

Organization of the Division of Corporation Finance

■ Responsibilities

- ❖ Selectively review the disclosure documents filed by public companies (including initial registrations)
- ❖ Provide interpretive assistance on SEC rules and forms
- ❖ Recommend new and revised rules to the Commission

■ Organization

- ❖ Disclosure Operations (12 industry groups)
- ❖ Legal and Regulatory Policy
- ❖ Office of Chief Accountant
- ❖ Policy and Capital Markets

Organization of the Division of Corporation Finance

The Financial Services Industry Group is divided into two separate groups:

- Office of Financial Services I (Office #7)— consists of approximately 700 financial institutions, including the vast majority of all community & mid-tier financial institutions
- Office of Financial Services II (Office #12) — consists of approximately 140 registrants representing 60+ of the largest financial institutions in the world (including 29 FPIs), as well as the GSEs and broker dealers of various sizes

Organization of the Division of Corporation Finance

Office of Financial Services I - Contact at: (202) 551-3770

- ❖ Todd Schiffman – Assistant Director
- ❖ John Nolan – Senior Assistant Chief Accountant
- ❖ Amit Pande – Accounting Branch Chief
- ❖ Sharon Blume – Assistant Chief Accountant

Office of Financial Services II - Contact at: (202) 551-3830

- ❖ Suzanne Hayes– Assistant Director
- ❖ Stephanie Ciboroski– Senior Assistant Chief Accountant
- ❖ Kevin W. Vaughn – Accounting Branch Chief
- ❖ Hugh West – Accounting Branch Chief

Organization of the Division of Corporation Finance

Corporation Finance – Office of the Chief Accountant (CF-OCA)

- **Mark Shannon – liaison to Fin Services I**
- **Kyle Moffatt – liaison to Fin Services II**

Contact us: (202) 551-3400

Primary Role:

- **Assist the review offices on complex matters**
- **Responsible for processing waiver requests and participating in OCA submissions**

DCF Comment Process

- **Types of Comments**
 - ❖ Request for additional supplemental information
 - ❖ Provide additional or different disclosure in a future filing
 - ❖ Amend filing to revise financial statements or disclosure
 - ❖ Completion of review letter
- **Gramm-Leach-Bliley process for sharing comment letters with Bank Regulators**
- **Comment letters and responses are posted on website (www.sec.gov) after review is closed**

Frequent Areas of Staff Comment

- 1. Loans & Allowances– 2nd Lien Loans, Credit Loss Disclosures, Credit Trends and Allowance Releases, Smaller Financial Institutions**
- 2. Troubled Debt Restructurings & Modifications**
- 3. Deferred Tax Assets**
- 4. Purchased Credit Impaired Loans**
- 5. Goodwill Impairment Testing**
- 6. FDIC-Assisted Acquisitions**
- 7. Fair Value Disclosures**
- 8. Mortgage Repurchase Reserves**
- 9. Other**

Loans & Allowances – 2nd Lien

Loans

- Continue to issue comments to understand how lack of information about the performance of the 1st lien is taken into consideration in developing the ALLL for 2nd liens
 - Financial institutions may have more limited information about the status of the 1st lien if they do not also hold or service the 1st lien
 - In many cases, the 2nd lien may still be performing, even though 1st lien may not be
 - Regulatory Guidance and increases of 2nd lien NPLs in Q1 2012

Loans & Allowances – 2nd Lien

Loans (cont'd)

- **Comments issued to obtain enhanced disclosure regarding different trends in 1st liens versus 2nd liens.**
 - **Example: Delinquency statistics may be lower for 2nd liens but charge-off ratios are higher**
- **Disclosure on when the HELOCs will convert to amortizing (and minimum payments increase)**
- **Data on whether different trends for loans that have converted to amortizing (i.e. higher delinquency or default statistics)**
- **Percent of borrowers making the minimum due (i.e. no principal payment) while in draw period**

Loans & Allowances - Credit Loss Disclosures

Typical Comment Themes:

1. Credit quality indicators

- Disclosed indicator not at the same granular level used internally (for example, commercial & corporate loans classified as performing vs. non-performing) or very wide FICO bands
- Enhanced disclosure about how the indicators relate to likelihood of loss
- Disclosure about updating or monitoring LTV ratios
- Lack of CQIs for consumer loans

Loans & Allowances - Credit Loss Disclosures (cont'd)

2. Charge-off and Nonaccrual Policies

- **Simply stating that charge-off policies comply with regulatory requirements instead of stating those thresholds**
- **Lack of discussion about factors considered for loans that are not charged-off at a specific past due threshold – for example C&I or CRE loans, when management determines the loan is no longer probable of collection**

Loans & Allowances – Credit Trends and ALLL Releases

- **Many financial institutions have had reserve releases (net charge-offs exceeding provision for loan losses) during the past two years**
- **Staff closely reviews credit trends and looks for directional consistency**

Typical Comment Themes:

- **Transparent disclosure about effect of reserve releases on net income (also consider risk factor disclosure)**
- **Change in ALLL methodologies**
- **Fluctuations in different components of the allowance relative to the total allowance**

Loans & Allowances – Credit Trends and ALLL Releases (cont'd)

Typical Comment Themes, cont'd

- **Fluctuating ratio of allowance to total loans with no clear disclosure supporting the change in trends**
- **Fluctuating coverage ratio (allowance to total non-performing loans) with no clear disclosure supporting the change in trends**
- **Large unallocated allowance presented under Guide 3 disclosure – particularly if not changing from period to period**
- **Clarity on how qualitative and other environmental factors are considered in the ALLL**

Loans & Allowances – Smaller Financial Institutions

- Continue to issue comments – themes generally consistent with prior years
- DGT No. 5
<http://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic5.htm>

Typical Comment Themes:

- Transparent disclosure about effect of reserve releases on net income (also consider risk factor disclosure)
- Change in ALLL methodologies
- Fluctuations in different components of the allowance relative to the total allowance

TDRs and Modifications

Common themes:

- Indication that workout programs are used without adequate explanation of the types of programs and quantification of the modified loans
- Indication that certain modified loans are not being accounted for as troubled debt restructurings without explanation of the reasons why
- The nonaccrual policy for restructured loans and effects on past due statistics
- Clarity on how “payment default” is defined for purposes of disclosure on defaults of TDRs
- Greater specificity on how defaults of TDRs are factored into the ALLL

TDRs and Modifications (cont'd)

If material amount of TDRs that continue to accrue interest, consider disclosing:

- **All the factors that were considered at the time a loan is restructured to determine whether the loan should accrue interest**
- **How the financial institution determined that the loan has been restructured so as to be reasonably assured of repayment and of performance**

TDRs and Modifications (cont'd)

May request enhanced disclosure when a financial institution removes loans from TDR disclosures due to the passage of time or due to loans with re-modified terms that qualify as new loans and that do not contain a concession

- **Disclose the entity's policy for all scenarios that would result in a TDR no longer being considered a TDR**
- **Quantify the amount of loans for which and the reasons why TDR designation has been removed**
- **Consider providing a roll-forward of TDRs if needed to provide sufficient information with respect to TDR activity**

Deferred Tax Assets

ASC 740-10-30-17

- “All available evidence, both positive and negative, shall be considered...”

ASC 740-10-30-21

- “Forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years”

Deferred Tax Assets – Areas of Staff Comment

- In evaluating cumulative loss scenario, excluding the significant increase in the loan loss provision during the current year
- Non-objective evidence in supporting how DTA will be realized, particularly if based substantially on income not expected to be achieved for several years in the future
- Lack of disclosure supporting the appropriateness of a partial valuation allowance

Deferred Tax Assets – Areas of Staff Comment

- Disclose both the positive and negative evidence considered in determining the extent of any valuation allowance and how such evidence was weighted
- To the extent there is reliance on tax planning strategies or offset of deferred tax liabilities in lieu of projected future taxable income for the realization of the DTAs, disclosure of these facts and a description of such strategies

Purchased Credit Impaired Loans

- **Determination that a portion of the acquired loans had a discount due at least in part to credit quality**
- **Aggregation of acquired loans into pools**
- **Disclosure**

Purchased Credit Impaired Loans (cont'd)

Similar credit risk?

Goodwill Impairment Testing

Determination of Reporting Units Carrying Value

- Many financial institutions appear to use an economic capital or risk-based capital approach as a proxy for the CV of their reporting units
- ASC 350-20-35-39 requires all assets and liabilities to be allocated to a reporting unit unless the specified criteria are met

Goodwill Impairment Testing

(cont'd)

If the reporting unit CV is determined using a capital allocation model, disclose:

- Policy for determining the CV of the reporting units
- Whether there is any “residual remainder” that is not allocated to the reporting units and what it represents
- How Step 2 of the goodwill test is performed when required

FDIC-Assisted Acquisitions

FDIC-assisted acquisitions - raise questions on the application of ASC 805 and ASC 310-30

- FDIC facilitates sale of a failing financial institution
- Company purchases the assets and liabilities of a failing financial institution
- FDIC enters into a Loss Sharing Arrangement (LSA) with the Company that indemnifies them from certain losses incurred on assets covered under the arrangement
- The indemnification asset and loans are measured initially by the Company at fair value in accordance with ASC 805
- Credit-impaired loans acquired are accounted for under ASC 310-30. Any subsequent increases in expected cash flows are accreted into income

FDIC-Assisted Acquisitions (cont'd)

- How do you subsequently measure the indemnification asset if there is a subsequent increase in cash flows related to the covered loans which results in a decrease in amounts collectible in the indemnification asset?
- What is meant by “measure on the same basis” and “subject to contractual limitation”?

FDIC-Assisted Acquisitions (cont'd)

FASB Proposed ASU – Comments were due July 16th, 2012

- **Amortize the decrease in the indemnification asset over the shorter of the term of the LSA and the term of the related loans**
- **Apply prospectively – any new indemnification assets and changes in cash flows on existing indemnification assets**

FDIC-Assisted Acquisitions (cont'd)

S-X Reporting: SAB Topic 1:K Waivers

- **Background**
- **Significance Tests**
- **Transactions without loss sharing**

Fair Value Disclosures

ASU 2011-04 went into effect in Q1 2012 10-Qs

Typical Comment Themes:

- **Disclosure of a wide range of data for the significant inputs – suggest also providing weighted average input and discussion of how that amount is determined**
- **Where multiple techniques are used for a class of instruments, quantification of the amount valued under each approach**
- **Not granular enough disclosure for the qualitative sensitivity disclosure**

Mortgage Repurchase Reserves

Continue to see large additions to the provision for mortgage repurchase reserves, as well as the inability to estimate the range of reasonably possible losses over the amount accrued in certain circumstances

Typical Comment Themes:

- Expanded disclosure supporting the factors driving the significant new provisions each quarter (particularly given vast majority of repurchase requests stem from 2006-2008)
- Changes in methodologies
- Request to continually evaluate providing the required ASC 450 range disclosure

Other Frequent Areas of Comment

- MD&A Disclosures
- Item 4.02 Form 8-Ks
- MSR Disclosures
- Basel III Capital/Liquidity Ratios
- Reporting Considerations for Bank Holding Companies under the JOBS Act
- Sovereign Debt Exposures
- VAR Disclosures

MD&A Disclosures

- **Disaggregation of revenue streams and discussion of drivers of changes in the fees**
 - **Examples: ATM Fees, Deposit Fees, Interchange Fees, etc.**
- **Critical accounting estimates**

Item 4.02 Form 8-Ks

- Compliance with the requirements of the form
- Description of the facts underlying the conclusion
- Any other relevant disclosures?

Mortgage Servicing Rights (MSR) Disclosures

Comment themes:

- **Wide range of assumptions disclosed – may request more granular disclosure by loan type or interest rate**
- **Lack of discussion about drivers of change in value – comments request separate discussion and quantification of factors driving the change in value as factors are often offsetting (lower prepayment speed versus higher servicing costs, etc.)**
- **Large changes in FV during the period – greater than the most recent sensitivity disclosed**

Basel III Capital/Liquidity Ratios

- Given that these capital ratios are not yet required by the banking regulations, they are non-GAAP measures
 - C&DI: Question 102.12
- Examples: Tier 1 common ratio, risk weighted assets, liquidity coverage ratio (LQR)
- Clearly disclose assumptions used in developing the metrics and that the measure may not be calculated consistently with others given that the rules are not yet finalized

Reporting Considerations: Bank Holding Companies under the JOBS Act

- **Termination of a bank holding company's reporting obligation under Section 12(g) of the Exchange Act**
- **Except in certain circumstances, the Form 15 is not effective for 90 days.**

Sovereign Debt Exposures

European sovereign debt exposure

- DGT No. 4 Issued January 2012 -
<http://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic4.htm>
- Indirect Exposures
 - Interpreted differently among companies

Sovereign Debt Exposures (cont'd)

- **Examples seen in disclosures:**
 - **Other entities that are highly exposed to the affected areas, indirect effects resulting from the impact on Western European banking sectors, slowdown in global economic activity and wider economic contraction in the corporate sector, potential for redenomination and devaluation risk, effects to payment and clearing systems or global exchanges, etc.**
- **Describe how indirect risk is considered and managed – be specific on factors considered in stress testing**

Value-at-Risk (VAR) Disclosures

Item 305 of S-K – Market Risk Disclosures (VAR is one option that may be selected but is not required)

Typical Comment Themes:

- **Number of different VAR models that are used to determine total trading VAR and the factors driving the need to use multiple different models**
- **How the different VAR models are aggregated to arrive at total trading VAR**
- **Whether the VAR models used for regulatory capital purposes are the same as the VAR models used for the Market Risk disclosures**

Value-at-Risk (VAR) Disclosures

(cont'd)

Typical Comment Themes (cont'd)

- Types of risks excluded from VAR calculation and why
- Process and validation procedures in place prior to implementing significant model and assumption changes, including whether regulatory approval is required
- Thought process for disclosure requirements under Item 305(a)(4) regarding model, assumptions and parameter changes

Questions???

Resources

www.sec.gov/divisions/corpfin.shtml

❖ General

- Filing Review Process
- Statutes, Rules, and Forms
- Compliance & Disclosure Interpretations
- What's New
- Information for Small Businesses (including JOBS Act Materials):
www.sec.gov/info/smallbus.shtml

Resources

Information for Accountants

www.sec.gov/divisions/corpfin/cfreportingguidance.shtml

- ❖ Division Financial Reporting Manual
- ❖ Compliance & Disclosure Interpretations
- ❖ Staff Accounting Bulletins
- ❖ Corporation Finance Comment Letters
- ❖ Corporation Finance Filing Review Process
- ❖ Other Frequently Requested Material
 - Letters to Industry (a/k/a “Dear CFO Letters”)
 - CF Disclosure Guidance Topics