DEAR BOARD OF DIRECTORS:

Earlier this year, we issued Letter to Credit Unions No. 99-CU-06 which discussed proposed changes to the Call Report. This letter discusses the comments we received, as well as our responses to the comments. As noted in Letter to Credit Unions No. 99-CU-06, changes to the Call Report were mandated by Congress in Public Law 105-219, the Credit Union Membership Access Act. The new law added Section 202(a)(6)(C) to the Federal Credit Union Act [12 U.S.C. 1782(a)(6)], which requires that reports filed with NCUA be consistent with generally accepted accounting principles (GAAP).

SUMMARY

We received responses from 34 commenters, including twenty credit unions, five credit union leagues, three trade associations, one state regulator, and one corporate credit union. The two most common areas of comment were changes required by GAAP: classifying shares as liabilities, and classifying the NCUSIF deposit as an “other asset.” In addition to these two areas, comments addressed combining the federal credit union and state credit union versions of the form, new questions on cyber financial services, implementation date of the changes, CUSO reporting, various instruction clarifications, and suggested new line items.

COMBINING THE FCU AND SCU FORM VERSIONS

Five comments support combining the federal credit union and state credit union forms into a single form. No comments opposed this combination. One comment suggested that NCUA provide a separate Call Report form for credit unions with assets less than $10 million because the new law provides an exception to the GAAP reporting requirement for these credit unions. NCUA considered this option before proposing the changes; however, the costs associated with creating and
maintaining two forms and two PC5300 programs would ultimately fall on credit unions through increased fees. Additionally, data comparability would be questionable. Therefore, only one form will be used, regardless of asset size.

**SHARES**

Seven comments supported the GAAP changes in general. Two of the changes required by GAAP were also the two changes addressed most frequently. The first of these is the classification of shares as liabilities. Three comments support this change because it complies with GAAP. Ten comments oppose this change, primarily on philosophical grounds. After the comment period officially ended, we received a second letter from a commenter which raises a legal question about the classification of shares as liabilities. We believe this issue requires further review by NCUA’s technical staff and general counsel. Therefore, shares will remain in their traditional classification on page 2 of the call report pending further review.

**NCUSIF DEPOSIT**

The second most frequent area of comment is the classification of the NCUSIF deposit as an “other asset” rather than its traditional classification as an investment. Four comments support this change noting that it both complied with GAAP and provided for a better measure of yield on investments. Six comments oppose this change, again primarily on philosophical grounds. Some comments expressed concern that not classifying the NCUSIF deposit as an investment could adversely affect the future of the deposit. Another comment suggested that this change would cause the NCUSIF deposit to be considered a risk asset.

Classification of the NCUSIF deposit as an “other asset” rather than as an investment on the Call Report is necessary to meet the GAAP reporting requirements set forth in the Federal Credit Union Act. Placement of the NCUSIF deposit on the Call Report in no way affects its future value. Additionally, the NCUSIF deposit is specifically defined as a non-risk asset by Section 700.1(i)(18) of the NCUA Rules and Regulations. (Note: The concept of risk assets will be eliminated with the implementation of the prompt corrective action net worth requirements in August 2000.)

**CYBER FINANCIAL SERVICES**

Nine comments opposed the collection of website host and vendor information, stating that there was no specific purpose, special risk, safety and soundness issues, and that the information is not required by other financial regulators. Most comments called for NCUA to remove these questions from the Call Report.

NCUA disagrees with these conclusions. In recent years, credit unions led all financial institutions in establishing a presence on the Internet. Credit unions
continue to embrace new technology for the benefit of their members: approximately one-fourth of all federally insured credit unions reported having a website as of June 1999, with one-fourth of those reported as interactive. Credit unions’ participation in cyber financial services has grown exponentially, and is expected to continue doing so as more credit unions offer these services to their members. Like other vendor services, cyber financial services present risk to credit unions, and therefore are a safety and soundness issue. Obtaining host and vendor information is essential for NCUA’s risk assessment of the credit union cyber financial services environment.

This conclusion was recently cited by the United States General Accounting Office in their report “Electronic Banking: Enhancing Federal Oversight of Internet Banking Activities” (GAO/GGD-99-91, July 1999). This report recommended to the United States Congress that NCUA:

...establish procedures to obtain centralized information on institutions’ plans to offer Internet banking. . . .[and] use this information to: (1) enhance monitoring of technological trends and innovations and thus their ability to assess emerging security and compliance issues; (2) provide more timely and specific risk management guidance to individual depository institutions, as necessary; and (3) augment the information used to plan the scope and timing of future examinations as well as to plan for the availability of examiners with appropriate information systems expertise.

The GAO report also recommends that NCUA “develop . . . procedures and begin to examine Internet banking related activities offered by credit unions.” NCUA believes that having these questions on the Call Report is necessary to implement such a program.

IMPLEMENTATION DATE

Six comments suggested that implementation of changes to the Call Report be delayed until next year, either for the sake of consistency or due to Y2K concerns. The GAAP reporting requirement of Section 202(a)(6)(C) of the Federal Credit Union Act was effective August 7, 1998, when the Credit Union Membership Access Act was signed into law. Delaying implementation more than a year beyond the effective date cannot be justified. Therefore, the changes will be effective in the September 1999 cycle for credit unions with assets greater than $50 million, and the December 1999 cycle for all other credit unions.

CUSO REPORTING

Three comments noted that the “new” requirement to report each CUSO investment/loan separately is unnecessary. Reporting each CUSO separately has been required since 1995. Two comments stated that consolidating CUSO financial data into the credit union’s financial data imposes an excessive burden, makes
comparison difficult, and may “pierce the corporate veil.” Consolidation of a CUSO’s financial statements into a credit union’s financial statements is required under GAAP if the credit union owns a controlling interest (whole or majority ownership). Therefore, such consolidation is required for Call Report purposes.

MISCELLANEOUS COMMENTS

Two comments noted that the terminology “direct financing leases” as used on the Statement of Financial Condition (page 1, line 17) may be confusing. We changed the wording to “Leases Receivable.”

One comment stated that the investment maturity breakdown included on Schedule C – Investments differs from the guidance provided in SFAS 115 (the Call Report uses a 3-year cutoff, while SFAS 115 uses a 5-year cutoff). The shorter periods used on the Call Report are used for evaluation of safety and soundness.

Two comments stated that the computation of insured shares included on page 2 of the Call Report is not consistent with the recent changes to Part 745 of NCUA’s Rules and Regulations regarding insured shares. NCUA staff will review this section for necessary changes when Part 745 is issued in final form.

One comment questioned whether the five new questions on Schedule E – Borrowings would remain on the form after the millennium date change. While these questions provide valuable information related to Y2K liquidity preparations, they also serve a long-term purpose. Section 204 of the Federal Credit Union Act (as amended by the Credit Union Membership Access Act), requires NCUA to assess the potential liquidity needs and options of each federally insured credit union as well as federally insured credit unions as a group. The new questions on Schedule E – Borrowings will assist us in meeting this requirement.

INSTRUCTIONS

Seventeen comments addressed changes to or clarification of instructions. The comments and suggestions are as follows:

☑ **Statement of Financial Condition (page 1):** One comment stated that the definition of “cash and cash equivalents” (line 1) is ambiguous. We received additional clarification from the American Institute of Certified Public Accountants (AICPA) for this definition. We revised the instructions to read: “Cash equivalents include short-term, highly liquid investments with original maturities of three months or less.”

☑ **Statement of Financial Condition (page 1):** One comment suggested that the number of credit card loans and lines of credit (line 11, account code 993)
should include only those loans with outstanding balances, not zero balance accounts. We clarified the instructions accordingly.

☑ Statement of Financial Condition (page 1): One comment stated that the instructions are not clear for “in-substance” foreclosures. “In-substance” foreclosures were previously reported as Other Real Estate Owned (OREO). The concept of “in-substance” foreclosures was essentially eliminated under GAAP with the implementation of Statement of Financial Accounting Standard No. 114. Under this GAAP standard, either physical possession or deed/title is required before the asset can be reported as an OREO. If this requirement is not met, then the asset should be recorded as a loan (likely delinquent).

☑ Loan Schedule: One comment suggested clarifying that credit card delinquency should be included in total delinquency (lines 1 through 4 on page 4). The instructions for total delinquency note that this section should include credit card delinquency; however, the term “credit card” is added to the heading above these lines for clarification.

☑ Loan Schedule: One comment requested clarification of which items should be reported “year-to-date.” Each “year-to-date” item is noted as such on both the form and the instructions.

☑ Miscellaneous Information: One comment suggested additional instruction for line 6 to clarify that the credit union’s e-mail address is requested, not an employee’s. We added this clarification to the instructions.

☑ Miscellaneous Information: One comment noted that the instructions for line 7 (website address) state that “http://www” should not be included as part of the response. However, some website addresses must include “www” to be correct. We agree with this observation, and corrected the instructions accordingly.

☑ Miscellaneous Information: One comment suggested additional instruction after line 7 to indicate that questions 8 through 10 should be skipped if no website address is reported in line 7. We added this clarification to the instructions.

☑ Miscellaneous Information: One comment requested more definitive instructions for calculating potential field of membership. The comment suggested using a standard formula rather than having the credit union make the determination, or removing the question from the Call Report. NCUA will review the instructions for further clarification.

☑ Schedule A – Real Estate Loans/Lines of Credit: One comment suggested that the number of home equity lines of credit (line 2c, account code 976)
should include only those loans with outstanding balances, not zero balance accounts. We clarified the instructions accordingly.

☑ **Schedule B – Member Business Loans:** One comment suggested that the instructions state that this supplemental schedule should be completed “only for member business loans greater than $50,000 outstanding.” A member business loan is defined by the original loan amount, not by the outstanding balance. We clarified the instructions accordingly.

☑ **Schedule B – Member Business Loans:** One comment suggested that, rather than referring to the regulation, the instruction should restate the definition of a member business loan. NCUA agrees that this addition is helpful, and added this to the instruction page.

☑ **Schedule E – Borrowings:** Two comments requested additional explanation of question 11, “Has your credit union purchased a committed line of credit with a corporate credit union, other credit union, or other financial institution?” Purchasing a committed line of credit means that the credit union paid a fee to guarantee access to the line of credit. A committed line of credit is not the same as a regular line of credit. We added clarifying instructions for this question.

☑ **Schedule F – Savings:** Two comments suggested clarifying that the maturity breakdown is by remaining maturity rather than original maturity by stating so on the form directly above the maturity grid. One comment noted that the instructions provided are adequate, but that many credit unions do not read the instructions. We added the instruction to the form page for clarification.

☑ **Instructions for Reporting Requirements (located just before page 1a):** One comment noted that the instructions for completing Schedule C list the NCUSIF deposit as an investment. We corrected this typographical error.

Several comments stated that while the instructions provided were adequate, many credit unions still have errors on the Call Report because they do not read the instructions. The suggested solution to this problem was to include the instructions on the form pages with the related line items rather than on separate pages. In some cases where space is available, this suggestion is implemented. However, most of the form pages do not have space available for the instructions. NCUA believes that a separate instruction page is appropriate in most circumstances. It is incumbent upon the credit union to read the instructions to ensure the Call Report is completed accurately.

Another miscellaneous change (although not part of a comment letter) is the renaming of the former “Investment Valuation Reserve” (account code 668, line 36
on page 2). This account, which applies only to state-chartered credit unions, records reserves set aside from Undivided Earnings to cover the excess of book value over fair value for investments not authorized by NCUA Rules and Regulations. With approval of the NCUA Board, the name was changed from “Investment Valuation Reserve” to “Appropriation for Non-Conforming Investments” to better reflect the true purpose of the account. This change was recommended by the AICPA.

SUGGESTED ADDITIONS

Nine comments included suggestions for the following items to be added to the Call Report:

- Income account for unconsolidated CUSO income;
- Expense accounts for “data processing” and “electronic services”;
- Accounts for guaranteed student loans and related delinquencies;
- Question of whether a bonus dividend was paid, and if so how much;
- Accounts for daily averages of loans, investments, assets, and shares;
- Account for non-real estate variable rate loans;
- Question of whether the credit union owns a controlling interest in a CUSO; and
- Separate accounts for IRA shares and IRA certificates (two comments suggested this).

Additionally, one comment suggested that separate categories for “new vehicle loans” and “used vehicle loans” are not necessary. Each of these suggestions will be evaluated and considered for future Call Reports.

We thank those who submitted comments for consideration. The September 1999 cycle Call Report materials will be issued in mid September.

Sincerely,

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Norman E. D’Amours
Chairman, NCUA Board

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