Chapter 205

ACCOUNTING AND FINANCIAL REPORTING

Introduction

The purpose of the accounting and financial reporting review is to determine the corporate has appropriate processes in place to identify, measure, monitor, report, and control risk from its accounting and financial reporting activities.

Key issues surrounding these areas include: staff expertise/training, the level of separation of duties and internal controls, timeliness, staff turnover/cross-training, adequacy of policies/procedures, and the integrity of the financial statements/reports.

An in-depth review of a corporate's accounting and financial reporting area will be the exception, rather than the rule during annual examinations. This is primarily due to two factors as follows:

1. Corporates are required to have Certified Public Accounting (CPA) opinion audits which typically have unqualified (except for the classification of member shares as equity) opinions; and
2. Corporates have internal audit functions to address on-going internal control and accountability deficiencies.

Corporates are required to maintain accurate accounting records and financial reports based on Section 704.4(c)(4) of the NCUA Rules and Regulations and sound business practices. Additionally, Section 704.4(c)(3) requires the board of directors of a corporate credit union to ensure Generally Accepted Accounting Principles (GAAP) are followed.

The following accounting and financial reporting areas will undergo the most review during an examination:

1. Accounting and financial reporting policies, procedures, practices, and internal controls;
2. Federal Reserve, U.S. Central FCU, and other cash account reconciliation processes;
3. Suspense account reconciliation process; and

4. 5310 reporting process.

A more extensive or expanded review of the accounting and financial reporting area may be appropriate depending upon the circumstances existing prior to and during each examination. To help determine if a more extensive review is appropriate, examiners will complete the Corporate Examination Questionnaire - Accounting and Financial Reporting - OCCU 205Q.

EICs have the flexibility to reduce or expand the accounting and financial reporting review as deemed necessary. However, if the examination scope is changed subsequent to receiving the CFS' approval, an EIC must justify why they plan to expand or reduce the scope and obtain CFS approval.

OCCU staff must be cognizant of situations that could be conducive to fraud and/or insider abuse. Examiners must determine adequate segregation of duties and internal controls are in place. Internal control weakness, poor documentation, improper internal audit relationships, inaccurate 5310s, un-reconciled accounts, and out-of-balance conditions are examples of significant accounting and financial reporting deficiencies most likely requiring corrective action. The degree and seriousness of these types of issues will help OCCU staff determine whether they are treated as a Document of Resolution (OCCU 102F) or Other Examiner's Findings (OCCU 102G).

OCCU staff should not attempt to reconcile out-of-balance conditions. These types of concerns should be brought to the attention of the CFS prior to being discussed with corporate officials. OCCU staff should determine why the condition exists, whether management has adequate expertise/resources to resolve the problem, what steps will be taken to resolve the problem, and when the problem will be resolved.

Cash and Federal Reserve Accounts

A corporate's cash and Federal Reserve Bank accounts are one of the most critical areas of the accounting and financial reporting review. It is imperative for OCCU staff to verify the Federal Reserve Bank account(s) are reconciled daily, adequate separation of duties exists, reconciling items are researched and cleared in a timely manner by corporate staff, and reconciliations are signed and dated by the reviewer and the preparer. To ensure this account is being properly reconciled, reconciliations as of the effective and current date must be reviewed. If the most current reconciliation has not been prepared for the last two business days, management must provide a reasonable explanation.

Examiners will perform a random sample review of the monthly cash account reconciliations, in addition to reviewing the reconciliations for the effective date of the examination. Related bank settlement and suspense accounts must also be closely reviewed. Reconciliation items should be traced to source documents along with any related correspondence, as deemed necessary.

Examiners must also perform a review of any overdrafts occurring with the Federal Reserve Bank during the examination period. If overdrafts have occurred, the examiner should ensure appropriate corrective action(s) has been taken by the corporate to minimize the likelihood of future overdrafts. Corrective actions vary but normally consist of policy and/or procedural changes, staff training, and/or increasing the minimum Federal Reserve Bank account balance.

Expenses

Normally, losses associated with the use of corporate credit cards and officials' expenses would not represent a significant risk to a corporate. However, if the examiner suspects or discovers abuses and/or expenses are excessive a review should be performed. When examining state chartered corporates, the EIC should coordinate the review of these areas with the SSA. EICs have the latitude to expand the review of the expense area as deemed necessary with the concurrence of the CFS.

Corporates involved in any type of shared expense arrangements with trade organizations or third parties will be reviewed for compliance with Section 704.16. Services, facilities, or equipment shared with any party must be supported by a written contract. Also, the contract must include the duties and responsibilities of each party specified, and the allocation of service fee/expenses must be fully supported and documented. Corporate staff should ensure it is not paying excessive fees by comparing fees charged to those of competitors in the marketplace. If OCCU staff perceives a problem, the CFS will be contacted prior to discussions with corporate management or the board. The consultation will help OCCU staff reach a supportable position regarding the extent of the problem, proper corrective action, and how it will be reported within the context of the examination report (Executive Summary, Document of Resolution, and/or Supplementary Facts).

Investments

Investment accounting is discussed in Chapter 201 of the Guide. The investment accounting review is normally performed by staff assigned to review the corporate's investment portfolio.

Future Dated ACH Transactions

For definition purposes, future-dated ACH transactions are debit and/or credit entry notices received by corporates from the Federal Reserve, which will post to a corporate's Fed account within a few days. The AICPA has concluded Generally Accepted Accounting Principles (GAAP) do not specifically address the accounting treatment of future-dated ACH transactions. In order to provide a consistent approach to reporting financial information within the corporate system, OCCU has instructed (Corporate Credit Union Guidance Letter No. 2007-04) all corporates to not record future-dated ACH transactions as assets and liabilities on financial statements for both regulatory and 5310 reporting purposes. Corporates, however, can report future-dated ACH transactions on their other external and internal financial statements based on the advice of their CPAs.

During regular supervision and examinations of corporates, it should be determined future-dated ACH transactions are reported as indicated above. A corporate, which incorrectly reports these transactions, may misstate their capital, NEV, and/or other financial ratios.

Examination Objectives

The objectives of the accounting and financial reporting review are to:

1. Determine policies, procedures, and internal controls for safeguarding assets, liabilities, and equity are adequate;

2. Determine corporate personnel operate in conformance with established policies, procedures, and internal controls;

3. Verify selected asset and liability account balances to ensure they are valid and are properly recorded;

4. Ensure cash and Federal Reserve Bank accounts are accurately reconciled in a timely fashion and reconciling items are researched and cleared in a timely manner;

5. Determine whether financial statements/reports generated by corporate staff are materially accurate;

6. Determine if the corporate complies with the FCU Act, NCUA Rules and Regulations, the Accounting Manual For Federal Credit Unions, and Generally Accepted Accounting Principles; and

7. Initiate corrective actions when material deficiencies or violations of policies, procedures, or internal controls are detected.

Examination Procedures

See Corporate Examination Procedures - Accounting and Financial Reporting (OCCU 205P).

Examination Questionnaire

See Corporate Examination Questionnaire - Accounting and Financial Reporting (OCCU205Q).

References

1. Federal Credit Union Act (Section 1756);

2. NCUA Rules and Regulations (Sections 704.3, 704.4, 704.15, and 704.16);

3. Accounting Manual for Federal Credit Unions;

4. NCUA Fraud Hotline - 1-800-827-9650 (703-518-6550 Washington, DC area);

5. Corporate Credit Union Guidance Letter No. 2007-04 Accounting for Future Dated Automated Clearing House (ACH) Transactions; and

6. Generally Accepted Accounting Principles.