FEDERAL RESERVE BANK
OF NEW YORK

AT-10759

January 6, 1995

FINANCIAL ACCOUNTING STANDARDS

--Accounting by Creditors for Impairment of a Loan (FAS 114)

--Accounting for Income Taxes (FAS 109)

To All Depository Institutions in the Second
Federal Reserve District:

Printed on the following pages is the text of a statement issued by the Federal Financial Institutions Examination Council (FFIEC) through its Task Force on Supervision dealing with (1) the reporting of allowances for loan losses (FASB Statement No. 114), and (2) the amount of deferred tax assets that can be used to meet capital requirements (FASB Statement No. 109). Concerning the latter, the Board of Governors of the Federal Reserve System has issued final amendments to its capital adequacy guidelines for State member banks and bank holding companies to establish limitations, as recommended by the FFIEC, on the amount of certain deferred tax assets that may be included in Tier 1 capital; those amendments will be mailed to you shortly.

Questions regarding either of these matters may be directed to Stephanie Martin, Senior Financial Specialist, Bank Analysis Department (Tel. No. 212-720-1418).

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Press Release

The Task Force on Supervision of the Federal Financial Institutions Examination Council (FFIEC)[1] announced today its decision regarding the regulatory reporting treatment of allowances established under Financial Accounting Standards Board (FASB) Statement No. 114, "Accounting by Creditors for Impairment of a Loan" (FAS 114), and its recommendation to the agencies pertaining to regulatory capital issues arising from FASB Statement No. 109, "Accounting for Income Taxes" (FAS 109). The Task Force's actions were taken under delegated authority.

<u>FAS 114</u>

The Task Force on Supervision has decided that the portion of an institution's allowance established pursuant to FAS 114 should be reported as part of the general allowance, which is

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[1] The FFIEC consists of representatives from the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS) (referred to as the "agencies"), and the National Credit Union Administration. The Task Force on Supervision is comprised of staff members from each of the agencies. The actions discussed in this press release are not directed to credit unions.

includable in Tier 2 capital subject to a limit of 1.25 percent of gross risk-weighted assets. In concluding that the FAS 114 allowance is general in nature, the Task Force notes that all amounts identified as losses (i.e., loss classifications) are excluded from the general allowance.

The Task Force has also reaffirmed existing supervisory policies that require banks to promptly charge-off identified losses and require savings associations to promptly charge-off or use specific allowances (which are reported separately from general allowances) for identified losses. With respect to impaired collateral-dependent loans, the agencies generally classify as loss any portion of the loan balance that exceeds the amount that is adequately secured by the fair value of the collateral; such losses on collateral-dependent loans will not be included in the general allowance or Tier 2 capital. Also, as previously announced, the FFIEC has decided to maintain its existing regulatory nonaccrual policies for problem loans.

<u>FAS 109</u>

The Task Force on Supervision is recommending to the agencies that they finalize their proposed amendments to regulatory capital standards to limit the amount of deferred tax assets reported pursuant to FAS 109 that can be used to meet capital requirements. As previously proposed, the Task Force recommends that, to the extent the realization of deferred tax assets is dependent on an institution's future taxable income, such deferred tax assets be limited for regulatory capital purposes to the amount that the institution expects to realize within one year of the quarter-end report date, or ten percent of Tier 1 capital, whichever is less. Under the Task Force's recommendation, deferred tax assets that can be realized from taxes paid in prior carryback years and from future reversals of existing taxable temporary differences would generally not be limited.

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