

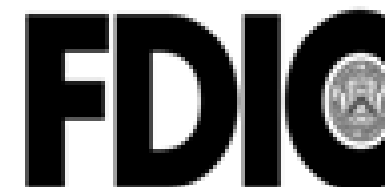


# The Effective Bank Director

## May 11, 2010

Sioux Falls Convention Center

FDIC Regulatory Panel  
Discussions





# FDIC Presenters

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# Kansas City Region 4<sup>th</sup> Quarter 2009

Ratio (Median)	KC Region			Nation		
	12/31/09	12/31/08	% Change	12/31/09	12/31/08	% Change
<b>Tier 1 Leverage</b>	9.28	9.28	0.00	9.32	9.40	(.85)
<b>Past Due and NA</b>	2.55	2.41	5.81	3.36	2.75	22.18
<b>NIM</b>	3.88	3.90	(.51)	3.73	3.77	(1.06)
<b>Provisions / Avg Assets</b>	.37	.22	68.18	.46	.28	64.29
<b>ALLL / Total Loans</b>	1.45	1.30	11.54	1.43	1.25	14.40
<b>ALLL / Noncurrent Lns</b>	.98X	1.06X	(7.55)	.73X	.89X	(17.98)
<b>ROAA</b>	.71	.85	(16.47)	.47	.60	(21.67)
<b>Non-Core Funding / TA</b>	19.47	20.36	(4.37)	23.73	25.20	(5.83)
<b>Brok Deps / Assets*</b>	3.56	3.84	(7.29)	5.14	6.10	(15.74)

# Kansas City Region

## 4<sup>th</sup> Quarter 2009

Ratio (Median)	South Dakota		
	12/31/09	12/31/08	% Change
<b>Tier 1 Leverage</b>	9.99	10.14	(1.48)
<b>Past Due and NA</b>	2.14	1.77	20.90
<b>NIM</b>	4.18	4.18	0.00
<b>Provisions / Avg Assets</b>	.38	.14	171.43
<b>ALLL / Total Loans</b>	1.45	1.26	15.08
<b>ALLL / Noncurrent Lns</b>	1.13X	1.58X	(28.48)
<b>ROAA</b>	.75	1.01	(25.75)
<b>Non-Core Funding / TA</b>	20.30	20.57	(1.31)
<b>Brok Deps / Assets*</b>	5.61	3.99	40.60



# Emerging Supervision Issues



# Accounting Hot Topics

- Accounting for Loan Participations Under ASC 860 (FAS 166)
- Allowance for Loan and Lease Losses
- Troubled Debt Restructuring
  - Other Real Estate Sales
- Acquisition of Failed Banks-Business Combination Accounting



# Loan Participations

## ■ Example 1

- On 7/1/09, Bank A originates a \$500,000 loan and also enters into a LIFO participation agreement with Bank B for 25% of the loan balance, which it transfers to Bank B in a transaction that qualifies as a sale under FAS 140
- On 3/1/10, Bank A transfers a 20% interest in its share of the loan to Bank C
  - This transfer does not affect the accounting for the LIFO participation transferred to Bank B on 7/1/09 because the transfer to Bank B predated the effective date of FAS 166
  - The transfer to Bank C cannot be accounted for as a sale because Bank A's interests in the entire financial asset (the \$500,000 loan) held initially and subsequently does not meet the definition of a participating interest



# Loan Participations

## ■ Example 2

- As of 12/31/09, Bank D has an outstanding construction loan commitment for \$500,000 under which \$400,000 has been advanced. Because Bank D's legal lending limit is \$400,000, it entered into a LIFO loan participation agreement with Bank E when commitment was originated in 2009. Bank E will fund the final \$100,000 in advances.
- On 2/1/10, borrower requests a \$50,000 advance, which in effect Bank E fully funds
  - The transfer of the \$50,000 advance would mean that neither Bank D's nor Bank E's interest in the construction loan meets the definition of a participating interest
  - The transfer of the \$50,000 participation should be reported as a secured borrowing



# Loan Participations

## ■ Example 3

- On 2/15/10, Bank F has a legal lending limit of \$100,000 and enters into two loan agreements with a borrower
- The first agreement is for \$80,000 and requires quarterly principal payments of \$20,000 beginning in three months, which it transfers to Bank G
- The second agreement is for \$100,000 and also requires quarterly principal payments of \$20,000, but the first payment is due in 15 months, which Bank F retains
- Both loans have 4% interest rate payable quarterly



# Loan Participations

- Example 3 (cont'd)

- In evaluating a transfer, FAS 166 requires consideration of all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer
  - Considering the two loans together as an entire financial asset, cash flows received are not divided proportionately and therefore the two loans do not meet the definition of a participating interest
  - The transfer of the \$80,000 loan should be reported as a secured borrowing



# Loan Participations

- Example 4

- On 1/15/08, Bank H originates a \$1,000,000 loan and also enters into a LIFO participation agreement with Bank J for 20% of the loan balance, which it transfers to Bank J in a transaction that qualifies as a sale under FAS 140
- The loan matures on 1/15/10 and Banks H and J agree to extend the loan and make other changes to the loan agreement
- How do the extension and the other changes affect the accounting for the participation transferred to Bank J?
  - Depends on whether the extended loan is treated as a new loan or a continuation of the old loan



# Loan Participations

## ■ Example 4 (cont'd)

- “If the terms of the new loan resulting from a loan refinancing or restructuring other than a troubled debt restructuring are at least as favorable to the lender as the terms for comparable loans to other customers with similar collection risks who are not refinancing or restructuring a loan with the lender, the refinanced loan shall be accounted for as a new loan. This condition would be met if the new loan's effective yield is at least equal to the effective yield for such loans.” (FAS 91, paragraph 12; ASC 310-20-35-9)
- If the extended loan is a new loan and the participation remains a LIFO participation, the participation would not meet the definition of a participating interest and it should be reported as a secured borrowing
- If the extended loan is a continuation of the old loan, there is no new transfer to evaluate




# Accounting Topics on the Horizon

- Financial Instruments Project
  - Fair Value Loans
- International Accounting Standards (IFRS)



# Emerging Compliance Issues



## Credit Card Act (Truth in Lending)

- Effective August 20, 2009
  - New mail requirements for periodic statements
  - Advance notice for APR increase or change in terms
- Effective February 22, 2010
  - Prohibition on rate increases during the first year and existing balances
  - Age restrictions
  - Limits on fees and promotional rates
  - Prohibition of two-cycle billing
  - Rules for payments application and due dates
  - New disclosure requirements
- Effective August 22, 2010
  - Look back review for rate increases



# Truth in Lending - Regulation Z

- Effective October 1, 2009
  - Higher-priced loans
    - Determine and document a borrower's ability to repay
    - Limit on prepayment penalties
    - Establish an escrow account
  - Change in standard early disclosure requirement
  
- Effective July 1, 2010
  - Application and solicitations format and content
  - New account disclosures
  - Revisions to periodic statement disclosures
  - New requirements for advertising
  - Reasonable cut-off hours
  - Changes to payment crediting



## Home Mortgage Disclosure (HMDA) - Regulation C

- Effective October 1, 2009
  - Calculation of rate spread changing to conform to Regulation Z's definition of higher-priced mortgage loans

## Truth in Savings - Regulation DD

- Effective January 1, 2010
  - Disclosure of Aggregate Overdraft Fees on Periodic Statements
  - Disclosure of Balance Information on Automated Systems



## Real Estate Settlement Procedures (RESPA) - Regulation X

- Effective January 1, 2010
  - New Application Process
  - New GFE
  - Revised GFE When Changes Occur
  - New HUD-1 and HUD-1A

## Higher Education Opportunity Act of 2008

- Effective February 14, 2010
  - Specific application, approval, and final disclosures for private education loans



## Expedited Funds Availability - Regulation CC

- Effective February 27, 2010
  - Only one single check-processing region

## Electronic Fund Transfers - Regulation E

- Effective July 1, 2010
  - New requirements for overdrafts created by ATM and one time debit card transactions
  - Debit card holds

## Gift Cards

- Effective August 22, 2010
  - Limits on expiration dates and fees
  - New rules for replacement cards
  - All fees must be clearly disclosed





# Top 10 Compliance Issues in South Dakota Banks

Time Period:

January 1, 2007 – April 22, 2010

65 examinations – 56 with Significant Violations

- 
- **Electronic Fund Transfers – Regulation E – 14%**
    - CV – Resolution of Disputes
    - BG – Overdrafts of Reg E Activity
  
  - **Fair Credit Reporting/FACTA – 14%**
    - CV – Notice to Home Loan Applicant
    - BG – Proper Disclosures when Sharing Information
  
  - **Non-deposit Products/NDIP – 18%**
    - CV – Insurance Disclosure not Provided
    - BG – Proper Disclosures of Risks

- 
- Truth in Savings – Regulation DD – 38%
    - CV – Clear and Conspicuous Disclosures
    - BG – Proper Disclosures of Fees and APY
  
  - Truth in Lending – Regulation Z – 34%
    - CV – Early Reg Z disclosures for RE
    - BG – APR, Finance Charge, and Reg Changes
  
  - RESPA – 39%
    - CV – Completion of GFE and HUD-1
    - BG – Section 8 Kickbacks and Escrow Accounts




- Home Mortgage Disclosure Act – HMDA – 20%

- CV – Improper Completion of LAR
- BG – Same as above + CMPs

- Flood Insurance – 41%

- CV – Completion of SFHDF
- BG – Correct Amount of Insurance in Timely Manner + CMPs

- 
- Unfair or Deceptive Acts or Practices – 14%
    - CV – Section 5 of FTC Act
    - BG – Same as above + CMPs and Restitution
  
  - Equal Credit Opportunity – Regulation B – 38%
    - CV – Monitoring Information
    - BG – Discrimination + DOJ + Press + ?



# CRA Concerns

- Reinvesting in Community
- Public Evaluation and Illegal Credit Practices
- Ability to branch, merge, purchase failing banks, etc.



# What Can You Do?

- Compliance Management System – CMS
- Board and Senior Management Oversight
- Compliance Program –  
Policies/Training/Monitoring
- Audit Program



# Resources

- Statement on Prudent Commercial Real Estate Loan Workouts

- <http://www.fdic.gov/news/news/financial/2009/fil09061.html>

- Accounting Updates each Quarter

- <http://www.fdic.gov/news/news/financial/2010/fil10011b.pdf>



# Resources

- Credit Card Final Rule  
<http://www.federalreserve.gov/newsevents/press/bcreg/20100112a.htm> FIL-134-2008 Regulation Z and Regulation C Amendments to the Regulation  
<http://www.fdic.gov/news/news/financial/2008/fil08134.html>
- FIL-26-2009 Regulation Z Early Disclosure Requirements  
<http://www.fdic.gov/news/news/financial/2009/fil09026.html>
- New Overdraft Rules for ATM and Debit Cards  
<http://www.federalreserve.gov/newsevents/press/bcreg/20100219a.htm>
- Final RESPA Rule  
<http://www.hud.gov/offices/hsg/sfh/res/finalrule.pdf>
- Higher Education Opportunity Act  
<http://www.federalreserve.gov/newsevents/press/bcreg/20090730a.htm>
- Reg CC – Notice of Change in Districts  
<http://www.federalreserve.gov/newsevents/press/bcreg/20091231a.htm>
- Extension of Transaction Account Guarantee Program  
<http://www.fdic.gov/news/board/April03.pdf>
- Final Gift Card Rule  
<http://www.federalreserve.gov/newsevents/press/bcreg/20100323a.htm>