

RESCINDED
BANKING ISSUANCES

Comptroller of the Currency
Administrator of National Banks

EB 93-1 has been replaced by BB 93-45

Type: Examining Bulletin

Subject: FDICIA Section 112 Annual
Independent Audits and Reporting
Requirements

TO: Deputy Comptrollers, District Administrators, Department
and Division Heads, and all Examining Personnel

Section 112 of the Federal Deposit Insurance Corporation Improvement Act of 1991 established new audit, reporting, and audit committee requirements for insured depository institutions with assets in excess of \$150 million. These new requirements are effective for fiscal years beginning after December 31, 1992.

On September 15, 1992, the Federal Deposit Insurance Corporation (FDIC) published for comment a proposed regulation to implement these provisions. The comment period closed on October 30, 1992 and the FDIC received over 300 comment letters responding to the proposed regulation.

The FDIC is working to resolve the numerous issues that were raised in the comment letters and expects to issue a final rule in the first quarter of 1993. In order to provide interim guidance until the final rule is issued, the FDIC issued the attached letter to all insured depository institutions with assets of \$125 million or more.

If you have any questions regarding this information, please contact the Chief National Bank Examiner's Office (202) 874-5180.

Donald G. Coonley
Chief National Bank Examiner

Attachment

FIL 94-92
December 28, 1992

OUTSIDE AUDITS

TO: CHIEF EXECUTIVE OFFICER

SUBJECT: Interim Guidance Concerning Annual
Audits, New Reporting Requirements

In September, the FDIC issued for public comment proposed Part 363 that would implement Section 112 of the FDIC Improvement Act of 1991 (FIL-67-92, dated September 21, 1992). That section of the law (also designated Section 36 of the Federal Deposit Insurance Act) generally requires insured depository institutions over a certain size to file audited financial statements and other specified information, and to establish and maintain independent audit committees. Although Section 36 becomes effective for fiscal years beginning after December 31, 1992, the FDIC will not be adopting final regulations until early 1993 in order to have time to resolve numerous complex and technical issues raised by the more than 300 letters responding to the proposed regulations.

At a meeting of the FDIC Board of Directors on December 15, 1992, FDIC staff presented their views on a number of pending issues. Those views were intended to provide interim guidance to institutions pending adoption of final regulations and to assist institutions in otherwise preparing for the final rules. The following is a summary of those views, which are those of staff, are subject to change, and are not necessarily those that the Board will adopt in early 1993.

Interim guidance on compliance prior to the adoption of final regulations:

- Audit Committee Independence: The new law mandates that an institution establish or restructure its audit committee to be independent of the institution's management. Because final independence standards have not yet been determined, staff is likely to recommend a phase-in period for compliance with these provisions. Institutions that do establish or restructure audit committees prior to the adoption of a final rule should do so in accordance with the mandate of Section 36 that such committees be independent of the institution's management.
- Holding Company Subsidiaries: A holding company subsidiary that reports under Part 363 using the consolidated financial statements and other reports of the holding company is not required to have its own separate audit committee. The subsidiary may rely on the holding company's audit committee so long as: (1) the holding company's audit committee members meet the independence requirements in Section 36 and (2) the subsidiary institution's total assets at the beginning of the fiscal year did not exceed \$5 billion or, if the subsidiary had between \$5 billion and \$9 billion in total assets at that time, it is in sound financial condition as indicated by a CAMEL composite or MACRO rating of 1 or 2 on the interagency rating system.

- Independent Public Accountant: Even without final rules, the law makes effective January 1, 1993, a requirement that an institution provide written notification to the appropriate FDIC Regional Director and any other appropriate federal and state banking agency of the hiring of a new independent public accountant within 15 days of the engagement. In addition, each institution is required to provide its independent public accountant with a copy of its most recent report of examination and all other reports required by Section 36(h).

Other staff views expressed at the December 15 Board meeting:

- Applicability: Under the September proposal, the initial applicability of Part 363 would cover institutions with total assets of \$150 million or more. In addition, "large institutions" (total assets of \$500 million or more) would be subject to more stringent audit committee requirements. FDIC staff is considering recommending that one or both of these thresholds be raised or some type of tiering be established such that the requirement for a traditional audit may be set at one level and the newer requirements at a higher level.
- Audit Period: Staff is considering proposing that internal controls be evaluated as of a point-in-time (i.e., as of the end of the institution's most recent fiscal year), rather than over the full audit period (i.e., the year).
- Large Customer: Section 36 precludes a "large customer" of a "large institution" from serving on its audit committee. The September proposal would define a large customer based on the customer's business as a percentage of capital or \$50 million. Staff is considering whether a better test exists than the percent of capital and expects to recommend the deletion of the \$50 million standard. Staff also expects to recommend that no prohibition be placed on service by an outside director of a large corporate customer.
- Internal Controls: Under Section 36, management must report on the effectiveness of "internal controls over financial reporting" and the independent public accountant must attest to management's assertions on such internal controls. However, the FDIC finds "internal controls over financial reporting" difficult to define. Staff is likely to propose that such controls include the safeguarding of assets as that term relates to reviewing loan files to assure that loans are properly documented and in accordance with the institution's policies.

For further information about this interim guidance, please contact Doris L. Marsh, Examination Specialist, in the Division of Supervision at (202) 898-8905, or Sandra Comenetz, Senior Attorney, in the Legal Division at (202) 898-3582.

Paul G. Fritts
Executive Director

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