Accounting News: Recent Developments Affecting the Accounting for Split-Dollar Life Insurance Arrangements

In recent years, an increasing number of banks have acquired life insurance assets to finance the cost of employee benefits, protect against the loss of key persons, or provide retirement and death benefits as part of certain employees' compensation. Data reported in the Consolidated Reports of Condition and Income (Call Report) reveal that more than 47 percent of all banks held life insurance assets as of December 31, 2006. For these banks, their total life insurance assets exceeded $96 billion, which represented more than 11 percent of their aggregate equity capital.

Banks often use split-dollar life insurance arrangements to provide retirement and death benefits to employees. These arrangements are commonly structured as either "endorsement" split-dollar arrangements or "collateral assignment" split-dollar arrangements. Although both types of split-dollar life insurance arrangements have existed for many years, within the past year the Financial Accounting Standards Board (FASB) has ratified separate consensuses reached by its Emerging Issues Task Force (EITF) on the accounting for these two types of arrangements. The consensuses in EITF Issues No. 06-4 and No. 06-10 cover endorsement and collateral assignment split-dollar life insurance arrangements, respectively.[1] The EITF addressed the accounting issues associated with these arrangements because of diversity in practice with respect to the deferred compensation and postretirement benefit aspects of typical split-dollar arrangements. As a consequence, institutions that have entered into split-dollar arrangements with employees now need to review how they account for them. For many banks, the application of the EITF consensuses will result in a change in accounting principles that will require them to recognize a liability at the beginning of 2008 for any benefits provided to these employees that extend to postretirement periods.

Split-Dollar Life Insurance Arrangements

The December 2004 Interagency Statement on the Purchase and Risk Management of Life Insurance,[2] which provides guidance regarding supervisory expectations for the acquisition and holding of life insurance by banks and savings associations, also addresses split-dollar life insurance arrangements. As noted in the Interagency Statement, under split-dollar arrangements, the employer and the employee share the rights to the insurance policy's cash surrender value (CSV) and death benefits. In general, the difference between endorsement and collateral assignment split-dollar life insurance arrangements is in the ownership and control of the life insurance policy. In an endorsement arrangement, the employer (bank) owns the insurance policy and controls all rights of ownership; in a collateral assignment arrangement, the employee owns the policy and controls all rights of ownership.

According to the EITF's description of a typical endorsement split-dollar arrangement,

> An employer purchases a life insurance policy to insure the life of an

[1] See EITF Issue No. 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements* (EITF 06-4), and EITF Issue No. 06-10, *Accounting for Collateral Assignment Split-Dollar Life Insurance Arrangements* (EITF 06-10). The FASB ratified the EITF's consensuses on these issues on September 20, 2006, and March 28, 2007, respectively.

[2] FIL 127-2004, Bank-Owned Life Insurance: Interagency Statement on the Purchase and Risk Management of Life Insurance, December 7, 2004, www.fdic.gov/news/news/financial/2004/fil12704.html.

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> employee and pays a single premium at inception of the policy. Based on the insurance carrier's experience (for example, mortality) it can either charge or credit the policyholder for the negative or positive experience, respectively. The additional premium or credit is typically effectuated through an adjustment to the cash surrender value of the policy. The employer enters into a separate agreement that splits the policy benefits between the employer and the employee….To effect the split-dollar arrangement, the employer endorses a portion of the death benefits to the employee (the employee designates a beneficiary for this portion of the death benefits). Upon the death of the employee, the employee's beneficiary typically receives the designated portion of the death benefits directly from the insurance company and the employer receives the remainder of the death benefits.[3]

In contrast, as described in the EITF's materials, a typical collateral assignment split-dollar arrangement has the following characteristics:

> An employee purchases a life insurance policy through an arrangement with the employer to insure the employee's life…[or] the employer purchases a life insurance policy and transfers ownership of the insurance policy to the employee…The employer usually pays all or a substantial part of the premium. The employee irrevocably assigns a portion or all of the death benefits to the employer as collateral for the employer's interest in the insurance policy [i.e., the employer's loan to the employee] (the collateral assignment arrangement). Amounts due to the employer vary but, typically, the employer is entitled to receive a portion of the death benefits equal to the premiums paid by the employer or premiums paid plus an additional fixed or variable return on those premiums.[4]

The appendix to the 2004 Interagency Statement contains similar descriptions of these two split-dollar arrangements. The Interagency Statement further provides that an institution's economic interest in the insurance policy underlying the split-dollar arrangement should at least be equal to the premium or premiums paid plus a rate of return comparable to returns on investments of similar maturity and credit risk.

Liability Recognition for Split-Dollar Arrangements under the EITF Consensuses

The EITF reached similar conclusions as to whether an employer should recognize a liability and related compensation costs for postretirement benefits associated with both endorsement and collateral assignment split-dollar life insurance arrangements. For both types of split-dollar arrangements, determining whether the employer should recognize a liability for postretirement benefits should be based on the substantive agreement with the employee. Thus, "if the employer has agreed to maintain a life insurance policy during the employee's retirement or provide the employee with a death benefit,"[5] the employer should recognize a liability for its postretirement benefit obligation to the employee. The liability must be recognized in accordance with FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions (FAS 106),* "if, in

[3] *EITF Abstracts,* Issue No. 06-4, paragraph 2.

[4] EITF 06-10, Issue Summary No. 1, paragraph 2.

[5] Unless otherwise noted, this quotation and subsequent quotations are taken from the *EITF Abstracts* for Issue No. 06-4 or Issue No. 06–10.

substance, a postretirement benefit plan exists," or Accounting Principles Board Opinion No. 12, *Omnibus Opinion—1967* (APB 12), "if the arrangement is, in substance, an individual deferred compensation contract." To determine the substance of an arrangement, all available evidence should be considered, including the "explicit written terms of the arrangement, communications made by the employer to the employee, the employer's past practices in administering the same or similar arrangements, and whether the employer is the primary obligor for the postretirement benefit."

Furthermore, when evaluating a collateral assignment split-dollar arrangement, an employer would be deemed to have agreed to maintain a life insurance policy "if the employer has a stated or implied commitment to provide loans to an employee to fund premium payments on the underlying insurance policy during the postretirement period." In the absence of evidence to the contrary, there is a presumption that an employer will "provide loans to an employee to fund premium payments on the underlying insurance policy in the postretirement period if the employer has provided loans in the past or if the employer is currently promising to provide loans in the future." For example, if, under the terms of the collateral assignment arrangement, the employer has either a stated or implied obligation "to provide loans to an employee to cover the experience gains and losses of the insurance company, that may indicate that the employer has a postretirement benefit obligation" to be recognized.

Therefore, after considering all available evidence surrounding a split-dollar arrangement, if the substance of the arrangement is the employer's agreement to maintain a life insurance policy on the employee during his or her retirement, "the estimated cost of maintaining the insurance policy during the postretirement period should be accrued." Similarly, if the substance of the arrangement is the employer's agreement "to provide the employee with a death benefit, the employer should accrue, over the service period, a liability for the actuarial present value of the future death benefit as of the employee's expected retirement date." These accruals should be made in accordance with FAS 106 or APB 12, as appropriate.

APB 12 requires that

> an employer's obligation under a deferred compensation agreement be accrued according to the terms of the individual contract over the required service period to the date the employee is fully eligible to receive the benefits, i.e., the "full eligibility date."...[It] does not prescribe a specific accrual method for the benefits under deferred compensation contracts, stating only that the "cost of those benefits shall be accrued over that period of the employee's service in a systematic and rational manner." The amounts to be accrued each period should result in a deferred compensation liability at the full eligibility date that equals the then present value of the estimated benefit payments to be made under the individual contract.[6]

FAS 106 also directs an employer to "recognize and measure the obligation for postretirement benefits based on the actuarial present value of all future benefits attributed to an employee's service rendered to that date [i.e., to the full

[6] *Instructions for the Preparation of Consolidated Reports of Condition and Income,* Glossary, "Deferred Compensation Agreements," page A-15 (3-04). Further guidance on accounting for deferred compensation agreements, including examples, is provided in the Interagency Advisory on Accounting for Deferred Compensation Agreements and Bank-owned Life Insurance. See FIL-16-2004, Accounting and Reporting, February 11, 2004, www.fdic.gov/news/news/financial/2004/fil1604.html.

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eligibility date]. FAS 106 requires an employer to attribute the costs of those postretirement benefits over the required service period."[7]

The EITF noted that the facts and circumstances relating to a collateral assignment split-dollar arrangement may change in periods after the inception of the arrangement, for example, as a result of an amendment to the arrangement or a change from the employer's past practice in administering these arrangements. Therefore, an employer should periodically evaluate the substance of its collateral assignment arrangements to determine whether any change in an arrangement has altered its substance and, hence, whether a liability for a postretirement benefit obligation should be recognized or a previously recognized liability should be adjusted.

Asset Recognition for Split-Dollar Arrangements under the EITF Consensuses

An employer must also ensure that it properly recognizes the asset resulting from its split-dollar arrangements with employees. Because the owner of the insurance policy differs under the two types of split-dollar arrangements, the resulting asset held by the employer must reflect the nature of the employer's interest in the life insurance.

In an endorsement split-dollar arrangement, the employer owns the insurance policy. Thus, the accounting guidance in the FASB's Technical Bulletin 85-4, *Accounting for Purchases of Life Insurance* (TB 85-4), as interpreted by the EITF in Issue No. 06-5, *Accounting for Purchases of Life Insurance—Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin* 85-4 (EITF 06-5), should be applied to the insurance policy. Under TB 85-4, "the amount that could be realized under the insurance contract as of the date of the statement of financial position should be reported as an asset." Normally, this amount is the CSV of a policy, less any applicable surrender charges not reflected by the insurance carrier in the reported CSV. However, EITF 06-5 explains that the employer, as policyholder, should also consider any additional amounts included in the contractual terms of the policy in determining the amount that could be realized under the insurance contract.

In this regard, EITF 06-5 notes that an insurance policy's contractual terms may include a "claims stabilization reserve" account and a provision that allows the policyholder to recover the upfront "deferred acquisition costs" (DAC) tax over a specified period of time.[8] When either of these amounts is present in an insurance policy used in an endorsement split-dollar arrangement and the amount is realizable based on the policy's contractual terms, this realizable amount should be included as part of the amount reported as a life insurance asset on the balance sheet. Thus, as long as the split-dollar arrangement entitles the employer to the entire CSV reported by the insurance carrier (less any applicable surrender charges not reflected therein) plus any additional realizable amounts, the employer should report this total amount as an asset.

In contrast, because the employee owns the life insurance policy in a collateral assignment split-dollar

[7] EITF 06-4, Issue Summary No. 1, Supplement No. 2, Revised, page 20.

[8] Under EITF 06-5, when measuring the amount that could be realized under an insurance contract, "amounts that are recoverable by the policyholder in periods beyond one year from the surrender of the policy [such as the DAC tax] should be discounted in accordance with" Accounting Principles Board Opinion No. 21, *Interest on Receivables and Payables* (APB 21).

arrangement, an employer's process for recognizing and measuring the asset in such an arrangement is not as straightforward. According to EITF 06-10, this process should be "based on the nature and substance" of the arrangement, which requires the employer to "evaluate all available information." To determine the nature and substance, "the employer should assess what future cash flows the employer is entitled to, if any, as well as the employee's obligation and ability to repay the employer." As an example, the EITF cited a collateral assignment split-dollar arrangement in which the employer is entitled to recover only the CSV of the employee's insurance policy even if the employer's loan to the employee is a larger amount. Under such an arrangement, the employer's asset as of any balance sheet date would be limited to the CSV. As a second example, if the employee is required "to repay the [loan from the] employer irrespective of the collateral assigned and the employer (a) has determined that the employee loan is collectible and (b) intends to seek recovery beyond the cash surrender value of the life insurance policy, the employer should recognize the value of the loan (including accrued interest, if applicable) considering the guidance in" APB 21.

Under APB 21, if the employer's loan to the employee requires repayment only of the premiums paid by the employer on the insurance policy, i.e., without the payment of interest or a rate of return on those premiums, the employer should "record a receivable from the employee at a discounted amount for the premiums paid."[9] Thus, the employer would need to determine the expected repayment date of the loan to the employee based on the terms of the split-dollar life insurance arrangement as well as the appropriate interest rate at which to discount the loan. APB 21 states that "the rate used for valuation purposes will normally be at least equal to the rate at which the debtor [i.e., the employee] can obtain financing of a similar nature from other sources at the date of the transaction. The objective is to approximate the rate which would have resulted if an independent borrower and an independent lender had negotiated a similar transaction under comparable terms and conditions." The employer would apply the interest method to amortize the resulting discount on the loan to the employee over the life of the loan at the rate used for valuation purposes.

Effective Date for the EITF Consensuses

The consensuses reached on EITF 06-4 and EITF 06-10 are expected to represent a significant change in accounting practice for many banks with split-dollar life insurance arrangements. As a result, the EITF delayed the effective date of these consensuses to allow adequate time for implementation. Thus, both consensuses take effect for fiscal years beginning after December 15, 2007, i.e., as of January 1, 2008, for banks with calendar year fiscal years. Calendar year banks with split-dollar life insurance arrangements must first report in accordance with these consensuses in their March 31, 2008, Call Reports and in any first quarter 2008 financial statements they issue. Earlier application of the consensuses is also permitted.

When the EITF initially reached a tentative consensus in EITF 06-4 in June 2006, it proposed that the consensus should take effect for fiscal years beginning after December 15, 2006. For calendar year banks, this meant that they would have had to apply this consensus at the beginning of 2007. In considering comments received on its

[9] EITF 06-10, Issue Summary No. 1, paragraph A2.

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tentative consensus on EITF 06-4 that requested a delay in the effective date, the EITF recognized that, absent any changes to banks' existing endorsement split-dollar arrangements, many banks with such arrangements would see a reduction in their Tier 1 capital upon their initial application of the consensus. This regulatory capital reduction would be the consequence of having to recognize a liability for postretirement benefits that these banks had not previously accrued on their balance sheets. Accordingly, the EITF reconsidered the effective date and moved it one year into the future. When the EITF subsequently reached its consensus on EITF 06-10 for collateral assignment split-dollar arrangements, it decided in the interest of consistency to set the same delayed effective date as for EITF 06-4.

For a bank whose split-dollar life insurance accounting practices differ from the consensuses reached by the EITF, the effects of applying the relevant consensus for the type of split-dollar arrangement into which the bank has entered with its employees should be recognized "through either (a) a change in accounting principle through a cumulative-effect adjustment to retained earnings…as of the beginning of the year of adoption or (b) a change in accounting principle through retrospective application to all prior periods." Because each Report of Income in a bank's Call Report covers a single discrete calendar year-to-date period rather than presenting comparative statements, a bank is not permitted to implement a change in accounting principle through retrospective application to prior years' Call Reports. Therefore, unless a calendar year bank elects earlier application of the relevant split-dollar EITF consensus, it will report the cumulative effect of applying the consensus as of January 1, 2008, as a direct adjustment to its equity capital in item 2 of Call Report Schedule RI-A—Changes in Equity Capital, and disclose this amount in item 4 of Schedule RI-E—Explanations.

Examination Considerations

Under the 2004 Interagency Statement on the Purchase and Risk Management of Life Insurance, institutions should have a comprehensive risk management process for purchasing and holding life insurance. A prudent risk management process includes effective senior management and board oversight as well as an effective ongoing system of risk assessment, management, monitoring, and internal control. As a key aspect of the ongoing monitoring process, management should provide a risk management review of the institution's insurance assets to the board of directors at least annually. The Interagency Statement provides examples of situations when more frequent reviews are appropriate. Although changes in accounting requirements are not specifically included among the examples, the EITF's two recent consensuses are of sufficient significance as to warrant a review outside of the annual cycle.

Among other elements, an institution's risk management review should include a comprehensive assessment of the risks of its life insurance holdings. In particular, the Interagency Statement notes that transaction/operational risk arises due to the tax and accounting treatments of life insurance products and instructs an institution to thoroughly review and understand how the accounting rules will apply to the insurance products it is considering purchasing. Therefore, when accounting rules change, a thorough review and understanding of the effect of the changes should be an integral part of the institution's risk management review. The Interagency Statement also notes that "[s]plit-dollar life insurance has complex tax and legal consequences" and that material modifications of these arrangements may unfavorably alter their tax treatment. As a consequence, the Interagency Statement cautions institutions to "consult qualified tax, insurance, and legal advisors" before entering into or modifying split-dollar life insurance arrangements.

Because the application of the consensuses in EITF 06-4 and EITF 06-10 may require banks with split-dollar life insurance arrangements to initially recognize a liability for postretirement benefits, which will reduce both equity capital and regulatory capital, and to subsequently recognize compensation costs over the remainder of the employees' required service periods until their full eligibility dates, banks should use the transition period during 2007 for risk management reviews that assess the substance of their split-dollar arrangements. In these reviews, banks should also consider the nature of their interest in the life insurance policies associated with their split-dollar arrangements to ensure that they are properly reporting their insurance assets. The results of these reviews, including consultations with their external accountants and other qualified advisors, should enable management to understand and evaluate the accounting consequences of the EITF consensuses; ascertain the impact of the consensuses on equity capital on their effective date and on earnings thereafter; and determine the actions needed, if any, to remedy the effects of applying the consensuses beginning in 2008. These actions may include considering whether to eliminate or reduce the postretirement benefits provided under these arrangements after addressing any relevant tax consequences from such modifications.

Thus, when examining banks that have entered into split-dollar life insurance arrangements with employees, examiners should ensure that management is aware of the recent accounting guidance issued by the EITF and is assessing, or has completed an assessment of, the impact that the consensuses will have on their organization as part of a timely risk management review of these insurance arrangements. In cases where management has not yet taken appropriate action, examiners should seek management's commitment to promptly address the EITF guidance relevant to its split-dollar arrangements.

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Regulatory and Supervisory Roundup

This section provides an overview of recently released regulations and supervisory guidance, arranged in reverse chronological order. Press Release (PR) or Financial Institution Letter (FIL) designations are included so the reader may obtain more information.

Subject	Summary
New Government-Wide ID Theft Home Page Established (PR-33-2007, April 23, 2007)	The Federal Deposit Insurance Corporation (FDIC), a participant in the government-wide Identity Theft Task Force, provided a direct link to the new, centralized government website on identity theft. The new site, www.idtheft.gov, was launched April 23, 2007. Initially, the site will provide the task force's strategic plan. The plan, which represents the input of 17 federal agencies, including the FDIC, sets out recommendations to prevent identity theft, to help identity theft victims recover from those crimes, and to prosecute and punish identity theft–related criminals.
Institutions Encouraged to Work with Mortgage Borrowers Who Are Unable to Make Their Payments (PR-32-2007, FIL-35-2007, April 17, 2007)	The FDIC, Federal Reserve Board (FRB), Office of the Comptroller of the Currency (OCC), Office of Thrift Supervision (OTS), and National Credit Union Administration (collectively, the federal financial institution regulatory agencies) issued a statement encouraging financial institutions to work with homeowners who are unable to make mortgage payments. Prudent workout arrangements that are consistent with safe and sound lending practices are generally in the long-term best interests of both the financial institution and the borrower. Institutions will not face regulatory penalties if they pursue reasonable workout arrangements with borrowers. See www.fdic.gov/news/news/press/2007/pr07032.html.
Comments Sought on Proposed Model Privacy Form (FIL-34-2007, April 16, 2007; PR-24-2007, March 21, 2007)	The federal financial institution regulatory agencies, the Securities and Exchange Commission (SEC), the Federal Trade Commission, and the Commodity Futures Trading Commission jointly published a notice of proposed rulemaking (NPR) seeking comment on a model privacy form financial institutions could use to satisfy the privacy notice requirements of the Gramm-Leach-Bliley Act (GLBA). The proposed privacy form would also provide consumers with the opportunity to limit certain information-sharing practices, as permitted by the GLBA and the Fair Credit Reporting Act. Comments on the proposed rule were due by May 29, 2007. See www.fdic.gov/news/news/financial/2007/fil07034.html.
Supervisory Policy on Identify Theft Issued (FIL-32-2007, April 11, 2007)	The FDIC issued its *Supervisory Policy on Identity Theft.* The policy describes the characteristics of identity theft. It also sets forth the FDIC's expectations that institutions under its supervision take steps to detect and prevent identity theft and mitigate its effects to protect consumers and help ensure the safe and sound operation of financial institutions. See www.fdic.gov/news/news/financial/2007/fil07032a.html.
Comments Sought on Expanded Examination Cycle for Certain Institutions (PR-29-2007, April 3, 2007)	The FDIC, FRB, OCC, and OTS (collectively, the federal bank and thrift regulatory agencies) requested public comment on proposed interim rules expanding the range of small institutions eligible for an extended 18-month on-site examination cycle. The proposed interim rules, which became effective May 10, 2007, allow well-capitalized and well-managed banks and savings associations with up to $500 million in total assets and a composite rating of 1 or 2 to qualify for an 18-month (rather than a 12-month) on-site examination cycle. Until recently, only institutions with less than $250 million in total assets could qualify for an extended 18-month on-site examination cycle. The proposed interim rules also revise the provisions governing the on-site examination cycle for the U.S. branches and agencies of foreign banks. The public comment period closed May 10, 2007. See ww.fdic.gov/news/

news/press/2007/pr07029.html.

Comments Requested on Proposed Statement on Subprime Mortgage Lending (FDIC-PR-18-2007, March 2, 2007; FIL-26-2007, March 9, 2007)

The federal financial institution regulatory agencies sought comment on the proposed *Statement on Subprime Mortgage Lending* (Subprime Statement). The Subprime Statement addresses the risks and emerging issues relating to subprime mortgage lending practices, most notably certain adjustable rate mortgage lending products. Comments were due by May 7, 2007. See www.fdic.gov/news/news/press/2007/pr07018a.html.

Comments Requested on Proposed Supervisory Guidance for Basel II (PR-13-2007, February 15, 2007; FIL-20-2007; February 28, 2007; *Federal Register,* Vol. 72, No. 39, p. 9084, February 28, 2007)

The federal bank and thrift regulatory agencies sought comment on proposed guidance describing the agencies' expectations for banking organizations that would adopt the Advanced Internal Ratings-Based Approach (IRB) for credit risk and the Advanced Measurement Approaches (AMA) for operational risk under the proposed new Basel II capital framework. The proposed guidance also establishes the process for supervisory review and the implementation of the capital adequacy assessment process under Pillar 2 of the Basel II framework. Comments on the proposed guidance were due May 29, 2007. See www.fdic.gov/news/news/financial/2007/fil07020.html.

Comments Requested on Proposed Guidelines on Assessment Rate Adjustment for Large Institutions and Insured Foreign Branches in Risk Category I (FIL-19-2007, February 27, 2007; *Federal Register,* Vol. 72, No. 34, p. 7878, February 21, 2007)

The FDIC sought comment on a proposed set of ten guidelines that would govern the process for determining when an assessment rate adjustment is appropriate and what the magnitude of the adjustment should be. These guidelines are intended to further clarify the analytical processes and the controls applied to them in making assessment rate adjustments. Comments on the proposed guidelines were due March 23, 2007. See www.fdic.gov/news/news/financial/2007/fil07019.html.

Certain Reporting Requirements Repealed (FIL-7-2007, January 26, 2007)

The FDIC issued a final rule repealing FDIC Part 349, Reports and Public Disclosure of Indebtedness of Executive Officers and Principal Shareholders to a State Nonmember Bank and Its Correspondent Banks. The final rule became effective on December 22, 2006. See www.fdic.gov/news/news/financial/2007/fil07007.html.

Supervisory Policy on Predatory Lending (FIL-6-2007, January 22, 2007)

The FDIC issued its *Supervisory Policy on Predatory Lending,* which describes certain characteristics of predatory lending and reaffirms that such activities are inconsistent with safe and sound lending and undermine individual, family, and community economic well-being. The statement describes the FDIC's supervisory response to predatory lending, including a list of policies and procedures that relate to consumer lending standards. See www.fdic.gov/news/news/financial/2007/fil07006a.html.

Final Statement Concerning Elevated Risk Complex Structured Finance Activities (PR-3-2007, January 6, 2007)

The federal financial institution regulatory agencies and the SEC issued a final statement on the complex structured finance activities of financial institutions. The statement describes the types of internal controls and risk management procedures that should help financial institutions identify, manage, and address the heightened legal and reputational risks that may arise from certain complex structured finance transactions. See

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www.fdic.gov/news/news/press/2007/pr07003a.html.

Comments Requested on Draft Guidelines on Small-Dollar Loans (PR-107-2006, December 4, 2006)

The FDIC sought comment on proposed guidelines from state nonmember banks to encourage them to offer affordable small-dollar loan products. FDIC-supervised institutions that offer these products in a responsible, safe, and sound manner may receive favorable consideration under the Community Reinvestment Act. Comments were due February 2, 2007. See www.fdic.gov/news/news/press/2006/pr06107a.html.

Final Rule Amending Part 328, Advertisement of FDIC Membership (FIL-112-2006, December 27, 2006; *Federal Register,* Vol. 71, No. 218, p. 66098, November 13, 2006)

The FDIC issued the final rule amending FDIC Part 328, Advertisement of Membership. Recent amendments to the Federal Deposit Insurance Act required the FDIC to prescribe an official sign that all FDIC-insured depository institutions would be required to display. The rule accomplishes that requirement and provides for other changes to the regulation. The final rule took effect November 13, 2006. See www.fdic.gov/news/news/financial/2006/fil06112.html.

Comments Requested on Modifications to the Risk-Based Capital Framework (Basel IA) (PR-112-2006, December 5, 2006; FIL-111-2006, December 26, 2006; *Federal Register,* Vol. 71, No. 247, p. 77446, December 26, 2006)

The federal bank and thrift regulatory agencies jointly issued an NPR and sought comment on possible modifications to the risk-based capital standards for all domestic banks, bank holding companies, and savings associations that are not subject to the risk-based capital framework proposed in the Basel II NPR. The comment period closed March 26, 2007. See www.fdic.gov/news/news/financial/2006/fil06111.html.

Comments Requested on Large-Bank Deposit Insurance Determination Modernization Proposal (PR-111-2006, December 5, 2006; FIL-109-2006, December 21, 2006; *Federal Register,* Vol. 71, No. 239, p. 74857, December 13, 2006)

The FDIC, through an advance notice of proposed rulemaking (ANPR), sought comment on whether and how the largest insured depository institutions should be required to modify their deposit systems so that the FDIC may calculate deposit insurance coverage quickly in the event of an institution's failure. Comments were due March 13, 2007. See www.fdic.gov/news/news/financial/2006/fil06109.html.

Revised Policy Statement Issued on the Allowance for Loan and Lease Losses (PR-115-2006, December 13, 2006; FIL-105-2006, December 13, 2006)

The federal financial institution regulatory agencies issued a revised *Interagency Policy Statement on the Allowance for Loan and Lease Losses* (ALLL) and supplemental frequently asked questions. The policy statement revises and replaces the banking agencies' 1993 policy statement on the ALLL. See www.fdic.gov/news/news/financial/2006/fil06105a.pdf.

Joint Guidance Issued on Commercial Real Estate Lending (PR-114-2006, December 6, 2006;

FIL-104-2006, December 12, 2006; *Federal Register,* Vol. 71, No. 238, p. 74580, December 12, 2006)

The federal financial institution regulatory agencies jointly issued *Guidance on Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices.* The guidance reminds institutions that strong risk management practices and appropriate levels of capital are essential elements of a sound commercial real estate (CRE) lending program, particularly when an institution has a concentration in CRE loans. See www.fdic.gov/news/news/financial/2006/fil06104.html.

Final Rules on Deposit Insurance Assessments and the Designated Reserve Ratio (PR-101-2006, November 2, 2006; FIL-102-2006, and FIL-103-2006, November 30, 2006; *Federal Register,* Vol. 71, No. 230, pp. 69270 and 69282, November 30, 2006)

The FDIC issued final rules to amend Part 327 of the FDIC rules and regulations. One rule creates a new system for risk-based assessments and sets assessment rates beginning January 1, 2007. The other rule sets the designated reserve ratio at 1.25 percent. The amendments were made to implement the Federal Deposit Insurance Reform Act of 2005 and were intended to make the deposit insurance assessment system react more quickly and more accurately to changes in institutions' risk profiles and to ameliorate several causes for complaint by insured depository institutions. The final rule took effect January 1, 2007. See www.fdic.gov/news/news/financial/2006/fil06102.html and www.fdic.gov/news/news/financial/2006/fil06103.html.

Guidelines for an Environmental Risk Program Issued (FIL-98-2006, November 13, 2006)

The FDIC issued updated *Guidelines for an Environmental Risk Program* to reflect changes to the Comprehensive Environmental Response, Compensation, and Liability Act. Environmental contamination and its associated liability can have a significant effect on the value of real estate collateral. It is also possible for a lending institution to be held directly liable for the environmental cleanup of collateral acquired by the institution. Institutions should have in place appropriate safeguards and controls to limit exposure to this potential environmental liability. See www.fdic.gov/news/news/financial/2006/fil06098a.pdf.

Final Rule Issued on Late Deposit Insurance Assessment Penalties (FIL-97-2006, November 9, 2006; *Federal Register,* Vol. 71, No. 217,