



## REVISITING FDICIA: A SUMMARY OF KEY PART 363 FINAL RULES

### Executive Summary:

- Part 363 rules are intended to identify problems in financial management
- Revisions were intended to clarify prior rules and incorporate some aspects of SOX 404
- Various disclosures and filings are required by management once assets are >\$500M
- Once >\$1B in assets, management has to assess and assert on internal control effectiveness; financial auditor will need to issue an opinion on effectiveness of financial and regulatory reporting controls
- Internal control assessment includes controls over regulatory reporting
- Audit committees have to meet independence requirements
- Compliance with insider loans and dividend restrictions is critical

The FDIC has recently released revised rules for Part 363, commonly known as FDICIA. The changes were driven by experience with prior compliance and a desire to clarify prior guidance and incorporate certain items from the Sarbanes-Oxley Act Section 404 into FDICIA requirements. The goal of the revised rules is consistent with the original rules, which is to facilitate the early identification of problems in financial management of covered institutions. The assumption behind the goal is that audited financial statements and effective internal controls over financial and regulatory reporting assist the FDIC in executing their oversight and monitoring role.

With the rules freshly finalized, this Accounting Insight summarizes the key requirements so you can consider their impact on your institution and your current state of readiness. Please note we have not addressed every compliance issue in Part 363, and we encourage you to read the full text and supporting documents at <http://www.fdic.gov/news/news/financial/2009/fil09033.html> to provide additional information on issues not addressed by this Accounting Insight.

### SIGNIFICANT REVISIONS TO CURRENT GUIDANCE

The most significant revisions to the existing rules will:

- Extend the time period for a non-public institution to file its Part 363 Annual Report by 30 days and replace the 30-day extension of the filing deadline that may be granted to an institution in certain circumstances with a late filing notification requirement.
- Provide relief from the annual reporting requirements for institutions that are merged out of existence before the filing deadline.
- Provide relief from reporting on internal control over financial reporting for businesses acquired during the fiscal year.
- Require management's assessment of compliance with the laws and regulations pertaining to insider loans and dividend restrictions and disclosure of any noncompliance with such laws and regulations.

## **SIGNIFICANT REVISIONS TO CURRENT GUIDANCE (CONTINUED)**

- Require an institution's management and the independent public accountant to identify the internal control framework used to evaluate internal control over financial reporting and disclose all identified material weaknesses that have not been remediated prior to the institution's most recent fiscal year-end.
- Clarify the independence standards with which independent public accountants must comply and enhance the enforceability of compliance with these standards.
- Specify that the duties of the audit committee include the appointment, compensation, and oversight of the independent public accountant, including ensuring that audit engagement letters do not contain unsafe and unsound limitation of liability provisions.
- Require certain communications by independent public accountants to audit committees.
- Establish retention requirements for audit working papers.
- Require board of directors to adopt written criteria for evaluating an audit committee member's independence and provide expanded guidance for board of directors to use in determining independence.
- Provide that ownership of 10 percent or more of any class of voting securities of an institution is not an automatic bar for considering an outside director to be independent of management.
- Require the total assets of a holding company's insured depository institution subsidiaries to comprise 75 percent or more of the holding company's consolidated total assets in order for an institution to be eligible to comply with Part 363 at the holding company level.
- Provide illustrative management reports to assist institutions in complying with the annual reporting requirements.

## **THE IMPACT OF ASSET SIZE ON COMPLIANCE REQUIREMENTS**

FDICIA has two main categories that are based on the asset size of the institution at the beginning of the institution's fiscal year. The two main categories are:

- >\$500 million to \$1 billion in assets, referred to here as Tier II.
- >\$1 billion in assets, referred to here as Tier I.

Throughout this Accounting Insight, we will indicate how banks within these asset size categories are affected by the requirements. Although there are bright line asset thresholds, it is important for management to plan ahead and not wait until reaching a threshold before putting in place the proper compliance procedures.

## **KEY DISCLOSURES AND REPORTING REQUIREMENTS**

For Tier II institutions, the key annual disclosures and reports include:

- Audited comparative annual financial statements with the independent public accountant's audit report.

- A management report containing management's responsibilities for:
  - Preparing the annual financial statements.
  - Establishing and maintaining an adequate internal control structure over financial and regulatory reporting.
  - Complying with safety and soundness laws and regulations pertaining to insider loans and dividend restrictions.
  - Assessing the institution's compliance with laws and regulations during the year pertaining to insider loans and dividend restrictions, including state laws, management's conclusion regarding this compliance, and disclosures of any instances of noncompliance.

Tier I institutions must meet all the requirements listed above for Tier II institutions and:

- Provide an assessment and conclusion by management on the effectiveness of internal controls over financial reporting at year-end, including:
  - The assessment framework used (generally COSO).
  - The controls over regulatory reporting, including identification of the regulatory reporting instructions used.
  - Disclosure of all material weaknesses not remediated prior to fiscal year-end.
- Provide an independent public accountant attestation report on the effectiveness of internal controls over financial reporting, including those over regulatory reporting.

## **AUDIT COMMITTEE IMPACTS**

Among other key requirements, audits committees for Tier I and Tier II institutions will need to ensure:

- Audit Committees are made up of outside directors and are independent of management. The specific requirements based on institution size are as follows:
  - Tier I – All members need to be outside directors and independent of management.
  - Tier II – Majority of members need to be outside directors and independent of management.
- Documented criteria are in place for evaluating if an audit committee member is an outside director and independent of management. Each committee member should be evaluated against these criteria annually. The written criteria and assessment should be in place by 12/31/09.
- If an audit committee member owns more than 10% of outstanding common shares of the institution, the Committee should determine and document their assessment of independence.
- Member compensation does not exceed \$100,000.
- The auditors engaged are independent and can adequately perform the work needed.
- Audit engagement letters do not contain unsafe or unsound limitations of external auditor liability either in provisions in engagement letters or in provisions that accompany alternative dispute resolution (ADR) agreements with respect to engagements for financial statement audits, audits of internal control over financial reporting, and attestations.

## **HOLDING COMPANY CONSIDERATIONS**

Compliance with the above requirements for individual institutions can be accomplished at the holding company level when 75% of the consolidated total assets of the holding company derive from insured depository institutions. This requirement was enacted to make sure the audit procedures done at the holding company level would adequately cover the individual institution(s). If your institution no longer qualifies for complying at the holding company level because of the 75% of total assets test, you will have until fiscal years ending on or after June 15, 2010, to become compliant at the insured depository institution level.

When filing the reports at the holding company level, a cover letter should be attached that clearly states what institution(s) are covered by the filing.

## **KEY DEADLINES**

Annual reports required under Part 363 need to be filed within the following time frames:

- Non-public company – 120 days after the end of the institution's fiscal year.
- Public company or subsidiary of a public company – 90 days after the end of the institution's fiscal year.

The Independent Public Accountants' Management Letter and other communication to the Board, including change, dismissal, or resignation of the independent public accountants, must be filed within 15 days of the receipt or event.

If an institution is not able to meet a filing deadline, it needs to file a *Notice of Late Filing* (no extensions will be provided).

## **CONTACT INFORMATION**

For more information, please contact your Wipfli relationship executive or:

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