

**CREDIT UNION DIVISION[189]**

**Adopted and Filed**

Pursuant to the authority of Iowa Code section 533.104, the Credit Union Division hereby amends Chapter 18, "Maintenance of Allowance for Loan Losses Account," Iowa Administrative Code.

The amendments serve to clarify the Division's expectations regarding methodologies and support for the Allowance for Loan and Lease Losses (ALLL). The amendments are intended to provide the necessary parallel guidance issued in Interpretive Rulings & Policy Statements (IRPS) 02-3 by the National Credit Union Administration for all federally insured credit unions.

Notice of Intended Action was published in the Iowa Administrative Bulletin on August 10, 2011, as **ARC 9672B**. No comments were received. These amendments are identical to those published under Notice.

After analysis and review of this rule making, no impact on jobs has been found.

These amendments are intended to implement Iowa Code chapter 533.

These amendments will become effective on November 9, 2011.

The following amendments are adopted.

ITEM 1. Amend **189—Chapter 18**, title, as follows:

**MAINTENANCE OF ALLOWANCE FOR LOAN AND LEASE LOSSES ACCOUNT**

ITEM 2. Amend rule **189—18.1(533)**, definitions of "Allowance for loan losses" and "Provision for loan losses," as follows:

~~"Allowance for loan and lease losses" means a valuation account of the general ledger that is established for the purpose of disclosing and recognizing probable loan losses and is reported as a reduction to the loan asset whenever the credit union's financial statement is generated.~~ means an estimate of loan and lease losses in the entire loan portfolio, including estimated inherent losses, in conformity with generally accepted accounting principles and which meets regulatory requirements for full and fair disclosure of the financial statements.

~~"Provision for loan and lease losses" means an expense account of the general ledger to which debit or credit adjustments to the allowance for loan and lease losses ~~account~~ are charged.~~

ITEM 3. Rescind the definitions of "Contingency," "Financial statement," "General ledger," "Loan classified as doubtful," "Loan classified as loss" and "Loan classified as substandard" in rule **189—18.1(533)**.

ITEM 4. Amend rule **189—18.3(533)** as follows:

**189—18.3(533) Generally accepted accounting principles.**

**18.3(1)** Credit union financial statements shall be prepared in accordance with generally accepted accounting principles (GAAP), except for authorized intentional regulatory accounting practices (RAP) which may differ, and shall provide for the complete and accurate disclosure of all assets, liabilities, and equity, including any valuation allowance accounts as may be necessary to correctly present the financial position; and all income and expenses necessary to correctly present the results of operations for the period concerned. ~~The financial statement shall be prepared and made available within 15 days after the end of each month showing the condition of the credit union as of the close of business on the last business day of the month.~~

**18.3(2)** The financial statement shall be prepared and made available within 15 days after the end of each month and shall show the condition of the credit union as of the close of business on the last business day of the month.

~~**18.3(2)**~~ **18.3(3)** Complete and accurate disclosure shall be required of a credit union so as to provide for a level of disclosure to any person or entity in order to clearly and objectively inform them of the financial condition and the results of operations of the credit union.

~~18.3(3)~~ Valuation allowance accounts shall be required of a credit union to provide for the net presentation of loan amounts without actually writing off estimated losses or expenses.

ITEM 5. Amend rule 189—18.4(533) as follows:

**189—18.4(533) Allowance for loan and lease losses.**

~~18.4(1)~~ Loans outstanding should be recorded to reflect the outstanding balance due the credit union and adjusted by the establishment of an allowance for loan losses account through periodic charges to operating expenses. This credit balance account reflects the amount set aside by the credit union to provide a cushion to absorb losses on outstanding loans. The amount carried in this account shall represent possible losses which may be incurred in the normal payoff of outstanding loans, and shall be considered as a deduction from total loans shown on the financial statement in order that the asset reflects fair market value. an amount at least equal to reasonably foreseeable loan and lease losses. Each credit union is required to establish and maintain a methodology to determine the amount needed in the allowance for loan and lease losses account in accordance with generally accepted accounting principles (GAAP).

~~18.4(2)~~ A credit union may, at its option, establish separate allowance accounts for each of its various categories of loans, i.e., allowance for loan losses—consumer loans, allowance for loan losses—lines of credit, etc. The credit union’s board of directors must adopt a policy ensuring that loans are charged off in a timely manner.

~~18.4(3)~~ Periodic adjustment of the allowance for loan losses account shall be required to provide for the disclosure of the credit union’s best estimate of potential losses which will be sustained in the liquidation of current outstanding loans. As At a minimum, the account shall be adjusted at least quarterly or prior to the end of each dividend period, or more often as required. The amount of the periodic adjustments shall be determined by the credit union after all charge-offs and recoveries applicable to the period have been recorded. Periodic adjustments to the allowance for loan and lease losses account will be charged to the provision for loan and lease losses account.

~~18.4(4)~~ The credit union shall maintain full and complete documentation of the determination of the balance in the allowance for loan and lease losses account.

~~18.4(4)~~ 18.4(5) The maintenance of an allowance for loan and lease losses account shall not eliminate the requirement for transferring the percentage of gross income before the payment of a dividend to the credit union’s regular reserves as required by Iowa Code chapter 533.

~~18.4(5)~~ Credit unions shall be required to use an acceptable method of adjusting the allowance for loan losses account, such as, but not limited to, the “adjustment method” or “experience method.” There is no one method that is preferable. The method used by a credit union shall be consistent, comprehensive, logical, and relevant to the credit union’s circumstances, and the calculation shall be comprehensive, taking into account the risks inherent in the various types of lending.

ITEM 6. Amend rule 189—18.5(533), catchwords, as follows:

**189—18.5(533) Allowance for loan and lease losses computation.**

ITEM 7. Amend subrule 18.5(1) as follows:

~~18.5(1)~~ The credit union shall perform a review of all loans to determine potential losses which will be sustained in collection and to establish an adequate allowance for loan losses account. The estimate shall be based on the best judgment of the credit union officials and take all pertinent factors into consideration including, but not limited to: Credit unions are responsible for determining an adequate allowance for loan and lease losses account and adopting a reasonable methodology for doing so. In determining the appropriate allowance, each credit union shall:

- a. Separate the loan portfolio into homogenous loan pools based on common risk factors;
- b. Calculate the net loss percentage of each pool, using the historical loss or adjusted loss method which includes consideration of: loan delinquency status of two months or more; collection experience of the credit union; unusual economic conditions that may affect collectibility; availability of pledged

shares;<sup>2</sup> collateral, security, or endorsers; insured FHA or educational loan coverage guaranteed status; and the general credit reputation of the borrowers;<sup>2</sup>

c. Individually classify loans with unique characteristics;

d. Add the resulting amounts to determine the amount needed in the allowance for loan and lease losses account.

ITEM 8. Rescind subrules **18.5(2)** to **18.5(4)**.

ITEM 9. Renumber subrule **18.5(5)** as **18.5(2)**.

ITEM 10. Amend renumbered subrule 18.5(2) as follows:

**18.5(2)** ~~The allowance for loan losses account should include estimated amounts to cover loan losses which may result from specifically identified troubled or classified loans, pools of classified loans, pools of loan types or credit instruments, and a general portion of all other loans and credit instruments for inherent losses. Credit unions are responsible for determining an adequate allowance for loan losses account, and adopting a reasonable methodology for doing so. If a credit union fails to determine an adequate and reasonable allowance for loan and lease losses account which will result in the fair presentation of its financial statement, the superintendent may require additional amounts to be set aside as provided by Iowa Code chapter 533.~~

ITEM 11. Amend rule 189—18.6(533) as follows:

#### **189—18.6(533) Accounting treatment.**

**18.6(1)** The allowance for loan and lease losses account shall be charged with the amount of the uncollectible loans which have been authorized for ~~write-off~~ charge-off by the board of directors or as directed by the superintendent. Likewise, recoveries on loans charged off shall be credited to this account.

**18.6(2)** Routine periodic adjustments to the allowance for loan and lease losses account, accomplished during an accounting or dividend period within the current fiscal year, shall be made by a charge to the provision for loan and lease losses account.

**18.6(3)** Prior period adjustments to the allowance for loan and lease losses account, within the current fiscal year, may be permitted only in relation to the correction of an error in a prior period financial statement. These corrections shall be accounted for and reported in the same manner as routine periodic adjustments, and shall be charged to the current period expenses through the provision for loan and lease losses ~~account~~.

**18.6(4)** Prior period adjustments to the allowance for loan and lease losses account, outside of the current fiscal year, may be permitted only in relation to the correction of an error in the previous fiscal year financial statement. These corrections shall be accounted for and reported as a charge to the undivided earnings account. If the result of this correction would create a deficit balance in the undivided earnings account, the deficiency so created may be transferred to other segregations of undivided earnings or to the legal reserve account, subject to the prior approval of the superintendent.

**18.6(5)** If a deficit is created in the legal reserve account, through the establishment or maintenance of the allowance for loan and lease losses account, the deficit shall be transferred first to undivided earnings and, if this shall cause a deficit in undivided earnings, then to other segregations of undivided earnings that may exist, exclusive of the special reserve account should it be required by the superintendent.

**18.6(6)** The superintendent may waive, in whole or in part, the requirement for the maintenance of the allowance for loan and lease losses account which is in excess of the statutory reserve requirements of Iowa Code chapter 533 but is required under this chapter. Such waiver shall be as a result of written

application from the directors of a credit union and shall set forth their justification for the requested waiver.

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