FEDERAL RESERVE BANK OF DALLAS

2200 N. PEARL ST.

DALLAS, TX 75201-2272

December 22, 2005

Notice 05-77

TO: The Chief Executive Officer of each financial institution and others concerned in the Eleventh Federal Reserve District

SUBJECT

Questions and Answers for Financial Institutions in Response to Hurricanes Katrina and Rita

DETAILS

The federal financial institutions regulatory agencies continue to receive inquiries from financial institutions on regulatory and reporting issues related to Hurricanes Katrina and Rita. Accordingly, the agencies have issued a complete set of questions and answers (Q&As) as of November 23, 2005, which includes the first set of Q&As previously issued in SR letter 05-20 on October 14, 2005. The issue date of a Q&A is indicated at the end of each question. The new Q&As provide guidance on

- Past due and nonaccrual reporting, including troubled debt restructurings, for commercial loans;
- Past due and nonaccrual reporting for small business loans subject to across-the-board payment deferral arrangements;
- Temporary hardship programs for non-credit card retail lending, including residential mortgage lending; and
- Treatment of municipal bond obligations.

For additional copies, bankers and others are encouraged to use one of the following toll-free numbers in contacting the Federal Reserve Bank of Dallas: Dallas Office (800) 333-4460; El Paso Branch *Intrastate* (800) 592-1631, *Interstate* (800) 351-1012; Houston Branch *Intrastate* (800) 392-4162, *Interstate* (800) 221-0363; San Antonio Branch *Intrastate* (800) 292-5810.

ATTACHMENTS

A copy of the Board's SR letter 05-24, dated December 2, 2005, and the agencies' complete set of Q&As are attached.

MORE INFORMATION

For more information, please contact Bobby Coberly, (214) 922-6209, or Randy Steinley, (713) 483-3117, Banking Supervision Department. Previous Federal Reserve Bank notices are available on our web site at **www.dallasfed.org/banking/notices/index.html** or by contacting the Public Affairs Department at (214) 922-5254.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

DIVISION OF BANKING
SUPERVISION AND
REGULATION

SR 05-24
December 2, 2005

TO THE OFFICER IN CHARGE OF SUPERVISION AND
APPROPRIATE SUPERVISORY AND EXAMINATION STAFF
AT EACH FEDERAL RESERVE BANK AND TO BANKING
ORGANIZATIONS SUPERVISED BY THE FEDERAL
RESERVE

SUBJECT: Questions and Answers for Financial Institutions in Response to Hurricanes Katrina and Rita

The federal financial institutions regulatory agencies continue to receive inquiries from financial institutions on regulatory and reporting issues related to Hurricanes Katrina and Rita. Attached to this SR letter is the complete set of questions and answers (Q&As) issued by the agencies as of November 23, 2005, which includes the first set of Q&As previously issued in SR letter 05-20 on October 14, 2005.[1] The issue date of a Q&A is indicated at the end of each question. The new Q&As provide guidance on:

- Past due and nonaccrual reporting, including troubled debt restructurings, for commercial loans.
- Past due and nonaccrual reporting for small business loans subject to across-the-board payment deferral arrangements.
- Temporary hardship programs for non-credit card retail lending, including residential mortgage lending.
- Treatment of municipal bond obligations

Reserve Banks are asked to provide a copy of this letter and attachment to state member banks and bank holding companies and to appropriate supervision staff. Additional hurricane-related guidance is available on the Board's Hurricane Katrina webpage. Questions should be directed to Molly Wassom, Associate Director, Division of Banking Supervision and Regulation at 202/452-2305. For accounting and reporting related questions, please contact Charles Holm, Deputy Associate Director, at 202/452-3502 or Art Lindo, Manager of Accounting Policy and Disclosure, at 202/452-2695.

Richard Spillenkothen
Director

Attachment: Interagency Questions and Answers for Financial Institutions in Response to Hurricanes Katrina and Rita (927 KB PDF)
As of November 23, 2005

Supersedes: SR letter 05-20

Notes:

1. As a result, SR letter 05-20 is superseded.

Attachment
Interagency Questions and Answers for Financial Institutions in Response to Hurricanes Katrina and Rita
(As of November 23, 2005).[1]

Third Quarter 2005 Regulatory Report Filings

Q1: Hurricanes Katrina and Rita (the Hurricanes) may affect the ability of financial institutions to submit timely and accurate regulatory reports for September 30, 2005. These reports include bank Reports of Condition and Income (Call Reports), Thrift Financial Reports, Thrift Holding Company Reports, credit union 5300 and 5310 Call Reports, and bank holding company Y reports. What approach do the member agencies of the Federal Financial Institutions Examination Council expect to take in situations where institutions affected by the Hurricanes expect to encounter difficulty completing their September 30, 2005, regulatory reports?
(October 7, 2005)

A1: Institutions affected by the Hurricanes that expect to encounter difficulty submitting accurate and timely data for the September 30, 2005, report date should contact their primary federal regulatory agency, as shown below, to discuss their situation. The agencies do not expect to assess penalties or take other supervisory action against institutions that take reasonable and prudent steps to comply with regulatory reporting requirements if those institutions are unable to fully satisfy those requirements by the specified filing deadlines because of the effects of the Hurricanes. The agencies' staffs stand ready to work with affected institutions that may be experiencing problems fulfilling their reporting responsibilities, taking into account each institution's particular circumstances, including the status of its reporting and recordkeeping systems and the condition of its underlying financial records.

Appropriate offices of federal regulatory agencies to contact:
Board: For Call and Y Reports, contact the Federal Reserve Bank to which the bank or bank holding company submits its reports. Alternatively, banks and bank holding companies may contact Douglas Carpenter, Supervisory Financial Analyst, Federal Reserve Board, at (202) 452-2205.

FDIC: For Call Reports, contact Data Collection and Analysis Section, Washington, DC, at (800) 688-FDIC (3342).

NCUA: For 5300 Call Reports, contact the Atlanta Regional Office (Alabama, Mississippi) at (678) 443-3000, the Austin Regional Office (Louisiana, Texas) at (512) 342-5600, or Ashley Rowe, Department of Risk Management, at (703) 518-6360. For 5310 Call Reports, contact the Office of Corporate Credit Unions at (703) 518 6640.

OCC: For Call Reports, contact the FDIC's Data Collection and Analysis Section, Washington, DC, at (800) 688-FDIC (3342).

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[1] Refer to the Board's website for additional information on Hurricanes Katrina and Rita or the FFIEC website.

OTS: For Thrift Financial Reports and Thrift Holding Company Reports, contact Vikki Reynolds, Financial Reporting Division, Dallas, TX, at (972) 277-9595. For securities filings sent directly to the OTS: For accounting issues, contact Lynnwood Campbell, Director, Securities Filings, Washington, DC, at (202) 906-5713; for legal issues, contact Kevin Corcoran, Deputy Chief Counsel, Washington, DC, at (202) 906-6962.

Third Quarter 2005 Allowance for Loan and Lease Losses

Q1: How should financial institutions with borrowers affected by the Hurricanes determine the appropriate amount to report for their allowance for loan and lease losses (ALLL) in their third quarter regulatory reports (e.g., Call Report, Thrift Financial Report, 5300 and 5310 Call Reports, Y Reports)? *(October 7, 2005)*

A1: For financial institutions with loans to borrowers in the affected area, it may be difficult at this time to determine the overall effect that the Hurricanes will have on the collectibility of these loans. Many of these financial institutions will need time to evaluate their individual borrowers, assess the condition of underlying collateral, and determine potential insurance proceeds and other available recovery sources.

For its third quarter regulatory reports, management should consider all information available prior to filing this report about the collectibility of the financial institution's loan portfolio in order to make its best estimate of probable losses within a range of loss estimates, recognizing that there is a short time between the storms' occurrence and the required filing date for the third quarter regulatory report. Consistent with generally accepted accounting principles (GAAP), the amounts included in the ALLL in third quarter regulatory reports for estimated credit losses incurred as a result of the Hurricanes should include those amounts that represent probable losses that can be reasonably estimated. As financial institutions are able to obtain additional information about their loans to borrowers affected by the Hurricanes, the agencies would expect that estimates of the effect of the Hurricanes on loan losses could change over time and that the revised estimates of loan losses would be reflected in financial institutions' subsequent regulatory reports.

Q2: Is there an ability for a financial institution to disclose additional information in its regulatory reports about the consequences of the hurricanes? *(October 7, 2005)*

A2: Yes, the agencies note that for banks, bank holding companies and thrifts that file Reports of Condition and Income (Call Report), financial statements for bank holding companies (Y-9 Report) or Statements of Condition and Operations (Thrift Financial Report), the management of such financial institutions may, if it wishes, submit a brief narrative statement on the amounts reported in the Call Report, Y-9 Report or Thrift Financial Report. This optional narrative statement will be made available to the public, along with the publicly available data in the Call Report, Y-9 Report or Thrift Financial Report. This statement has long been available for the use

of financial institutions that are required to file a Call Report, Y-9 Report or Thrift Financial Report. Financial institutions may wish to comment on certain financial consequences to their institutions resulting from the effects of the Hurricanes in the optional narrative statement. Please refer to page RC-X-1 of the Call Report instructions for the "Optional Narrative Statement Concerning the Amounts Reported in the Reports of Condition and Income", page BS notes 1 of the FR Y-9C instructions, page SP notes 1 of the FR Y-9SP instructions or to Schedule NS of the Thrift Financial Reporting Instructions for the "Optional Narrative Statement" for further guidance.

Sales of Held-to-Maturity Securities

Q1: If a financial institution affected by major-category hurricanes (such as Hurricane Katrina and Hurricane Rita) sells investment securities that were classified as "held to maturity" (HTM) to meet its liquidity needs, will that financial institution's intent to hold other investment securities to maturity be questioned? *(October 7, 2005)*

A1: Under normal circumstances the sale of any HTM investment would call into question an institution's intent to hold its remaining HTM investments to maturity. However, paragraph 8 of FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, indicates that events that are isolated, nonrecurring, and unusual for the reporting enterprise that could not be reasonably anticipated may cause an enterprise to sell or transfer an HTM security without necessarily calling into question its intent to hold other HTM debt securities to maturity. The FASB staff believes that the above provision encompasses the sales of HTM investment securities by a financial institution that are required to meet the abnormally increased liquidity needs of that financial institution that are directly related to a major-category hurricane (such as Hurricane Katrina and Hurricane Rita) that has caused extraordinary devastation over a wide area affecting a vast number of the financial institution's customers.

Past Due and Nonaccrual Reporting

Q1: Some financial institutions have engaged in programs to temporarily provide consumer borrowers affected by Hurricane Katrina or Rita (the Hurricanes) additional flexibility in repaying loans. For example, some institutions have encouraged borrowers that were affected by the Hurricanes to contact the institution to work out new repayment arrangements (e.g., waiving late fees and deferring interest and principal payments for a short period of time, such as 30 – 90 days). Other institutions have provided similar repayment arrangements across-the-board to all consumer borrowers in the affected area, unless a customer requests otherwise. How should financial institutions report such loans in regulatory reports (e.g., Call Report, Thrift Financial Report, 5300 and 5310 Call Reports, or Y Reports)? *(October 13, 2005)*

A1: Each financial institution should consider the specific facts and circumstances regarding its temporary payment deferral program for consumer borrowers affected by the Hurricanes in

determining the appropriate reporting treatment in accordance with generally accepted accounting principles (GAAP) and regulatory reporting instructions.

Past Due Reporting: Past due reporting status in regulatory reports should be determined in accordance with the contractual terms of a loan as its terms have been revised under a temporary payment deferral program, either as agreed to with the individual customer or provided across-the-board to all affected customers. Accordingly, if all payments are current in accordance with the revised terms of the loan, the loan would not be reported as past due. Furthermore, for loans subject to a payment deferral program on which payments were past due prior to the Hurricanes, the agencies have determined that the delinquency status of the loan may be adjusted back to the status that existed at the date of the applicable hurricane (i.e., "frozen") for the duration of the payment deferral period. For example, if a consumer loan subject to a payment deferral program was 60 days past due on the date of a hurricane, it would continue to be reported in its regulatory reports as 60 days past due during the deferral period (unless the loan is reported in nonaccrual status or charged off as discussed below).

Nonaccrual Status, Allowance for Loan and Lease Losses, and Charge-offs: Each financial institution should refer to the applicable regulatory reporting instructions, as well as its internal accounting policies, in determining whether to report loans to affected customers on which payments have been temporarily deferred as nonaccrual assets in regulatory reports. Furthermore, each institution should maintain an appropriate allowance for loan losses for these loans, considering all information available prior to filing its reports about their collectibility (for further information, see answer 1 to "Third Quarter 2005 Allowance for Loan and Lease Losses"). As information becomes available indicating a specific loan will not be repaid (e.g., information related to the likelihood of collection on a specific loan or the inability of the institution to contact the borrower within a reasonable period), the institution's charge-off policies should be applied.

Regulatory Reporting Disclosures: Each banking organization or thrift institution is encouraged, but not required, to disclose information related to its deferral programs (e.g., amount and types of loans subject to the program) in the optional narrative statements in the Call Report, Y-9 Report, or Thrift Financial Report (for further information, see answer 2 to "Third Quarter 2005 Allowance for Loan and Lease Losses").

Q2: Some financial institutions are working with certain commercial borrowers affected by Hurricane Katrina or Rita (the Hurricanes) to provide additional flexibility in repaying loans (e.g., commercial and industrial loans, commercial real estate loans, and certain small business loans). In this regard, some institutions have renegotiated the repayment terms of specific loans (e.g., deferring or waiving interest and principal payments) with such borrowers, considering the borrower's current situation and overall ability to repay. How should financial institutions report such commercial loans in regulatory reports (e.g., Call Report, Thrift Financial Report, 5300 and 5310 Call Reports, or Y Reports)? *(November 22, 2005)*

A2: Each financial institution should consider the specific facts and circumstances regarding the renegotiated contractual repayment terms for commercial borrowers affected by the Hurricanes in determining the appropriate reporting treatment of these loans in accordance with generally accepted accounting principles (GAAP) and regulatory reporting instructions. Institutions should refer to GAAP and regulatory reporting instructions for further information. Some areas to consider are summarized in the guidance below.

This guidance applies to commercial loans (including small business loans) with terms that have been individually renegotiated. However, financial institutions offering an across-the-board temporary deferral program to small business borrowers should refer to answer 3 to "Past Due and Nonaccrual Reporting."

Past Due (Delinquency) Reporting: Past due reporting status in regulatory reports should be determined in accordance with the contractual terms of a loan as its terms have been renegotiated with the borrower.

Troubled Debt Restructurings (TDRs): Financial institutions should determine whether commercial loans to affected borrowers with renegotiated repayment terms should be reported as TDRs in separate memoranda items for such loans in regulatory reports. A TDR is a loan restructuring in which an institution, for economic or legal reasons related to a borrower's financial difficulties, grants a concession to the borrower that it would not otherwise consider. However, a loan extended or renewed at a stated interest rate equal to the current interest rate for new debt with similar risk is not reported as a TDR. Financial institutions may refer to Financial Accounting Standards Board (FASB) Statement No. 15 for additional guidance on determining whether a loan with renegotiated terms should be accounted for as a TDR. FASB Statement No. 114 also provides guidance on accounting for impairment losses on TDRs (summarized below in "Allowance for Loan and Lease Losses and Charge-offs").

Nonaccrual Status: Each financial institution should refer to the applicable regulatory reporting instructions, as well as its internal accounting policies, in determining whether to report commercial loans to affected borrowers as nonaccrual assets in regulatory reports. In general, institutions shall not accrue interest on any commercial loan: (1) which is maintained on a cash basis because of deterioration in the financial condition of the borrower, (2) for which payment in full of principal or interest is not expected, or (3) upon which principal or interest has been in default for a period of 90 days or more, unless the loan is both well secured and in the process of collection. Accordingly, if interest or principal has been waived on a commercial loan, the loan generally should be placed on nonaccrual status. If interest or principal has been deferred (i.e., no payments are required during the deferral period), but not waived, judgment should be used to determine whether the loan should be placed on nonaccrual status (e.g., by evaluating whether or not full payment of principal and interest is expected).

While a commercial loan is in nonaccrual status, some or all of the cash interest payments received may be treated as interest income on a cash basis as long as the remaining book balance of the loan (i.e., after charge-off of identified losses, if any) is deemed to be fully collectible. Guidance on restoring nonaccrual loans to accrual status is provided in regulatory reporting instructions.

Allowance for Loan and Lease Losses and Charge-offs: Each institution should maintain an appropriate allowance for loan losses for all commercial loans to borrowers affected by the Hurricanes, considering all information available prior to filing its reports about their collectibility. In particular, for commercial loans whose terms have been modified in a TDR that provides for a reduction of either interest or principal (referred to as a modification of terms), financial institutions should measure the impairment loss on the restructured loan in accordance with GAAP (FASB Statement No. 114). In this regard, a credit analysis should be performed in conjunction with the restructuring to determine the loan's collectibility and estimated impairment. The amount of this impairment should be included in the allowance for loan and lease losses..

As information becomes available indicating a specific commercial loan, including a loan that is a TDR, will not be repaid (e.g., information related to the likelihood of collection on a specific loan or the inability of the institution to contact the borrower within a reasonable period or, for a renegotiated loan, to make further contact with the borrower within a reasonable period after revising the repayment terms), the institution's charge-off policies should be applied.

Regulatory Reporting Disclosures: Each banking organization or thrift institution is encouraged, but not required, to disclose information related to its efforts to work with commercial borrowers affected by the Hurricanes in its optional narrative statements in the Call Report, Y-9 Report, or Thrift Financial Report (for further information, see answer 2 to "Third Quarter 2005 Allowance for Loan and Lease Losses").

Q3: Some financial institutions have engaged in programs to temporarily provide small business borrowers affected by Hurricane Katrina or Rita (the Hurricanes) additional flexibility in repaying loans, similar to the programs provided to consumer borrowers. In this regard, some institutions have provided new repayment arrangements (e.g., waiving late fees and deferring interest and principal payments for a short period of time, such as 30-90 days) across-the-board to small business borrowers in the affected area, unless a customer requests otherwise. How should institutions report such small business loans subject to across-the-board payment deferral arrangements in regulatory reports (e.g., Call Report, Thrift Financial Report, 5300 and 5310 Call Reports, or Y Reports)? *(November 22, 2005)*

A3: Each financial institution should consider the specific facts and circumstances regarding its temporary payment deferral program for small business borrowers affected by the Hurricanes in determining the appropriate reporting treatment in accordance with generally accepted accounting principles (GAAP) and regulatory reporting instructions. Institutions should refer to GAAP and regulatory reporting instructions for further information.

Past Due (Delinquency) Reporting: For loans subject to an across-the-board temporary payment deferral program on which payments were past due prior to the Hurricanes, the agencies have determined that the delinquency status of the loan may be adjusted back to the status that existed at the date of the applicable hurricane (i.e., "frozen") for the duration of the payment

deferral period. For example, if a small business loan subject to a payment deferral program was 60 days past due on the date of a hurricane, it would continue to be reported in its regulatory reports as 60 days past due during the deferral period (unless payments are received on the loan that alter its delinquency status or the loan is reported in nonaccrual status or charged off as discussed below).

Nonaccrual Status: Each financial institution should refer to the applicable regulatory reporting instructions in determining whether to report small business loans to affected borrowers as nonaccrual assets in regulatory reports. In general, institutions shall not accrue interest on any small business loan: (1) which is maintained on a cash basis because of deterioration in the financial condition of the borrower, (2) for which payment in full of principal or interest is not expected, or (3) upon which principal or interest has been in default for a period of 90 days or more, unless the loan is both well secured and in the process of collection.

When interest and principal has been deferred (i.e., no payments are required during the deferral period), judgment should be used to determine whether the loan should be placed on nonaccrual status (e.g., by evaluating whether or not full payment of principal and interest is expected).

While a small business loan is in nonaccrual status, some or all of the cash interest payments received may be treated as interest income on a cash basis as long as the remaining book balance of the loan (i.e., after charge-off of identified losses, if any) is deemed to be fully collectible. Guidance on restoring nonaccrual loans to accrual status is provided in regulatory reporting instructions.

Allowance for Loan and Lease Losses, and Charge-offs: Each institution should maintain an appropriate allowance for loan losses for small business loans to borrowers affected by the Hurricanes, considering all information available prior to filing its reports about their collectibility. As information becomes available indicating that a specific small business loan will not be repaid (e.g., information related to the likelihood of collection on a specific loan or the inability of the institution to contact the borrower within a reasonable period), the institution's charge-off policies should be applied.

Regulatory Reporting Disclosures: Each banking organization or thrift institution is encouraged, but not required, to disclose information related to its efforts to work with small business borrowers affected by the Hurricanes in its optional narrative statements in the Call Report, Y-9 Report, or Thrift Financial Report (for further information, see answer 2 to "Third Quarter 2005 Allowance for Loan and Lease Losses").

Credit Card Temporary Hardship and Workout Programs

The following Q&As provide additional guidance concerning the Account Management and Loss Allowance Guidance for Credit Card Lending issued by the federal banking agencies on January 8, 2003 ("Credit Card Guidance") and the Uniform Retail Credit Classification and Account Management Policy, issued by the federal banking agencies on June 6, 2000 ("Retail

Credit Policy Statement") that may be relevant for institutions that have customers affected by Hurricane Katrina and Hurricane Rita ("the hurricanes").

Note: The timeframes for reestablishing communications with customers in the comments below may not be appropriate for institutions physically located in the disaster area. These institutions should work with their primary supervisor to determine appropriate timeframes.

Q1: May an institution place an account in a temporary hardship program before contact with the customer occurs? *(October 7, 2005)*

A1: An institution may place a customer in a temporary hardship program before making contact with the customer. However, placing a customer in a long-term hardship program without communication with the customer generally would not be appropriate. Institutions should work to reestablish communications with customers within 90 days to determine if a temporary hardship program is appropriate for the customer's circumstances. When contact is made, the elements of the hardship program can be modified based on the consumer's situation.

Q2: What should an institution do if communication with a customer isn't reestablished within a reasonable timeframe, such as within 90 days? *(October 7, 2005)*

A2: Institutions should continue to assess their exposure to such customers. Lack of communication with a customer for an extended period heightens the level of risk for the account. Strategies should be developed to determine actions that will be taken if communication is not reestablished, including ensuring that interest and fee income is not overstated, appropriate loss allowances are established, and losses are recognized as appropriate for these accounts.

Q3: May an institution extend the 12-month timeframe for temporary hardship programs or the 60-month timeframe for accounts in workout programs as set forth in the Credit Card Guidance? *(October 7, 2005)*

A3: Temporary hardship programs of up to 18 months may be appropriate for some customers in the affected areas. Institutions should reevaluate the account prior to granting extensions beyond 12 months to determine if an extension of the hardship program is necessary for the customer. For customers in the affected areas with accounts already enrolled in workout programs, an institution may extend repayment timeframes for 12 months beyond the 60-month repayment target set forth in the Credit Card Guidance to accommodate payment deferrals and the need to lower payment amounts. Institutions should maintain appropriate loss allowances for accounts needing the extended timeframes.

Q4: The Retail Credit Policy Statement states that "open-end accounts should not be re-aged more than once within any twelve-month period and no more than twice within any five year period." Does this policy continue to apply to accounts of customers located in the affected areas at the time of the hurricanes? *(October 13, 2005)*

A4: The policy statement, including the limits described above, would continue to apply to such accounts. However, if an institution has agreed to defer customer payments as a result of the hurricanes, the institution may make delinquency bucket adjustments back to the customer's payment status at the time of the hurricanes, which may preclude the need to re-age the account.

Delinquency and Credit Bureau Reporting

Q1: Should an institution temporarily suspend reporting adverse information to the consumer reporting agencies for customers in the affected areas? *(October 7, 2005)*

A1: While financial institutions are not required to report information to consumer reporting agencies, those institutions that do furnish information are encouraged to avoid reporting adverse information to the consumer reporting agencies for customers located in the affected areas until conditions stabilize and borrowers can reasonably be expected to resume payment activity. For example, to prevent reporting adverse information to the consumer reporting agencies, some institutions have temporarily suspended reporting and/or maintained accounts in their payment status at the time of the event even though payments have not been received.

Q2: If an institution cannot contact a customer due to the hurricanes, may an institution maintain the payment status of the customer's account at the time of the hurricanes until contact is reestablished? *(October 13, 2005)*

A2: Freezing an affected account's payment status as of the time of the hurricanes is an acceptable action to prevent the account from rolling through the delinquency buckets and to prevent fee assessments. If communication with the customer is not reestablished within 90 days of the event, the institution should evaluate whether this strategy remains appropriate, and should ensure that interest and fee income is not overstated, that appropriate allowances are established, and that losses are recognized as appropriate for this segment of the institution's accounts.

Retail Credit

Q1: The agencies previously provided clarification on how the June 6, 2000 FFIEC Uniform Retail Credit Classification Policy ("Retail Credit Policy Statement") and the January 8, 2003 Account Management and Loss Methodology for Credit Card Lending ("Credit Card Guidance") apply to credit card temporary hardship and workout programs. See the four Q&A's (three dated

October 7, 2005 and one dated October 13, 2005) under "Credit Card Temporary Hardship and Workout Programs." Does this guidance also apply to other forms of retail credit, including residential mortgage lending? *(November 23, 2005)*.

A1: Yes, with one exception. The Retail Credit Policy Statement applies to credit cards as well as other types of retail credit, including mortgages. Therefore, the four Katrina Q&A's interpreting this guidance with respect to credit cards are also applicable to other types of retail credit. However, that portion of question 3 of the Katrina Q&A under "Credit Card Temporary Hardship and Workout Programs" providing clarification on the 60 month timeframe for credit card workout programs refers to the Credit Card Guidance and does not apply to other forms of retail lending.

Municipal Bond Obligations

Q1: How will the agencies treat bonds issued or backed by state or local governments in the areas affected by Hurricane Katrina and Hurricane Rita (the Hurricanes) for supervisory classification purposes? *(October 24, 2005)*

A1: While it is apparent that state and local governments in Alabama, Louisiana, Mississippi, and Texas have suffered significant physical damage and economic disruption from the Hurricanes, it is too soon to adequately assess the impact on outstanding municipal bond obligations. The extent of support from state and federal assistance and from state, federal, and private insurance has not been determined. Rating agencies have placed a number of issues in Louisiana and Mississippi on credit watch for possible downgrades, but the regulatory agencies are not aware of any municipal bonds that have been downgraded as a result of the Hurricanes. Therefore, for the time being, the agencies will continue to treat municipal bonds issued by Hurricane-affected issuers as investment quality debt securities, provided they were investment quality before the Hurricanes and have not been downgraded subsequently to below investment quality. For non-rated municipal bonds, the institution's management should monitor their exposures in order to assess whether those bonds continue to be the credit equivalent of an investment grade security.

Q2: How should financial institutions holding municipal bonds from issuers in the Hurricane-affected areas on which fair value is less than amortized cost, assess these bonds for "other-than-temporary" impairment for purposes of their third quarter regulatory reports (e.g., Call Report, Thrift Financial Report, 5300 and 5310 Call Reports, Y Reports)? *(October 24, 2005)*

A2: Under GAAP, when the fair value of a municipal bond has declined below its amortized cost, the financial institution holding the bond must assess whether the decline represents an "other-than-temporary" impairment and, if so, write the cost basis of the municipal bond down to fair value through earnings. When making this assessment, financial institutions should apply relevant "other-than-temporary" impairment guidance as required by existing authoritative literature which includes Financial Accounting Standards Board (FASB) Statement No. 115 and

Securities and Exchange Commission (SEC) Staff Accounting Bulletin No. 59, *Other Than Temporary Impairment of Certain Investments in Debt and Equity Securities*. (Topic 5.M. in the Codification of Staff Accounting Bulletins).

In this regard, if a financial institution decided prior to the end of the third quarter that it would sell a municipal bond after quarter-end and management did not expect the fair value of the bond, which is less than its amortized cost, to recover prior to the expected time of sale, a write-down for "other-than-temporary" impairment should be recognized in earnings in the institution's third quarter regulatory reports. Otherwise, for third quarter regulatory reports, management should consider all information available prior to filing this report when assessing Hurricane-affected municipal bonds for "other-than-temporary" impairment. In each subsequent reporting period, financial institutions should continue to assess whether any declines in fair value below amortized cost of these municipal bonds are "other-than-temporary" impairments.