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SEC, REGULATORS REACH COMMON GROUND ON LOAN LOSS RESERVES

- *SEC worried about manipulation of financial statements.*
- *Prudent, conservative allowances are acceptable.*
- *Disclosures should explain allowance amounts.*

Banking regulators and the SEC have come to terms on allowances for loan loss reserves, ending a squabble that began last September when SEC officials aired concerns that financial institutions were manipulating earnings reports.

PROXIES REJECTED. The conflict stemmed from the SEC's belief that banks were overstating loan loss reserves; bank regulators insisted that the reserves should be increased. When one bank holding company's proxy materials were rejected by the SEC with orders that reserves be reduced and earnings restated, the OCC and the Fed objected. The bank regulators claimed that problems in the world financial markets warranted higher reserves, and that banks should have the flexibility to adjust reserves as economic and credit conditions change.

JOINT AGREEMENT. The impasse ended with a joint statement by the SEC and regulators recognizing the need for "prudent, conservative, but not excessive" allowances that reflect estimated losses for specific problem loans and for the balance of the portfolio. It stressed the importance of accuracy for the benefit of investors, warning banks not to use the reserves to "manipulate earnings or mislead investors" or regulators.

DISCLOSURE REQUIRED. The joint statement calls for documentation supporting the amount of the allowance, identifying economic and other factors that may have an impact on the collection of the loans. The reasoning behind the allowance must be included in disclosures for investors.

STEPS TO TAKE. Olive's Credit Quality Assurance Group will review the adequacy of your loan loss reserves and supporting documentation. To learn more, contact John Bourquard at 317.383.3783 (e-mail: jbourqua@admin.olivellp.com). ●

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