

# NEWS



AN ELECTRONIC REPORT FROM THE CUNA CHIEF FINANCIAL OFFICER COUNCIL

## Improve the odds of success

**Ninth Annual CUNA CFO Council  
Conference and Roundtable**  
May 18-21, 2003  
Flamingo Hotel  
Las Vegas, Nevada

The Ninth Annual CUNA CFO Council agenda includes general and breakout sessions sure to be of great professional interest to members. The theme for this year's conference is *Improving the Odds of Success*.

### Features:

- Pre-conference workshop, Sunday, May 18: Gary Raddon, chairman, Raddon Financial Group, will facilitate a session on member, household, and product profitability;
- Golf tournament, Sunday, May 18: Dragon Ridge Country Club;
- Opening general session, Monday May 19: Bill Strickland, president & CEO, Manchester Craftsmen's Guild and The Bidwell Training Center will address *The Art of Leadership*: changing the reality of distressed communities through education, cultural development and social enterprise;
- Membership Recognition Luncheon, Monday, May 19: The awards ceremony recognizes individuals achieving five years of council membership for their long-term dedication and support to the council;
- Breakout sessions on cash management and long-term borrowing, incentive plans, top ten technology trends, investment strategies, risk-based examination processes, and current accounting issues;
- Mini-workshops on cost

accounting and ALM;

- Round-robin dinners;
- Special general session on the housing and mortgage market outlook;
- Roundtable discussions;
- Learning tracks on mortgage lending and starting up a business lending program;
- Closing general session, Wednesday, May 21: Humorist Simon Cotter.

*Improving the Odds of Success* is sure to be a memorable conference and roundtable. Don't miss this exceptional opportunity to network with your peers and other leaders in the credit union industry. ♦

*The conference agenda, hotel information, and registration form are available on the CFO council website under the Events tab.*



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## Scott Waite begins service on FASB Advisory Council

CUNA CFO Council chairman Scott Waite is already immersed in the weighty issues being addressed by the Financial Accounting Standards Advisory Council (FASAC). Waite, senior vice president and CFO for Patelco Credit Union in San Francisco, says he was invited to make a contribution from the start. "I began receiving background briefs immediately after my appointment, so that I could hit the ground running when my term began on January 1," says Waite.

The FASAC consists of thirty-three representatives from among the top tier of American business, academic, and accounting practitioners. Among them is the head of the U.S.

General Accounting Office (GAO), the comptroller general of the United States. It's a diverse representation through which the Financial Accounting Standards Board (FASB) receives guidance and advice.

FASB enters 2003 with some critical big-picture issues that set its agenda and priorities for the year. Prominent among those issues are provisions required under the Sarbanes/Oxley Act, which is intended to reform public company accounting and protect investors. "The Act identifies FASB as the standard-setting body for all public and private companies in the U.S.," says Waite. "The Act requires the Securities & Exchange Commission (SEC) to acknowledge FASB as its guiding standard-setter. That provides a much-needed clarity to the entire financial community."

The number-one item on FASB's agenda, says Waite, is restoring investor confidence. There is no single more important issue to deal with in 2003. To accomplish that goal, FASB has embraced a system called *fair value measurement*. Under fair value measurement, U.S. accounting standards will move toward having fair (market) value representation in financial statements. This means presenting

the financial position of every public and private company in the country as fairly and accurately as possible.

FASB will also look into the matter of aligning U.S. and international accounting standards, working with the International Accounting Standards Board. Currently, the U.S. has a rules-based system while the international community operates on a principles-based system.

"We are also dealing with special purpose entities (SPEs)," says Waite. "We're making rules on these entities right now, to address some of the abuses that came to light in the wake of the Enron collapse. SPEs are high on the list of rules in the works, to avoid similar problems in the future."

And the advisory council is dealing with stock-based compensation. The treatment of stock options has everybody's attention.

"In my role as a representative on the FASB Advisory Council," says Waite, "many of the issues we address will be directly related to credit union operations. We have just issued guidance to the AICPA on proposed changes to the treatment of credit losses. In this capacity, I will be serving as a point person for financial institutions in the group."

The only other financial institution representative on FASAC is the CFO of J.P. Morgan.

Waite describes his appointment to the advisory council as both an honor and a humbling experience. "When I was appointed, I realized what a great honor it was first to have the support and be nominated by CUNA, and then to achieve the appointment. Representing credit unions, I can give them a voice in some of the largest accounting issues that have faced this country in some time. Rules made today will forever change the way America does business. I am looking forward to what it can do for credit unions, and for my own professional development." ♦



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## AICPA will issue loan-loss reserve guidelines for public comment

CUNA has been closely monitoring the progress of the American Institute of Certified Public Accountants' (AICPA) proposal to clarify how Generally Accepted Accounting Principles (GAAP) apply to financial institutions' loan-loss reserves.

The AICPA's Accounting Standards Executive Committee (AcSEC) has been working on these guidelines for many years. According to AcSEC, the goal of the loan-loss reserve guidelines is to instill more discipline and less subjectivity in the establishment of the loan loss reserve.

On January 8, the Financial Accounting Standards Board (FASB) cleared the AICPA to release the draft guidelines, subject to the incorporation of several revisions, for public comment. The proposed Statement of Position (SOP), Allowance for Credit Losses, is expected out at the end of January or the beginning of February.

The following are the main directives of the draft guidelines, which would amend existing guidance in the AICPA Audit and Accounting Guide—*Certain Financial Institutions and Entities that Lend to or Finance the Activities of Others*:

- Avoid application of expected-loss models to pools of loans (the guidance will emphasize the incurred loss model);
- Eliminate cushions in the reserve;
- Make additional disclosures of credit data in financial statements.

Under the draft guidelines, "a creditor should group into pools, based on similar credit risk characteristics, loans other than those that were individually determined to be impaired. Those pools should be evaluated for collective loan impairment...." The draft guidelines would require creditors to specifically consider relevant observable data in the recognition and measurement of collective loan impairment. Components of collective loan impairment should be measured based on the present value of expected future cash flows.

Further, footnote disclosures would be required to help ensure that a creditor's credit

loss accounting is "directionally consistent with changes in the related observable data from period to period...."

The two areas in which AcSEC will revise the draft guidelines before they are issued as a proposed SOP are: (1) clarification of the definition of incurred losses versus expected future losses and (2) clarification of the use of historical data on losses to set up-to-date reserves for a given portfolio.

CUNA CFO Council Chairman, Scott Waite, chairman of CUNA's new Accounting Task Force and SVP-CFO of Patelco CU in San Francisco, will be involved with the task force in reviewing this issue which he says "has the potential to dramatically impact the financial statements of credit unions

and other financial institutions, particularly in terms of narrowing allowable cushions for credit losses."

Waite says that "FASB's approval of this draft in an important step forward in the narrowing of the considerably wide band of acceptable practice of accounting for credit

losses." Waite, who is just beginning his tenure as the first credit union representative ever to be appointed to FASB's Advisory Council, is "looking forward to assisting FASB in determining whether issues such as this one will get on FASB's agenda in the near future." He will also provide input as to the rule's final form.

Once AICPA has incorporated feedback from the public comments and approves the SOP, the SOP will go to FASB for final approval. If given final approval, the provisions of the SOP would be effective for financial statements for fiscal years beginning after December 15, 2003.

In light of the other guidance being developed that would affect loan-loss reserves, including efforts by the International Accounting Standards Board on loan-loss reserve rules and FASB's own fair (market) value accounting project, these draft guidelines may not become GAAP. ♦

*Catherine Orr*

*Senior Regulatory Counsel, Credit Union National Association*



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## The ABCs of ALLL

Many federally insured credit unions have voiced concern regarding how to comply with NCUA's new guidance on Allowance for Loan and Lease Losses (ALLL). ALLL is the amount required to be set aside based on each credit union's estimate of probable loan and lease portfolio losses.

There is continued flexibility in the new ALLL framework for management to determine the credit union's allowance and provision based on their judgment regarding the quality of the credit union's loan portfolio. Under the new guidance, credit union management is responsible for establishing an appropriate ALLL and documenting the methodology used.

Based on CUNA's analysis of the guidance as well as our recent audio conference call on this topic, here are some important points to keep in mind when determining your credit union's ALLL:

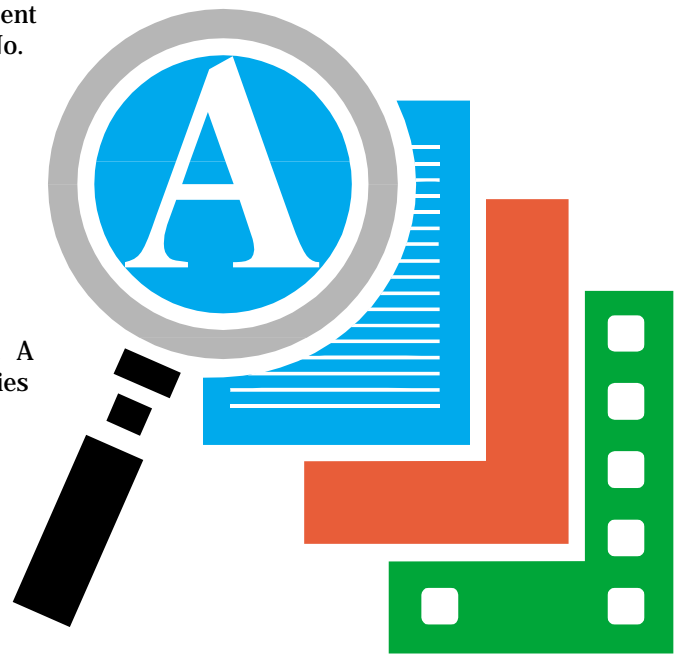
- The goal of the new framework is to have credit unions measure loan losses consistent with Generally Accepted Accounting Principles (GAAP). Therefore, there should not be significant changes in the ALLL assessment process for those credit unions that have been following GAAP.
- Under the incurred loss model of GAAP adopted by the new guidance, management should estimate losses on consumer loans on a pool basis (according to Statement of Financial Accounting Standards No. 5 [FAS 5], Accounting for Contingencies) and individually evaluate only large unique non-consumer loan that fall under FAS 114, Accounting by Creditors for Impairment of a Loan.
- A credit union's method for calculating its ALLL should take into account all factors that impact the loan portfolio's degree of credit risk. A key component of most methodologies is a credit classification process, which involves segmenting loans into risk categories. Each category should have common characteristics, such as past-due status and type of loan.
- It is crucial that management maintain written documentation of the logic behind the ALLL calculation—document how the credit

union came up with its loan pools, document how the loss factors were calculated, and document the relevant internal/external data regarding loan collectibility used to adjust those factors.

- The board of directors should have the methodology evaluated (including comparison of prior estimates of the allowance with subsequent results to assess the reliability of the process used to develop the allowance) on at least an annual basis and, if appropriate, revised. The guidance emphasizes the importance of independent review of management's methodology and documentation practices by the credit union's supervisory/audit committee or internal/external auditors. ♦

*For more information, please see CUNA's final analysis of the ALLL guidance in the Regulations and Compliance section of CUNA's website at <http://www.cuna.org>. Click on CUNA Final Rule Analysis, then NCUA Guidance on Allowance for Loan and Lease Losses.*

*Catherine Orr  
Senior Regulatory Counsel, Credit Union  
National Association*



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## HEARD IT ON THE LISTSERV

A listserv is a tool for discussions among and between council members. Get up-to-the moment information, make requests, post challenges, and share your experience with other council members. To join the listserv, click on the Community tab at the CUNA CFO Council web site, then on Listserv, and follow the directions to subscribe.

This month's hot topics and interesting conversations:

**Payroll processing:** Who in the credit union is responsible for employee payroll processing, accounting or human resources?

In the majority of responding credit unions, HR is responsible for payroll processing, some assign payroll to accounting. A strong accounting overview is necessary wherever the payroll is handled.

**GAP insurance:** Do you give incentives to your staff for GAP Insurance and/or GAP Plus policies sold? Some responses:

- Pay the loan officer \$25 per policy sold and the credit union \$120;
- Pay a \$25 incentive on each sale of GAP Plus, which reduces complaints about the amount of paperwork involved;
- Do not offer incentives for GAP, but may offer them in the future;
- Offer a sales commission of \$35 for every GAP sold;
- Structure incentives so that loan officers can earn more if they sell GAP in addition to credit life and disability instead of just one or the other.

**Educational & Promotional Expenses:** What's included in your credit union's educational and promotion expense budget? A majority of respondents, includes the following in their education/promotion expense budget:

- Product and service marketing;
- Awareness marketing;
- Annual reports;
- Website enhancements;
- R&D on new products and services;
- Charitable donations;
- Scholarships;
- Sponsorships;
- Seminars (e.g. ID fraud).

Some respondents include the following:

- The monthly contract fee for a MCIF software system;

- Annual report expenses in a separate category with annual meeting expenses;
- Postage expenses for marketing efforts, either in the educational and promotional expense budget, or as a separate line item;
- Website enhancements and all costs related to e-branch as a separate budget item;
- All costs related to the MCIF program;
- All e-branch related costs.

### **Accounting for defined contribution**

**retirement plans:** If an employee is 30 percent vested, does 3 percent of his salary accrue, or the full 10 percent? Responses:

- Fully fund the contribution. If the employee leaves before 100% vesting, there is a refund from the administrator of the pension;
- The accrual/contribution is 10 percent, and forfeitures are dealt with if and when the individual leaves employment;
- The answer often depends upon the specific wording of the employer's plan;
- The plan should provide an actuary statement that defines what the credit union should accrue for the year;
- In defined contribution plans, all contributions to the plan are expensed as they occur. If the employee decides to leave prior to full vesting, the expense is credited to the account for the unvested amount that is returned from the plan.

**VISA Debit Card transactions:** What do credit unions charge members for VISA Debit Card transactions? Responses:

- Don't charge for either debit or credit transactions. Card purchases - pin or credit - are less expensive for the credit union than check processing.
- Charge \$1- \$1.50 per transaction when used as a debit card and nothing when used as a credit card;
- Use different fees to motivate members to use the credit function, which generates higher interchange income than the debit function;
- Charge for pin-based transactions and keep signature-based transactions free because of the difference in income between swipe & sign transactions and swipe & pin transactions;
- Give members their first six ATM transactions per month, and then charge \$1 per

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transaction. PIN-based debit card transactions count against the limit. Signature-based transactions are always free;

- Implement a charge for pin-based transactions and send newsletter articles and flyers to all debit card members telling them how to avoid a fee. Talk to members when they come into the credit union to inform them of the difference.

**Merchant vs. credit union:** Some merchants steer their customers to use pin-based credit transactions rather than signature credit transactions. In Chicago, a major grocery chain is experimenting with requiring a manager's override at the register for signature debit card transactions. Signature transactions can't be prohibited, but the chain may be trying to make the process so inconvenient that people will give up and use their PIN instead. Some thoughts:

- Such a practice will backfire on the grocery store chain unless all other merchants follow suit. Supervisors will be frustrated by standing by to perform overrides, and all customers will be inconvenienced by having to

wait in line;

- Several stores in Michigan do employ the override policy. Signature based transactions require a manager's override, or the consumer must press the cancel button on the key pad, and the merchant enters a code in the terminal for the transaction to work as signature-based. Many terminals are programmed to ask for a pin number, including Nordstrom's;
- Reports from a VISA card conference show the override practice is becoming a trend that may result in lower income for credit unions;
- In California, more merchants are requesting ID's on all transactions to reduce fraud;
- The practice of requiring identification is against VISA regulations. The only ID required is comparing the signature on the back of the card with the one on the purchase document. If a merchant gets more information, including address and telephone number, they could purchase items on the consumer's card over the phone. ♦

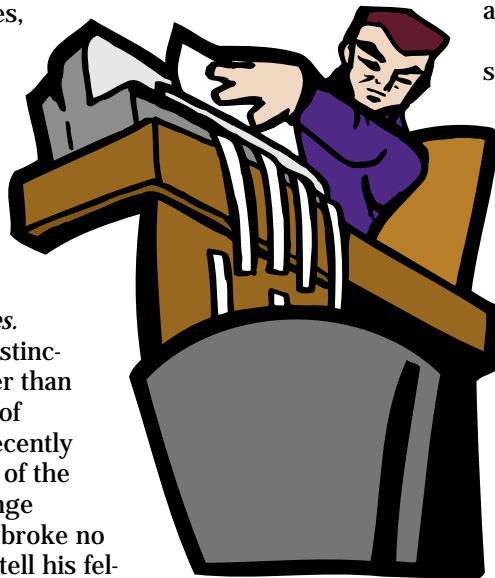
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## NEWS FROM OUTSIDE

### Will more rules yield better corporate behavior?

With all the recent corporate scandals, there's a temptation to call for new regulations and laws that will ensure no such malfeasance occurs again. Such directives, the thinking goes, will guide companies to be more ethical in their dealings. But the scandals are not so much a failure of laws and regulations as they are a failure of behavior, says Jeffrey L. Seglin in *The New York Times*.

Nowhere has this distinction been made clearer than in the recent exploits of Harvey L. Pitt, who recently resigned as chairman of the Securities and Exchange Commission. Mr. Pitt broke no law when he failed to tell his fel-



low S.E.C. commissioners that William H. Webster, his choice to be the chairman of a new accounting oversight panel, had headed the audit committee of a company now under investigation for fraud. Mr. Webster subsequently resigned from the new accounting oversight board.

When an outsider is being considered for a leadership position, those doing the considering should learn as much as possible about how that person has behaved in the past. Mr. Pitt had information that the S.E.C. commissioners might have found useful in making a judgment about Mr. Webster's ability to lead.

Serving on an audit committee of a company under investigation for fraud doesn't automatically indict Mr. Webster's leadership ability. But Mr. Pitt's decision not to disclose this critical piece of informa-

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tion was a behavioral and arguably an ethical lapse that should have been easy to avoid.

“You don’t legislate morality,” said David A. Nadler, the chairman of Mercer Delta Consulting in New York. “What we should be doing is expecting leaders of our companies to take responsibility for it.”

If we’re looking for fixes in corporate America to restore the public’s faith, says Seglin, we should ensure that the leaders put in place are those we know are of the highest integrity, whether it’s to lead the S.E.C. or any American company. ♦

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## WELCOME NEW MEMBERS

The CUNA CFO Council has added a total of sixteen new members this year. By joining their colleagues on the council, these individuals have demonstrated their commitment to developing superior skills. In addition, they join over 470 council members in networking for the free exchange of ideas and improving the overall effectiveness of their credit union’s financial operations.

**Russ R. Dalke**  
Mazuma CU  
Kansas City, MO

**Mark P. Magasic**  
FAA Eastern Region FCU  
Clark, NJ

**Edward A. Seidenberg**  
Harborstone CU  
Tacoma, WA

**Gary Dooley**  
LSI CU  
Grand Rapids, MI

**Thomas J. Martin**  
Arizona Central CU  
Phoenix, AZ

**Sandra E. Steele Riordan**  
AmeriCU CU  
Rome, NY

**Jeremy Kaufman**  
Community Choice CU  
Livonia, MI

**Shirley J. McKenney**  
General Mills FCU  
Minnetonka, MN

**Gerald J. Strausbaugh**  
USA FCU  
Troy, MI

**Julie A. Kreinbring**  
Huron River Area CU  
Ann Arbor, MI

**Renee Nelson**  
Oregon FCU  
Coquille, OR

**Jeanne L. Walkley**  
Honeywell FCU  
Minneapolis, MN

**Bohdan Kurczak**  
Self Reliance NY FCU  
New York, NY

**Richard G. Putrelo**  
Pittsford FCU  
Pittsford, NY

**Mark P. Labbe**  
Middlesex FCU  
Middletown, CT

**Janice Ringo**  
Ball State FCU  
Muncie, IN



CFO News is a web-based newsletter published bimonthly by the CUNA CFO Council. Send news and CFO Council information to Scott Waite, SVP/CFO, Patelco CU, San Francisco, CA, phone (415) 442-7158; fax (415) 442-7193 or Mike Lord, SVP/Comptroller, State Employees CU, Raleigh, NC, phone (919) 839-5084; fax (919) 839-5100. For council membership and administration information, call Pam Frey, manager of CUNA Council Administration, at 1-800-356-9655, extension 4141 or e-mail her at [pfrey@cuna.coop](mailto:pfrey@cuna.coop).

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