Statement of Position (SOP) No. 01-6 “Accounting by Certain Entities that Lend to or Finance the Activities of Others”

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On December 26, 2001, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position (SOP) No. 01-6 “Accounting by Certain Entities that Lend to or Finance the Activities of Others”. The purpose of this statement is to eliminate differences in accounting methods established by audit guides previously issued where such differences are not warranted. Most of the differences addressed by this SOP related to financial statement presentation and disclosure and may require changes to the current presentation of a credit union’s financial statements, while some changes will affect specific accounting treatments for all credit unions. The areas noted below address issues affecting most credit unions. The SOP does address other issues that may affect your credit union. For more information on how your credit union could be impacted, contact your auditor.

Recognition and Measurement

Credit Losses
Credit losses for loans, which may be for all or part of a particular loan, should be deducted from the allowance. The related loan balance should be charged-off in the period in which the loan receivable is deemed uncollectible. Recoveries of loans previously charged-off should be recorded when received.

Most credit unions are doing just as noted above; however, there are timing differences as to when a charge-off should be recorded. This SOP addresses this issue by stating the loan should be charged-off when deemed uncollectible either all or in part.

Federal Home Loan Bank or Federal Reserve Bank Stock
Federal Home Loan Bank (FHLB) and Federal Reserve Bank (FRB) stock should be classified as a restricted investment security, carried at cost, and evaluated for impairment. Both cash and stock dividends received on FHLB stock are reported as income. When evaluating stock for impairment, its value should be determined based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value.
National Credit Union Share Insurance Fund (NCUSIF)

Amounts deposited with the NCUSIF should be accounted for and reported as assets as long as such amounts are fully refundable. The refundability of NCUSIF deposits should be reviewed for impairment. When the refundability of a deposit is evaluated, the financial condition of both the credit union and of the NCUSIF should be considered.

Foreclosed and Repossessed Assets

Foreclosed and repossessed assets should be classified as a separate balance-sheet amount or included in other assets on the balance sheet with separate disclosures in the notes to the financial statements. This will require most credit unions to discontinue including repossessed vehicles as part of loans until time of the sale. The accounting treatment for collateral in process should now follow that of Other Real Estate Owned (OREO) property. This accounting treatment requires that when the asset is seized, an estimate of its net realizable value be determined. Any difference between the loan balance and the net realizable balance should be charged-off through the allowance for loan losses at that time. Subsequent losses should be shown as a non-operating loss on disposition of assets. Therefore, it is important to make good initial estimates of net realizable value. Gains on sales can be recorded as recoveries up to the amount of the original charge-off.

Presentation & Disclosure Requirements

Regulatory Capital

Noncompliance with regulatory capital requirements could materially affect the economic resources of a credit union and claims to those resources. Accordingly, credit unions are required to disclose in the notes to the financial statements a description of the regulatory requirements and the actual or possible effects of non-compliance with those requirements.

Effective Date

Changes in accounting and financial reporting required by this SOP should be applied prospectively and shall be effective for annual and interim financial statements issued for fiscal years beginning after December 15, 2001.

If you have any questions or need further information regarding SOP No. 01-6, call us at (800) 288-0293 or e-mail us at info@nearman.com.