



REGULATORY INTERPRETATION 2000-RI-06

Date: June 23, 2000

Subject: Accounting Issues: Independent Auditor's Review of Quarterly Financial Information

Request Summary:

This is an interpretation of 12 C.F.R. § 985.6(b)(1) and is issued in response to a final rule (Release No. 34-42266) adopted by the Securities and Exchange Commission (SEC) on December 22, 1999 (17 C.F.R. § 228.310, 64 Fed. Reg. 73389 (Dec. 30, 1999)).

Background:

On December 22, 1999, the SEC adopted a final rule (Release No. 34-42266) that, among other things, amends SEC Regulation S-X (17 C.F.R. part 210). The SEC rule, effective for fiscal quarters ending on or after March 15, 2000, requires that companies' independent auditors perform a review of financial information of SEC registrants in accordance with Statement of Auditing Standards 71 prior to the companies filing their quarterly reports on Form 10-Q or Form 10-QSB with the SEC. The SEC noted in their release that "the five largest U.S. accounting firms, the so-called 'Big 5,' and some other firms, currently have in place policies that require their clients to have interim reviews as a condition to acceptance of an audit." PricewaterhouseCoopers (PwC), the Federal Home Loan Bank (Bank) System's independent auditor, confirmed to Federal Housing Finance Board (Finance Board) staff that they, and the other Big Five accounting firms, now require such reviews for their publicly held clients.

On June 2, 2000, the Finance Board adopted a rule amending its regulations governing the operations of the Office of Finance. As part of that rulemaking, new section 985.6(b)(1) codifies existing Finance Board policy by requiring that the scope, form and content of the Bank System's combined financial reports be consistent with the requirements of the SEC's Regulations S-K and S-X (17 C.F.R. parts 229 and 210). In addition, section 989.3 of the Finance Board regulations requires each Bank to provide the preparer of the Bank System's combined quarterly financial reports with financial information and other information the preparer may request to facilitate the preparation of such reports.

Analysis or Discussion:

The SEC adopted the new rule to improve disclosure and to enhance the reliability and credibility of the financial statements of public companies. The SEC stated it believes

that more discipline is needed for the quarterly financial reporting process [and] that the reviews required will facilitate early identification and resolution of material accounting and reporting issues because the auditors will be involved earlier in the year. In addition, increasing the level of scrutiny by independent auditors of companies' quarterly financial statements should lead to fewer year-end adjustments, and, therefore more reliable financial information about companies throughout the reporting year.

Finance Board staff has determined that the quarterly reviews required by the new SEC rule represent current "best practice" for publicly held companies, and that this practice should be adopted by the FHLBanks.

Interpretation:

Effective with the second quarter of 2000, each Bank and the combined Banks shall comply with the SEC rule requiring quarterly reviews of financial information by independent auditors. The information to be reviewed by the Banks' independent auditor is the financial information the Banks provide to the preparer of the Bank System's combined quarterly financial reports as well as the resulting quarterly combined reports. These reviews by the independent auditor shall be conducted in accordance with the professional standards and procedures for conducting such reviews established by the American Institute of Certified Public Accountants.

<p>A <u>Regulatory Interpretation</u> applies only to the particular transaction or activity proposed by the requestor, may be relied upon only by the requestor, and is subject to modification or rescission by action of the Board of Directors of the Finance Board. 12 CFR part 907.</p>
