EM-33.3

Category: **Compliance**
Topic: **Financial & Shareholder Reporting**
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Overview

The Financial & Shareholder Reporting topic provides guidance on evaluating a Farm Credit System (System) institution's guidance and controls over financial and shareholder reporting processes. Institutions must provide financial information and other relevant disclosures to shareholders and FCA. These requirements are set forth in FCA Regulations, primarily in Parts 620 and 621. The purpose of the regulations is to ensure shareholders are provided with complete and accurate disclosure of all matters relating to the financial condition of the institution, enabling them to make informed decisions and take appropriate actions as necessary. These disclosures include the annual and quarterly reports to shareholders, annual meeting information statements, and notices to shareholders. In addition, each institution must provide FCA with quarterly Uniform Reports of Financial Condition and Performance (Call Reports).

FCA Regulations and Call Report instructions prescribe the preparation, filing, accuracy, and content requirements for each disclosure to shareholders and the quarterly Call Reports, respectively. FCA's FAQs About the Disclosure and Reporting Rule contain additional information and clarifications. Institutions must have effective financial reporting controls to comply with regulatory requirements. Incomplete, inaccurate, or misleading disclosures on the part of any institution, employee, director, or director nominee are prohibited. If examiners identify incomplete or erroneous disclosures, they can require the institution to make additional or corrected disclosures.

Examination Procedures and Guidance

General

1. Annual Report:

Determine if the annual report to shareholders complies with regulatory disclosure requirements and adequately informs shareholders of the institution's financial condition and results of operations.

Guidance:

Institutions must prepare comprehensive annual reports on their financial condition, results of operations, and related disclosure items for distribution to shareholders and investors. FCA Regulations identify specific requirements for annual report preparation, filing, accuracy, and content. General expectations are summarized below (refer to the regulations for additional details).

- FCA Regulations 620.2 and 620.4 require institutions to prepare and provide annual reports to shareholders and FCA according to the instructions contained in Part 620 of the regulations. Additional guidance on the filing requirements is provided in an Informational Memorandum on Instructions for Filing Part 620 Reports with FCA dated February 7, 2008. Each institution must submit an electronic copy of its annual report to FCA within 75 calendar days after yearend and post a copy of the report on its website when it is submitted to FCA. Within 90 days after yearend, institutions must provide shareholders a copy that is substantively identical to the report submitted to FCA. Refer to FCA's Informational Memorandum on Maintaining and Using Stockholder Lists dated February 4, 2021, for additional guidance on distributing the report to shareholders.

- FCA Regulation 620.3 requires that annual reports not be incomplete, inaccurate, or misleading. For those institutions with over $1 billion in assets, the report must include management's assessment of internal controls over financial reporting. Each report must be dated and signed by the chief executive officer (CEO), chief financial officer (CFO), and a board member, with the signatories certifying the report's financial accuracy.

- FCA Regulation 620.5 requires annual reports to contain the following items in substantially the same order:

    - Description of business
    - Description of property
    - Legal proceedings and enforcement actions
    - Description of capital structure
    - Description of liabilities
    - Selected financial data
    - Management discussion and analysis of financial condition and results of operations
    - Directors and senior officers
    - Relationship with qualified public accountant
    - Financial statements
    - Credit and services for young, beginning, and small (YBS) borrowers

- FCA Regulation 620.6 requires disclosure of director and senior officer compensation in the annual report. Associations have the option to disclose senior officer compensation in the annual meeting information statement. Refer to the *Compensation Disclosures* and the *Bank Director Compensation* sections in FCA's FAQs About Governance Changes in 2006 for additional information and clarifications. The regulation also requires disclosures of other items, such as involvement in legal proceedings and transactions with directors and senior officers.

- FCA Regulations 628.61, 628.62, and 628.63 establish public disclosure requirements for each bank related to the capital requirements in Part 628.

- FCA Bookletter BL-074 – Sound governance of wholesale funding and related processes outlines regulations that require accurate disclosure of wholesale funding arrangements between banks and associations, and the System's overall asset/liability management practices.

Refer to FCA's *Annual Report to Shareholders* workpaper for additional guidance and information (see Part 3 of the Examination Manual).

2. Quarterly Report:

Determine if quarterly reports to shareholders comply with regulatory disclosure requirements and adequately inform shareholders of the institution's financial condition and results of operations.

Guidance:

A quarterly report is a document required by FCA Regulations reporting on an institution's financial results for the quarter and noting any significant changes or events. Quarterly reports contain unaudited interim financial statements and management's discussion and analysis, and may include disclosures on significant or material events that have occurred. FCA Regulations identify specific requirements for quarterly report preparation, filing, accuracy, and content, as summarized below (refer to the regulations for additional details).

- FCA Regulations 620.2 and 620.10 require institutions to prepare and provide quarterly reports to shareholders and FCA according to the instructions contained in Part 620 of the regulations. Additional guidance on the filing requirements is provided in an Informational Memorandum on Instructions for Filing Part 620 Reports with FCA dated February 7, 2008. Each institution must submit an electronic copy of its quarterly report to FCA within 40 calendar days of quarter-end. When the institution submits the report to FCA, it must also post a copy on its website.

- FCA Regulation 620.3 requires that quarterly reports not be incomplete, inaccurate, or misleading. For those institutions with over $1 billion in assets, the report must disclose any material change(s) in the internal control over financial reporting occurring during the reporting period. Each report must be dated and signed by the CEO, CFO, and a board member, with the signatories certifying the report's financial accuracy.

- FCA Regulation 620.11 requires quarterly reports to contain interim financial statements, a Management Discussion and Analysis section, and other related financial items. They may also include notices required under FCA Regulation 620.15.

- FCA Regulations 628.61, 628.62, and 628.63 establish public disclosure requirements for each bank related to the capital requirements in Part 628.

Refer to FCA's *Quarterly Report to Shareholders* workpaper for additional guidance and information (see Part 3 of the Examination Manual).

3. AMIS:

Determine if the annual meeting information statement (AMIS) complies with regulatory disclosure requirements.

Guidance:

An AMIS is a document informing eligible shareholders of the institution's annual meeting in which shareholders are asked to vote on director or Nominating Committee positions, and may include other voting topics such as mergers. The statement is essentially an invitation which includes the date, time, location, and disclosure information for the annual shareholder meeting. FCA Regulations identify specific requirements for AMIS preparation, filing, accuracy, and content. General expectations are summarized below. Refer to the regulations, other documents listed below, and the *Director Elections and the AMIS* section in FCA's FAQs About Governance Changes in 2006 for additional details and guidance.

- FCA Regulations 620.2 and 620.20 require institutions to prepare and provide an AMIS to shareholders and FCA according to the instructions contained in Part 620 of the regulations. Additional guidance on the filing requirements is provided in an Informational Memorandum on Instructions for Filing Part 620 Reports with FCA dated February 7, 2008. The AMIS must be provided to shareholders and FCA at least 10 business days, but not more than 30 business days, before an annual meeting or director election. Refer to FCA's Informational Memorandum on Maintaining and Using Stockholder Lists dated February 4, 2021 and FAQs About Governance Changes in 2006 #35, for additional guidance on distributing the AMIS to shareholders. When issued, the institution must provide an electronic copy to FCA. Institutions may post the AMIS to their website (not required) and, if so, it must remain on the website for at least 30 calendar days. Also, the statement must be available for public inspection at the institution's offices.

- FCA Regulation 620.3 requires that the AMIS not be incomplete, inaccurate, or misleading. Each AMIS must be dated and signed by the CEO, CFO, and designated board member. Refer to questions 8A, 8B, and 8C in FCA's FAQs About the Disclosure and Reporting Rule for information on signature and certification expectations.

- FCA Regulation 620.6 allows associations to disclose senior officer compensation in either the annual report or AMIS.

- FCA Regulation 620.21 requires disclosure in the AMIS of the annual meeting date, time, location, and venue (online or at a physical location). Other standardized disclosures include financial updates, identifying the number of shareholders entitled to vote, information on existing board members, director-nominee disclosure information collected under FCA Regulation 611.330, and other voting items.

Refer to FCA's *Annual Meeting Information Statement* workpaper for additional guidance and information (see Part 3 of the Examination Manual).

4. Call Report:

Determine if quarterly Call Reports are accurate and comply with applicable regulatory requirements and instructions.

Guidance:

Call Reports provide FCA and other interested persons with information about the financial condition, results of operations, and various other activities of institutions. FCA Regulations identify the general requirements for submission of Call Reports. These requirements are summarized below (refer to the regulations for additional details).

- FCA Regulation 621.12 requires institutions to submit electronic Call Reports to FCA as of each quarter-end in accordance with FCA instructions. The instructions require banks to file Call Reports within 20 days after quarter-end. Associations and service corporations must file by the last day of the month following quarter-end.

- FCA Regulation 621.13 requires institutions to prepare their Call Reports in accordance with generally accepted accounting principles (GAAP) and FCA instructions and procedures.
- FCA Regulation 621.14 requires Call Reports to be certified as correct by an officer of the institution who has been named for that purpose by action of the board or, if no such person has been named, the president or CEO.
- FCA Regulation 621.15(a) requires institutions to prepare and submit reports of accounts and exposures to the Reporting Entity (the Federal Farm Credit Banks Funding Corporation). The reports must be accurate, complete, timely, and prepared in accordance with FCA instructions. In addition, the institution must provide a written certification to the Reporting Entity and respond to questions from the Reporting Entity. The Reporting Entity maintains the certifications for FCA's review, so the institution does not file certifications directly with FCA. However, the institution should retain a copy. The regulation also requires the institution to develop, implement, and maintain an effective system of internal controls over the data. Examiners should evaluate the adequacy of these controls as part of examination work in the *Security* procedure within the *Information Technology and Security* Examination manual topic. Note: Refer to FCA Regulation 621.15(b) for specific Reporting Entity (Funding Corporation) requirements, including policy, procedure, and internal control expectations.

FCA provides instructions for preparing and filing Call Reports on its website. In addition to providing guidance for each Call Report line item, there is a General Instructions section that covers requirements for preparing, verifying, certifying, filing, revising, and retaining Call Reports. The Call Report spreadsheet also has a Difference Report that can be used as part of cross-checking data before submission.

FCA relies on the data provided through the Call Report system to make decisions and publish periodic reports regarding System institutions. As such, it is critical for Call Reports to be submitted in a timely manner and to accurately present the condition and performance of each institution. All items reported on the Call Report must reflect appropriate adjusting and closing entries to the reporting institution's financial records. If any material errors are discovered, the institution must file a corrected copy. Also, it is important that institutions keep the *Institution Profile* information current as FCA uses this information for several purposes.

5. Financial Reporting Controls:

Evaluate the adequacy of policies, procedures, audits, and other internal controls to ensure accurate and complete financial reporting and compliance with GAAP and applicable regulatory requirements.

Guidance:

The accuracy and completeness of an institution's financial and shareholder reporting is dependent on the effectiveness of its financial reporting control processes. FCA Regulation 621.3 requires each institution to prepare and maintain, on an accrual basis, accurate and complete records of its business transactions as necessary to prepare financial statements and reports, including reports to FCA, in accordance with GAAP. Furthermore, an institution must prepare and maintain its books and records in a manner that facilitates reconciliation with financial statements and reports prepared from them. Effective controls help ensure that disclosure information is complete and accurate, financial statements are reliable, and the reports comply with GAAP, laws, and regulations.

Evaluative questions and items to consider when examining financial reporting controls include:

- ***Audit Committee:*** **Has the board's Audit Committee provided effective direction and oversight of financial reporting?** As outlined in FCA Regulation 620.30, the Audit Committee must oversee management's preparation of the report to shareholders; review the impact of any significant accounting and auditing developments; review accounting policy changes relating to preparation of financial statements; and review annual and quarterly reports prior to release. In addition, the Audit Committee must oversee the institution's system of internal controls relating to preparation of financial reports, including controls relating to the institution's compliance with applicable laws and regulations. The Audit Committee also serves as a knowledgeable authority with which internal and external auditors can discuss financial reporting issues and concerns. This committee must include any director designated as a financial expert. In addition, if the institution hires a financial expert advisor, that advisor will also serve as an advisor to the Audit Committee. Refer to the *Audit Committee* procedure in the *Audit & Review Programs* Examination Manual topic for more comprehensive guidance on examining audit committees. (Note: FCA Regulation 630.6 requires the Funding Corporation to have a System Audit Committee.)

- ***Management Assessment:*** **Has management completed a thorough assessment of internal controls over financial reporting?** FCA Regulation 620.3 requires that annual reports of those institutions with over $1 billion in total assets (as of the prior fiscal yearend) must include a report by management assessing the effectiveness of internal control over financial reporting. The assessment must be conducted during the reporting period and be reported to the board. Quarterly and annual reports for those institutions with over $1 billion in total assets must also disclose any material change(s) in the internal control over financial reporting occurring during the reporting period.

- ***Policies, Procedures, and Processes:*** **Are adequate policies, procedures, and processes in place for financial reporting?** Policies and procedures that communicate financial and shareholder reporting requirements serve as an important control to ensure financial statements are accurate and disclosures to shareholders and FCA include all required information. Examples of items to consider when evaluating the adequacy of policies, procedures, and processes for financial and shareholder reporting include:

    - Do policies and procedures include the expectations, delegations, responsibilities, and steps for developing, approving, and distributing shareholder and Call Reports? If there is no board policy, the process should be sufficiently documented by some other means. However, FCA Regulations specifically require institutions to have board policies in the following areas related to financial reporting:

        - FCA Regulation 620.15(a) – notices of significant or material events.
        - FCA Regulation 621.30 – engagement of external auditors.
        - FCA Regulation 628.62(b) – banks must maintain a policy on internal controls over capital disclosures.
        - FCA Regulation 630.4(a) – Funding Corporation must maintain written policies and procedures to be carried out by the disclosure entities for preparation of the report to investors.

    - Are internal controls sufficient to ensure the institution addresses all key items in the reports and meets regulatory requirements? Typical practices include having segregation of duties, using checklists and templates, requiring verification of data by someone other than the preparer, and cross-training staff to allow reports to be completed when the main preparer is absent. Additionally, the Institute of Internal Auditors Three Lines Model can help institutions identify organizational structures and processes to facilitate a strong internal control environment.

  - Is supporting workpaper documentation maintained and does it include the certifications, general ledger, loan trial balance, and other documents for support of numbers in the financial statements and Call Reports? The Call Report instructions identify guidance on these items, including a required retention period of 10 years for Call Reports and the certifications.

- ***Systemwide Disclosure Program:*** **Is an effective internal controls over financial reporting (ICFR) program in place to fulfill entity-level reporting as required by the general financing agreement with the bank and the System's Funding Corporation Disclosure Program?** To achieve System-level attestation, the Funding Corporation annually determines the significant accounts, disclosures, and business processes and cycles that impact System-level financial statements. This approach requires management at each institution to formally document its risk assessment and identification of the key controls over significant accounts, disclosures, and business processes and cycles each year. Additionally, management should identify key applications, systems, and databases that support significant processes. The Audit Committee should maintain oversight and have an understanding of the ICFR program. Management is responsible for the control environment and implementation of the ICFR program. Internal audit may be involved in ICFR testing. Individuals assigned to test key controls should have an appropriate level of competence, objectivity, and independence. Control testing should be consistent with population sizes, timing and frequency of the control, and risk associated with a control breakdown. Processes for the evaluation of control deficiencies should evidence a complete understanding of the nature and implications of the deficiency and its potential impact on the financial statements. The System ICFR workgroup designed a practice aid and toolkit to assist institutions in maintaining compliance with regulatory requirements related to ICFR and to strengthen the disclosure program. FCA regulations do not require institutions to adopt or utilize the System toolkit. However, if an institution chooses not to use the documents provided in the toolkit, it should have comparable tools in place to document compliance with the disclosure program. As part of the ICFR process, and described in the Funding Corporation's annual scoping memo to all System institutions, each institution is responsible for, but not limited to, the following:

  - Designing disclosure controls and procedures with respect to material financial information.

  - Evaluating the effectiveness of those disclosure controls and procedures.

  - Designing ICFR to provide reasonable assurance regarding the reliability of financial information in accordance with GAAP.

  - Documenting the institution's processes underlying significant accounts and disclosures from initiation through completion of the financial reporting process.

  - Documenting the institution's controls in accordance with the 2013 Committee of Sponsoring Organizations of the Treadway Commission framework.

    - Identifying the key controls within the significant processes.
    - Testing the key controls that have been identified. This step includes designing and executing a test plan and retaining documentation of testing performed and related results.
    - Evaluating all identified control deficiencies for significance and classification as one of the following:
        - Control deficiency
        - Significant deficiency
        - Material weakness
    - Developing a remediation plan for all identified control deficiencies regardless of classification of significance.
    - Reporting all identified control deficiencies, significant deficiencies, and material weaknesses to it's funding bank and, ultimately, the Funding Corporation through the Summary of Aggregated Deficiencies report. A sound practice is to report all deficiencies to the institution's Audit Committee.

  Note: ICFR program effectiveness is closely tied to controls in other areas, such as credit administration, allowance for losses, segregation of collateral evaluation duties, and access controls to electronic data. Refer to the applicable Examination Manual topics (*Credit Administration*, *Allowance for Losses*, *Collateral Risk Management*, and *Information Technology & Security*, respectively) for information on examining internal controls in these areas and consider examination results in these areas when concluding on the adequacy and effectiveness of the ICFR program.

- ***External Audit:* Has a qualified, independent accountant (as defined in FCA Regulation 619.9270) audited the financial statements? Were any material concerns identified?** FCA Regulation 621.4 requires each institution, at least annually, to have its financial statements audited by a qualified public accountant in accordance with generally accepted auditing standards. The qualified public accountant's opinion of the financial statements must be included as a part of the annual report to shareholders. If an institution disagrees with the accountant's opinion on the financial statements, or if there is a change in the accountant engaged to audit the financial statements, additional disclosures are required and FCA must be notified. Also, FCA Regulations in Part 621, Subpart E include specific requirements on auditor independence. Furthermore, Public Company Accounting Oversight Board Auditing Standard 1305.04 requires all significant deficiencies and material weaknesses be reported to management and the institution's Audit Committee.

6. Audit:

Determine if the institution conducts an effective audit (scope, reporting, and followup) of financial and shareholder reporting.

Guidance:

The internal audit and review program is a key mechanism for ensuring financial and shareholder reporting is accurate and complies with regulations, and the reporting process is functioning effectively. The internal auditor or other qualified, independent party should review financial and shareholder reporting processes to ensure compliance with applicable criteria. The audit risk assessment and scope should address financial reporting topics, and audit or review frequency should be commensurate with the complexity of the institution's operations and risk profile. The potential impact of unreliable reporting supports the need for strong detective controls in the form of internal audit coverage.

Note: This procedure focuses on evaluating the reliability and effectiveness of internal audits and reviews in this topical area. Refer to the *Audit & Review Programs* topic in the Examination Manual for guidance on examining the overall internal audit and review program.

Evaluative questions and items to consider when examining the audit or review of financial and shareholder reporting include:

- ***Audit Coverage:*** **Is there periodic audit or review coverage of financial and shareholder reporting processes?** Audit or review coverage and frequency should be appropriate relative to risks, changes in the operating environment, regulatory requirements, and periodic testing needs. Coverage should also be consistent with the institution's risk assessment results and annual audit plan.

- ***Scope and Depth:*** **Are audit or review scope and depth sufficient to conclude on the accuracy, completeness, and timeliness of financial and shareholder reporting?** The scope and depth of work, including transaction testing, should cover the primary processes and controls within the area being audited or reviewed and be sufficient to determine if internal controls are functioning as intended and regulatory requirements are met. The scope and depth of coverage should be documented and consistent with the approved audit or review plan and engagement contract (if applicable). Audit or review workpapers should be examined to verify the actual scope and depth of work performed. The workpapers may indicate the scope and depth deviated from what was identified (or implied) in the audit plan. For example, workpapers may indicate the work performed was limited to evaluating the existence of policies and procedures and didn't include reviewing other controls, such as training or reporting, or testing compliance with regulations or institution guidance. If the work deviated materially from the original planned scope, internal audit should notify the board (or Audit Committee, if so delegated) of the reasons for the change. Specific items that should be considered in the audit or review scope include:

    - Financial and shareholder reporting (including FCA call reporting) policies and procedures.

    - Compliance with financial and shareholder reporting-related policies, procedures, accounting requirements, bank or Funding Corporation direction, FCA Regulations, and other FCA guidance.

    - Monitoring and control processes (e.g., reporting, management oversight, delegated authorities, separation of duties, management information systems and data).

    - Fraud-related threats and vulnerabilities, as well as anti-fraud controls.

- ***Reliability of Results:*** **Did FCA identify any concerns with audit or review reliability?** It is important to understand the scope and depth of the audit or review being examined, as discussed above, when evaluating audit or review reliability. With this understanding, the following are key considerations when evaluating the reliability of audit or review results:

- *FCA Testing* – Evaluate the reliability of internal audit or review work by comparing the results to FCA's examination results in this area. This comparison often includes FCA testing transactions that were covered in the internal audit or review (transactions are often loans or loan applications, but may include other types of transactional activity, as well). In addition to the audit or review report, examiners should request and review the workpapers and hold discussions with the auditor to obtain a more thorough understanding of work completed. This can be especially important if the audit or review report is not sufficiently detailed or FCA's examination work and testing identifies potential concerns. Auditors and reviewers complete line sheets, flowcharts, control matrices, standard work programs, workpaper forms, or other relevant audit evidence when conducting and supporting their work. (IIA Standards 2240, 2300, 2310, and 2320) Workpapers should adequately document the work performed and support the final report. If FCA identifies weaknesses that were not identified in the audit or review, the cause for any discrepancy should be determined.

- *Audit/Review Staffing* – Whether internal or outsourced, auditors and reviewers conducting the work need to be qualified, independent, and objective to ensure reliable results. They should have the right mix of knowledge, skills, and other competencies needed to perform the work. (IIA Standard 2230) Additionally, auditors and reviewers need to be independent of the activities they audit so they can carry out their work freely and objectively. (IIA Standards 1100, 1112, 1120, and 1130) For example, audit and review staff should not be involved in developing and installing procedures, preparing records, operating a system of internal controls, or engaging in any other activity that they would normally review. Examiners should evaluate the staffing on the individual audit or review being examined as part of determining the reliability of results.

- *Institution Review of Work Performed* – The institution should complete an independent review of the workpapers to ensure audit or review objectives and scope were met and the results and conclusions were reliable and supported. (IIA Standard 2340) Examples could include a supervisory review of in-house audit work by the Chief Audit Executive (CAE) or other audit staff, or a review of outsourced work by the CAE or audit coordinator. Examiners should consider whether the institution completed these reviews, and if any concerns were identified, when concluding on audit or review reliability.

- ***Reports:* Does the internal audit or review report sufficiently communicate financial and shareholder reporting review results and recommendations, if applicable?** Examiners should consider the following when evaluating the audit or review report:

    - Is the report prepared and communicated in accordance with the institution's guidelines?

    - Is an executive summary or overview included to provide the board with a general conclusion on audit or review results?

    - Is the report accurate, concise, supported, and timely in communicating the audit or review objectives, scope, results, conclusions, and recommendations? (IIA Standards 2330, 2400, 2410, 2420, 2440, and 2450)

- Are conclusions and recommendations realistic and reasonable, with material and higher risk issues clearly identified and prioritized?
- Are conclusions and recommendations supported by convincing evidence and persuasive arguments (condition, criteria, cause, and effect)?
- Do results in the workpapers align with report conclusions?
- Does the report conclude whether the institution adheres to policies, procedures, and applicable laws or regulations, and whether operating processes and internal controls are effective?
- Does the report address potential vulnerabilities to fraud, if applicable?

- ***Corrective Action:*** **Are management responses to audit or review findings in this area reasonable, complete, and timely? Have corrective actions been effective?** Audits and reviews are only effective if corrective action is taken to remedy the weaknesses identified. As such, there should be a reasonable, complete, and timely management response to the audit or review report. Management commitments and agreements or any areas of disagreement should be documented in the report or in a separate memo or tracking system. (IIA Standards 2500 and 2600) If corrective actions are not resolving the issues or concerns in a timely manner, examiners should further investigate the reasons. For example, this could indicate the audit or review did not sufficiently identify the underlying causes or materiality of weaknesses, sufficient resources are not being directed toward corrective actions, or weaknesses exist in the institution's corrective action process, including board oversight of the process.