

Federal Reserve Bank of San Francisco
101 Market Street, San Francisco, California 9410

January 4, 2007

**BANKING SUPERVISION AND REGULATION:
INTERAGENCY POLICY STATEMENT**

To State Member Banks, Bank
Holding Companies, U.S. Branches
and Agencies of Foreign Banks,
and Others Concerned,
in the Twelfth Federal Reserve District

Interagency Policy Statement on the Allowance for Loan and Lease Losses

The federal financial regulatory agencies announced the issuance of a new interagency policy statement on the Allowance for Loan and Lease Losses (ALLL), and supplemental Frequently Asked Questions (FAQs). The agencies believe an assessment of the appropriateness of the ALLL is critical to the safety and soundness of a financial institution, especially in today's uncertain economic environment and when concentrations in untested loan products are present. The policy statement has been updated to ensure consistency with generally accepted accounting principles (GAAP) and post-1993 supervisory guidance.

The revised policy statement updates this guidance and extends it to credit unions and their examiners, as well as reiterates key concepts and requirements included in GAAP and existing ALLL supervisory guidance. The ALLL represents one of the most significant estimates in an institution's financial statements and regulatory reports. Because of its significance, each institution has a responsibility for developing, maintaining and documenting a comprehensive, systematic, and consistently applied process appropriate to its size and the nature, scope, and risk of its lending activities for determining the amounts of the ALLL and the provision for loan and lease losses.

Consistent with longstanding supervisory guidance, institutions must maintain an ALLL at a level that is appropriate to cover estimated credit losses on individually evaluated loans determined to be impaired as well as estimated credit losses inherent in the remainder of the loan and lease portfolio. Estimates of credit losses should reflect consideration of all significant factors that affect the collectibility of the portfolio as of the evaluation date. Arriving at an appropriate allowance involves a high degree of management judgment and results in a range of estimated losses. Accordingly, prudent, conservative, but not excessive, loan loss allowances that represent management's best estimate from within an acceptable range of estimated losses are appropriate.

In addition to the revised policy statement, the agencies are issuing sixteen FAQs to assist institutions in complying with GAAP and the ALLL supervisory guidance.

Additional Information

All circulars and documents are available on the internet through the Federal Reserve Bank of San Francisco's website, at <http://www.frbsf.org/banking/letters>.

For additional information, please contact our Banking Supervision and Regulation Department at (415) 974-2225.

FEDERAL RESERVE BANK OF SAN FRANCISCO

Attachment: [Interagency Policy Statement
Questions and Answers on ALLL](#)