Board of Governors of the Federal Reserve System

Supplemental Instructions **March 2004**

Editing of Data by Respondents

On December 15, 2003, the Federal Reserve announced in the *Federal Register* proposed changes to the FR Y-9 series that will require validation checks to be performed by respondents as part of the electronic submission process. This change will be implemented as of September 30, 2004, for the FR Y-9C and LP reports and will require that your bank holding company (BHC) perform published validity and quality checks on your data (so-called edits) by the filing deadline. Although this change has similarities to the Call Report Modernization Initiative, this effort is separate and distinct from that initiative, and it has different technical requirements.

Currently, after the Federal Reserve receives a BHC report, it is subjected to validation checks to assess the accuracy and reasonableness of the data submitted. If this validation process identifies any edit exceptions in a BHC's report, a Federal Reserve analyst may contact the BHC and ask for clarification of the data associated with these edit exceptions. The BHC must then provide revised data or explanatory comments concerning edit exceptions.

Under the new system, all BHCs must submit their FR Y-9 reports via the Federal Reserve's internet submission facility, IESUB, using either data entry or file transfer. This data collection system will subject a BHC's electronic data submission to the published validity and quality edit checks and transmit the results of such checks to the BHC shortly thereafter. The BHC will then be expected to correct its report data to eliminate any validity edit exceptions. The BHC will also be provided a method for supplying explanatory comments concerning quality edit exceptions. These explanatory comments will be held confidential. Your BHC's report must be free of any validity edit failures and include any explanations of quality edit failures at the filing deadline. Reports that contain validity edit failures or have quality edit failures that are not explained on or before the filing deadline will be deemed late.

Companies that offer computer software to aid in the preparation of FR Y-9 reports or BHCs that have developed their own reporting software may also choose to incorporate validity and quality edit checks into their software. The Federal Reserve will provide technical specifications in May 2004.

Overall these changes are expected to reduce the number of inquiries you receive from the Federal Reserve Bank analysts and improve the timeliness and quality of BHC data. As additional information comes available, we will forward it to your holding company. The Federal Reserve will also provide updates about the enhanced IESUB submission process on the web site: *www.reportingandreserves.org* under the heading BHC Modernization project.

Accelerated Filing Deadline

The Board approved the acceleration of the filing deadline for ***top-tier*** FR Y-9C filers and will follow the SEC's phased-in approach by implementing a 40-day deadline in June 2004 and a 35-day deadline in June 2005. The new filing deadlines apply for the March, June, and September report dates. The December filing deadline for top-tier FR Y-9C filers will remain at 45 days after the report date.

The 40-day deadline for filing the June 30, 2004, report will be August 11, 2004.

The 35-day deadline is defined as "5 business days after the 30th day after the report date" to allow time for integration of bank data in the event that the 30th day falls on a weekend. For example, the 30th day after the June 30, 2005, report date is Saturday, July 30. The 35-day deadline will be Friday, August 5, 2005.

The FR Y-9LP, FR Y-9SP, FR Y-9ES and all lower-tier bank holding companies that file the FR Y-9C are not subject to the accelerated deadline. The deadline for these reports will remain at 45 days after the report date.

FASB Interpretation No. 46

The FASB issued Interpretation No. 46 (Revised), *Consolidation of Variable Interest Entities*, in December 2003. Revised interpretation No. 46 replaces interpretation No. 46, which was issued in January 2003. This interpretation explains how to identify a "variable interest entity" (previously referred to as a "special purpose entity") and how an organization should assess its interests in a variable interest entity to decide whether to consolidate that entity. Variable interest entities often are created for a single specified purpose, for example, to facilitate securitization, leasing, hedging, research and development, and reinsurance. Most small bank holding companies (BHCs) are unlikely to have any "variable interests" in variable interest entities.

In general, a variable interest entity is an entity in which either the controlling financial interests are not voting interests or the equity investors do not bear the entity's residual economic risks. A variable interest is a contractual or ownership interest in an entity that changes when the value of the entity's net assets changes. An organization that has a variable interest (or a combination of variable interests) that will absorb a majority of a variable interest entity's expected losses if they occur, receive a majority of the entity's expected residual returns if they occur, or both, is the "primary beneficiary" of the variable interest entity and must consolidate it.

For FR Y-9C purposes, bank holding companies with variable interests in variable interest entities must apply the provisions of Interpretation No. 46 (Revised) to those entities in accordance with the interpretation's effective date and transition provisions, a summary of which follows. Special provisions of the revised interpretation apply to organizations that have fully or partially applied Interpretation No. 46 prior to the issuance of the revision. Otherwise, application of the revised interpretation (or Interpretation No. 46) was required of bank holding companies that are public companies, or subsidiaries of public companies, that have interests in

variable interest entities or potential variable interest entities commonly referred to as special-purpose entities beginning December 31, 2003. Application of Interpretation No. 46 (Revised) by bank holding companies that are public companies (other than small business issuers), or subsidiaries of such public companies, for all other types of variable interest entities is required beginning March 31, 2004. Application of Interpretation No. 46 (Revised) by bank holding companies that are small business issuers, or subsidiaries of small business issuers, to variable interest entities other than special-purpose entities is required beginning December 31, 2004. Application of Interpretation No. 46 (Revised) by bank holding companies that are neither public companies nor subsidiaries of public companies is required immediately for variable interest entities created after December 31, 2003, and for all other variable interest entities at the beginning of the first fiscal year beginning after December 15, 2004 (January 1, 2005, for calendar year bank holding companies).

The assets and liabilities of a consolidated variable interest entity should be reported on the FR Y-9C balance sheet (Schedule HC) on a line-by-line basis according to the asset and liability categories shown on the balance sheet. This reporting treatment also carries over to the other schedules in the FR Y-9C.

Reporting of Trust Preferred Securities

The Federal Reserve modified the definition of Schedule HC, Balance Sheet, item 20, "Other liabilities," and Schedule HC-G, Other Liabilities, item 4," Other," to include information on trust preferred securities. This information will no longer be included in Schedule HC, item 22, "Minority interest in consolidated subsidiaries and similar items." BHCs are advised that this reporting change does not represent any change to the risk-based capital treatment for trust preferred securities. Consistent with guidance previously provided in Federal Reserve Supervisory Letter SR 03-13 of July 2, 2003, BHCs should continue to include eligible trust preferred securities in their tier 1 capital for regulatory capital purposes until further notice is given to the contrary. The amounts qualifying for inclusion in tier 1 capital should be reported in Schedule HC-R, Regulatory Capital, new item 6(b), "Qualifying trust preferred securities," in accordance with the reporting instructions. Current Schedule HC-R, item 6, "Qualifying minority interests in consolidated subsidiaries" has been renumbered as item 6.a. The Federal Reserve will review the regulatory implications of any accounting treatment changes and, if necessary or warranted, will provide further appropriate guidance.

Bank holding companies are encouraged to consult with their external auditor on the appropriate application of generally accepted accounting principles (GAAP), including FIN 46 and revised FIN 46 (FIN 46R), on the consolidation or deconsolidation of trusts issuing trust preferred stock for financial statements and regulatory reporting. Consistent with their GAAP determination and SR 03-13, bank holding companies that deconsolidate such trusts for financial reporting purposes should include the full amount of the deeply subordinated note issued to the trust in Schedule HC, Balance Sheet, item 20, "Other liabilities," and Schedule HC-G, Other Liabilities, item 4," Other," and the bank holding company's investment in the special purpose subsidiary should be reported in Schedule HC, item 8, "Investments in unconsolidated subsidiaries and associated companies." The amount of the subordinated note issued to the trust, net of the bank holding company's investment in the special purpose subsidiary, is equivalent to the amount of

the trust preferred securities issued. The net amount (that qualifies for inclusion in tier 1 capital) should be reported in new item 6.b and in memoranda item 3.d, "Other cumulative preferred stock eligible for inclusion in Tier 1 capital."

Bank holding companies that file the FR Y-11 should continue to report special purpose entities issuing trust preferred securities that qualify as a subsidiary as defined by Regulation Y and in the FR Y-11 reporting instructions, regardless of whether the entity is consolidated on the FR Y-9C report. Bank holding companies that file the FR Y-9LP should continue to report any notes payable to special-purpose subsidiaries that issue trust preferred securities in Schedule PC-B, item 16 (and included in Schedule PC, item 18(b) and Schedule PC-B, item 5(b)). However, for purposes of reporting Schedule PC, item 15(b), "Total combined loans and leases of nonbank subsidiaries", the term "subsidiary" is inclusive of only companies that have been consolidated in the FR Y-9C. Therefore, if the bank holding company has deconsolidated the special purpose entity issuing trust preferred securities, the loan from the subsidiary to the parent bank holding company would not be included in this item.

AICPA Statement of Position 03-3 on Purchased Loans

In December 2003, the AICPA issued Statement of Position 03-3, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*. In general, this Statement of Position applies to purchased impaired loans, i.e., loans that a banking organization has purchased, including those acquired in a purchase business combination, when there is evidence of deterioration of credit quality since the origination of the loan and it is probable, at the purchase date, that the banking organization will be unable to collect all contractually required payments receivable. The Statement of Position does not apply to the loans that a banking organization has originated.

Under this Statement of Position, a purchased impaired loan is initially recorded at its purchase price (in a purchase business combination, the present value of amounts to be received). The Statement of Position limits the yield that may be accreted on the loan (the accretable yield) to the excess of the banking organization's estimate of the undiscounted principal, interest, and other cash flows expected at acquisition to be collected on the loan over the banking organization's initial investment in the loan. The excess of contractually required cash flows over the cash flows expected to be collected on the loan, which is referred to as the nonaccretable difference, must not be recognized as an adjustment of yield, loss accrual, or valuation allowance. Neither the accretable yield nor the nonaccretable difference may be shown on the balance sheet. After acquisition, increases in the cash flows expected to be collected generally should be recognized prospectively as an adjustment of the loan's yield over its remaining life. Decreases in cash flows expected to be collected should be recognized as an impairment.

The Statement of Position prohibits a banking organization from "carrying over" or creating valuation allowances in the initial accounting for purchased impaired loans. This prohibition applies to the purchase of an individual impaired loan, a pool or group of impaired loans, and impaired loans acquired in a purchase business combination.

The Statement of Position applies to loans acquired in fiscal years beginning after December 15,

2004, with early adoption permitted. Bank holding companies must follow this Statement of Position for FR Y-9C reporting purposes in accordance with its effective date based on their fiscal years.

GNMA Mortgage Loan Optional Repurchase Program

Government National Mortgage Association (GNMA) mortgage-backed securities are backed by residential mortgage loans that are insured or guaranteed by the Federal Housing Administration (FHA), the Department of Veterans Affairs/Veterans Administration (VA), or the Farmers Home Administration (FmHA). GNMA programs allow financial institutions to buy back individual delinquent mortgage loans that meet certain criteria from the securitized loan pool for which the institution provides servicing. At the servicer's option and without GNMA's prior authorization, the servicer may repurchase such a delinquent loan for an amount equal to 100 percent of the remaining principal balance of the loan. Under FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* this buy-back option is considered a conditional option until the delinquency criteria are met, at which time the option becomes unconditional.

When the loans backing a GNMA security are initially securitized, Statement No. 140 permits the issuer of the security to treat the transaction as a sale for accounting purposes because the conditional nature of the buy-back option means that the issuer does not maintain effective control over the loans. The loans are removed from the issuer's balance sheet. When individual loans later meet GNMA's specified delinquency criteria and are eligible for repurchase, the issuer (provided the issuer is also the servicer) is deemed to have regained effective control over these loans and, under Statement No. 140, the loans can no longer be reported as sold. The delinquent GNMA loans must be brought back onto the issuer-servicer's books as assets and initially recorded at fair value, regardless of whether the issuer intends to exercise the buy-back option. An offsetting liability would also be recorded. Whether or not these rebooked delinquent loans are repurchased, the issuer-servicer should report them as loans on the FR Y-9C balance sheet (Schedule HC) and related schedules. These loans should be reported as held for sale (Schedule HC, item 4.a) or held for investment (Schedule HC, item 4.b), based on facts and circumstances, in accordance with generally accepted accounting principles. These loans should not be reported as "Other assets" (Schedule HC, item 11). The offsetting liability should be reported as "Other borrowed money" (Schedule HC, item 16).

For risk-based capital purposes, these rebooked loans should be risk-weighted in the same manner as all other FHA, VA, and FmHA loans, i.e., at 20 percent to the extent of the conditional guarantee. For leverage capital purposes, these rebooked loans should be included in the bank holding company's average total assets.

Accounting for Deferred Compensation Agreements, Including Indexed Retirement Plans

On February 11, 2004, the Federal Reserve issued supervisory letter SR-04 with an attached Interagency Advisory on Accounting for Deferred Compensation Agreements and Bank-Owned Life Insurance. The agencies had found that many institutions were incorrectly accounting for their obligations under a type of deferred compensation agreement commonly referred to as a

revenue neutral plan or an indexed retirement plan, the typical characteristics of which are described in the advisory. The benefits payable to employees under these plans generally are based on the performance of the bank-owned life insurance (BOLI) policies on these employees.

The agencies believe the guidance in the advisory on the appropriate accounting for deferred compensation agreements and BOLI is consistent with generally accepted accounting principles. The table below sets forth the appropriate reporting of BOLI in the FR Y-9C report.

Y-9C Item	Amount to Report
Schedule HC, Item 11, "Other assets," and Schedule HC-F, Item 5, "All other assets"	Include the amount that could be realized under BOLI policies as of the report date.
Schedule HC-F, Item 5.a, "Cash surrender value of life insurance"	Include the amount that could be realized under BOLI policies as of the report date if such amount exceeds 25% of the total of "All other assets" reported in Schedule HC-F, Item 5.
Schedule HI, Item 5.l, "Other noninterest income"	Include the net change in the cash surrender value of BOLI policies. [1]
Schedule HI-E, Memoranda item 6.b, "Earnings on/increase in value of cash surrender value of life insurance"	Include the net change in the cash surrender value of BOLI policies if such amount is greater than 1% of the sum of total interest income and total noninterest income.
Schedule HI, Item 7.d, "Other noninterest expense"	Include the BOLI expenses for policies in which the institution is the beneficiary.[2]
Schedule HI-E, Item 2.h, "Other noninterest expense"	Include the BOLI expenses for policies in which the institution is the beneficiary if such amount is greater than 1% of the sum of total interest income and total noninterest income.

The following table sets forth the appropriate reporting of deferred compensation agreements in the FR Y-9C report.

---

[1] For the FR Y-9C, the net earnings (losses) on or the net increases (decreases) in the cash surrender value may be reported. Alternatively, the gross earnings (losses) on or increases (decreases) in value may be reported in Schedule HI, Item 5.l, and the BOLI policy expenses may be reported in Schedule HI, Item 7.d.

[2] Applicable for the FR Y-9C report only if institutions report the gross earnings (losses) on or increases (decreases) in the cash surrender value in FR Y-9C Schedule HI, Item 5.l.

FR Y-9C Item	Amount to Report
Schedule HC, Item 20, "Other liabilities," and Schedule HC-G, Item 4, "All other liabilities"	Include the amount of deferred compensation liabilities.
Schedule HI, Item 7.a, "Salaries and employee benefits"	Include the annual compensation expense (service component and interest component) related to deferred compensation agreements.

Bank holding companies should review their accounting for deferred compensation agreements to ensure that their obligations to employees under these agreements have been properly measured and reported. As indicated in the interagency advisory, any necessary changes in a bank holding companies accounting for these agreements should be reflected in its March 31, 2004, FR Y-9C. Unless amendments to prior FR Y-9C reports are required, corrections of material errors on prior years' earnings, net of applicable taxes, should be reported as an adjustment to the beginning balance of equity capital (i.e., as a prior period adjustment) in Schedule RI-A, item 2. The accounting and reporting guidance in the advisory will be incorporated into the June 2004 FR Y-9C reporting instructions.

FASB Statement No. 149 and Loan Commitments That Must Be Accounted for as Derivatives

FASB Statement No. 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities,* provides guidance on the circumstances in which a loan commitment must be accounted for as derivative. Under Statement No. 149, loan commitments that relate to the origination of mortgage loans that will be held for sale, commonly referred to as interest rate lock commitments, must be accounted for as derivative instruments by the issuer of the commitment. Commitments to originate mortgage loans that will be held for investment purposes and commitments to originate other types of loans are not considered derivatives. In addition, for commitments to purchase or sell existing loans, the definition of a derivative in FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*, should be applied to these commitments to determine whether they meet this definition and are subject to the provisions of Statement No. 133 (see page GL-19 of the Glossary section of the FR Y-9C instructions).

Interest rate lock commitments are considered over-the-counter written interest rate options for FR Y-9C reporting purposes. Because they are derivatives, these commitments should not be reported as unused commitments in item 1 of Schedule HC-L, Derivative and Off-Balance Sheet Items. Instead, interest rate lock commitments must be reported on the balance sheet (Schedule HC) at fair value. Consistent with Securities and Exchange Commission (SEC) Staff Accounting Bulletin No. 105, in recognizing commitments to originate mortgage loans that will be held for sale that are entered into after March 31, 2004, a bank holding company may not consider the expected cash flows related to the associated servicing of the mortgage loan. Further, no other internally developed intangible assets should be recorded as part of the loan

commitment derivative. This SEC Staff Accounting Bulletin can be accessed at www.sec.gov/interps/account/sab105.htm.

The par value of the mortgage loans to be originated under these commitments must be reported in Schedule HC-L, item 11.d.(1), column A, and in Schedule HC-L, item 13, column A. The fair value of these interest rate lock commitments must be reported in the appropriate subitem of Schedule HC-L, item 14.b. As written options, interest rate lock commitments are outside the scope of the credit conversion process that applies to derivatives under the Federal Reserve's risk-based capital standards. However, if the fair value of any of these commitments after initial recognition is positive and therefore reported as an asset, this positive fair value is subject to the risk-based capital standards and must be risk weighted as an on-balance sheet asset.

The unused portion of loan commitments that are not considered derivatives should continue to be reported in Schedule HC-L, item 1. Unused commitments with an original maturity exceeding one year are subject to the risk-based capital standards and must be reported in Schedule HC-R, item 53.

Reporting Asset-Backed Commercial Paper Conduits in Schedules HC-L, HC-R, and HC-S

For purposes of Memorandum item 3 of Schedule HC-S, Servicing, Securitization, and Asset Sale Activities, bank holding companies (BHCs) must report the requested information on credit enhancements and liquidity facilities provided to asset-backed commercial paper conduits regardless of their accounting treatment for the conduit. Thus, whether or not a BHC must consolidate the conduit for reporting purposes in accordance with FASB Interpretation No. 46 (Revised), the BHC must report its maximum credit exposure arising from and its unused commitments to conduit structures in Memorandum items 3.a and 3.b, respectively.

The banking agencies have issued an interim final rule that sets forth a temporary risk-based capital treatment for assets in asset-backed commercial paper conduits that sponsoring bank organizations are required to consolidate in accordance with Interpretation No. 46. This interim capital treatment allows sponsoring bank organizations to exclude the consolidated asset-backed commercial paper program assets from their risk-weighted asset bases when they calculate their risk-based capital ratios. However, sponsoring bank organizations must continue to hold risk-based capital against all exposures arising in connection with these programs, including direct credit substitutes, recourse obligations, residual interests, long-term liquidity facilities, and loans. Furthermore, any minority interests in consolidated asset-backed commercial paper programs are not eligible for inclusion in Tier 1 capital (or total risk-based capital). This interim risk-based capital treatment will be in effect through the March 31, 2004, FR Y-9C report date. In addition, the interim risk-based capital treatment does not alter the accounting rules for balance sheet consolidation under Interpretation No. 46 (Revised), nor does it affect the denominator of the Tier 1 leverage capital ratio calculation, which continues to be based primarily on on-balance sheet assets as reported under generally accepted accounting principles.
However, bank holding companies should continue to report in the appropriate items of Schedule HC-R any credit enhancements and liquidity facilities that they provide to the asset-backed commercial paper programs they sponsor.

Under the agencies' interim rule, bank organization sponsors of any consolidated asset-backed commercial paper programs should include the consolidated assets in the appropriate balance sheet asset categories when completing items 34 through 43, column A, in Schedule HC-R, Regulatory Capital. The amounts of these consolidated assets should also be reported in items 34 through 43, column B, "Items not Subject to Risk-Weighting." However, sponsoring bank organizations must continue to hold risk-based capital against all exposures arising in connection with these programs, whether or not the programs are consolidated, including direct credit substitutes, recourse obligations, residual interests, long-term liquidity facilities, and loans. These exposures should be reported in the appropriate items of Schedule HC-R. Furthermore, any minority interests in consolidated asset-backed commercial paper programs are not eligible for inclusion in Tier 1 capital (or total risk-based capital), and therefore not be included in Schedule HC-R, item 6(a), “Qualifying minority interests in consolidated subsidiaries and similar items.”

For those asset-backed commercial paper programs that a bank holding company consolidates, any credit enhancements and liquidity facilities the bank provides to the conduit should not be reported in Schedule HC-L, Derivatives and Off-Balance Sheet Items. In contrast, for programs that are not consolidated, the bank should report the credit enhancements and liquidity facilities it provides to the programs in the appropriate items of Schedule HC-L.

Reporting Gains and Losses from Extinguishments of Debt, Including Prepayment Penalties

Until it was rescinded by FASB Statement No. 145 in April 2002, FASB Statement No. 4 required gains and losses from the extinguishment (repayment or retirement) of debt to be aggregated and, if material, reported as extraordinary items. Under Statement No. 145, such gains and losses should be classified as extraordinary items only if they meet the criteria in Accounting Principles Board Opinion No. 30. For FR Y-9C purposes, except for those unusual and infrequent gains and losses that qualify as extraordinary, bank holding companies should aggregate their gains and losses from the extinguishment of debt, including losses resulting from the payment of prepayment penalties on borrowings such as Federal Home Loan Bank advances, and consistently report the net amount in item 7.d, "Other noninterest expense," of the income statement (Schedule HI). Only if a bank holding company's debt extinguishments normally result in net gains over time should the bank holding company consistently report its net gains (losses) in Schedule HI, item 5.l, "Other noninterest income." This reporting guidance will be incorporated in the June 2004 reporting instructions.

In addition, under FASB Emerging Issues Task Force (EITF) Issue No. 96-19, “Debtor’s Accounting for a Modification or Exchange of Debt Instruments,” the accounting for the gain or loss on the modification or exchange of debt depends on whether the original and the new debt instruments are substantially different. If they are substantially different, the transaction is treated as an extinguishment of debt and the gain or loss on the modification or exchange is reported immediately in earnings as discussed above. If the original and new debt instruments are not substantially different, the gain or loss on the modification or replacement of the debt is deferred and recognized over time as an adjustment to the interest expense on the new

borrowing. EITF Issue No. 96-19 provides guidance on how to determine whether the original and the new debt instruments are substantially different.

Deposit Accounts on Which the Interest Rate Has Been Reduced to Zero

Many depository institutions offer deposit products, such as money market deposit accounts or NOW accounts, on which they periodically adjust the interest rate paid on the accounts in response to changes in market interest rates and other factors. If a depository institution's rate adjustments on certain deposit accounts have reduced the interest rate to zero, but the interest rate paid on these accounts can be increased as market conditions change, the bank holding company should continue to report the deposits as interest-bearing accounts in item 13 of Schedule HC, Balance Sheet, and include them in the appropriate deposit items in Schedule HC-K, Quarterly Averages. This reporting guidance will be incorporated in the June 2004 reporting instructions.

Equity-Indexed Certificates of Deposit

Under FASB Statement No. 133, a certificate of deposit (CD) that pays "interest" based on changes in an equity securities index is a hybrid instrument with an embedded derivative that must be accounted for separately from the host contract, i.e., the CD. Examples of equity-indexed CDs include the "Index Powered CD" and the "Dow Jones Industrials Indexed Certificate of Deposit."

At the maturity date of a typical equity-indexed CD, the holder of the CD receives the original amount invested in the CD plus some or all of the appreciation, if any, in an index of stock prices over the term of the CD. Thus, the equity-indexed CD contains an embedded equity call option. To manage the market risk of its equity-indexed CDs, a bank that issues these CDs normally enters into one or more separate freestanding equity derivative contracts with an overall term that matches the term of the CDs. At maturity, these separate derivatives are expected to provide the bank with a cash payment in an amount equal to the amount of appreciation, if any, in the same stock price index that is embedded in the CDs, thereby providing the bank with the funds to pay the "interest" on the equity-indexed CDs. During the term of the separate freestanding equity derivative contracts, the bank will periodically make either fixed or variable payments to the counterparty on these contracts.

When a subsidiary bank of a bank holding company (BHC) issues an equity-indexed CD, it must account for the written equity call option embedded in the CD separately from the CD host contract. The fair value of this embedded derivative on the date the CD is issued must be deducted from the amount the purchaser invested in the CD, creating a discount on the CD that must be amortized to interest expense over the term of the CD using the effective interest method. This interest expense should be reported in the income statement, of the FR Y-9C, in the appropriate subitem of Schedule HI, item 2.a, "Interest on deposits." The equity call option must be "marked to market" at least quarterly with any changes in the fair value of the option recognized in earnings. On the balance sheet, the carrying value of the CD host contract and the fair value of the embedded equity derivative may be combined and reported together as deposit liabilities on the balance sheet (Schedule HC). As for the separate freestanding derivative

contracts the bank enters into to manage its market risk, these derivatives must be carried on the balance sheet as assets or liabilities at fair value and "marked to market" at least quarterly with changes in their fair value recognized in earnings. The fair value of the freestanding derivatives should not be netted against the fair value of the embedded equity derivatives for FR Y-9C balance sheet purposes because these two derivatives have different counterparties. The periodic payments to the counterparty on these freestanding derivatives must be accrued with the expense reported in earnings along with the change in the derivative's fair value. In the FR Y-9C income statement (Schedule HI), the changes in the fair value of the embedded and freestanding derivatives, including the effect of the accruals for the payments to the counterparty on the freestanding derivatives, should be netted and reported consistently in either "Other noninterest income" (item 5.l) or "Other noninterest expense" (item 7.d).

The notional amounts of the embedded and freestanding equity derivatives must be reported in column C of Schedule HC-L, items 11.d.(1) and 11.e, respectively. The notional amounts of both derivatives must also be included in Schedule HC-L, item 13, column C. The fair values of these two derivative contracts must be included in the appropriate subitems of Schedule HC-L, item 14.b, column C. The equity derivative embedded in the indexed CD is a written option, which is not covered by the Federal Reserve's risk-based capital standards. However, the freestanding equity derivative is covered by these standards.

A BHC or its subsidiary that purchases an equity-indexed CD for investment purposes must account for the embedded purchased equity call option separately from the CD host contract. The fair value of this embedded derivative on the date of purchase must be deducted from the purchase price of the CD, creating a discount on the CD that must be accreted into income over the term of the CD using the effective interest method. This accretion should be reported in the FR Y-9C income statement in Schedule HI, item 1.c. The embedded equity derivative must be "marked to market" at least quarterly with any changes in its fair value recognized in earnings. These fair value changes should be reported consistently in either "Other noninterest income" (item 5.l) or "Other noninterest expense" (item 7.d). The carrying value of the CD host contract and the fair value of the embedded equity derivative may be combined and reported together as interest-bearing balances due from depository institutions on the balance sheet in Schedule HC, item 1.b. The notional amount of the embedded derivative must be reported in Schedule HC-L, item 11.d.(2), column C, and item 13, column C, and, if appropriate, its fair value (which will always be positive or zero, but not negative) must be reported in Schedule HC-L, item 14.b.(1), column C. The embedded equity derivative in the indexed CD is a purchased option, which is subject to the Federal Reserve's risk-based capital standards. Guidance on the accounting and reporting treatment of these CDs will be incorporated into the June 2004 FR Y-9C reporting instructions.

Listing of Revisions

Revisions to the FR Y-9C for March 2004:

Report Form and Corresponding Instructions

(1) *Cover page.* Updated reporting date to March 31, 2004. Added line for E-mail address of contact.
(2) *Schedule HC, item 20.* Added footnote indicating that trust preferred securities are included in other liabilities.
(3) *Schedule HC-C, memoranda item 1.* Corrected reference to Schedule HC-N, memoranda item 2, to Schedule HC-N, memoranda item 1.
(4) *Schedule HC-M, item 22.* Added item for "Address (URL) for the reporting bank holding company's web page that displays risk disclosures, including those about credit and market risk." Item is to be reported by bank holding companies with total assets of $30 billion or more.
(5) *Schedule HC-R, item 6.* Added new item 6(b), "Qualifying trust preferred securities," and renumbered current item 6, "Qualifying minority interests in consolidated subsidiaries" as item 6.a.
(6) *Schedule HC-R, memoranda item 3.* Removed the caption for memoranda item 3.a, "Perpetual preferred stock eligible for inclusion in Tier 1 capital:," and modified the caption for memoranda item 3 to read "Preferred stock (including related surplus) eligible for inclusion in Tier 1 capital:." Renumbered memoranda item 3.a.(1) as item 3.a. and modified the caption to read "Noncumulative perpetual preferred stock (included and reported in "Total equity capital," on Schedule HC)." Renumbered memoranda item 3.a.(2) as item 3.b. and modified the caption to read "Cumulative perpetual preferred stock (included and reported in "Total equity capital," on Schedule HC)." Modified current memoranda item 3.b, "Cumulative preferred stock (e.g., trust preferred securities) included and reported in 'Minority interest in consolidated subsidiaries and similar items,' on Schedule HC" to read "Other cumulative preferred stock eligible for inclusion in Tier 1 capital (e.g., trust preferred securities) (included in Schedule HC, items 20 or 22" and renumbered as memoranda item 3.d. Added a new memoranda item 3.c, "Other noncumulative preferred stock eligible for inclusion in Tier 1 capital (e.g., REIT preferred securities) (included in Schedule HC, item 22)."

Instructions Only

(1) *General Instructions.* Clarified "Amended Reports" removing pooling of interest reference.
(2) *Schedule HI, item 2(d).* Clarified reporting of interest on notes payable to unconsolidated special purpose entities that issue trust preferred securities.
(3) *Schedule HI, item 5(h)(1).* Added clarification on premiums transferred, and replaced certain text with reference to the Glossary entry on "Insurance Premiums."
(4) *Schedule HI, items M12(b)(1), M12(b)(2) and M12(c).* Changed language removing reference to earned versus written premiums and added other clarifying language.
(5) *Schedule HC, item 8.* Clarified that investments in unconsolidated special purpose entities issuing trust preferred securities are included.

(6) *Schedule HC, items 19 and 22.* Modified instructions to indicate that trust preferred securities of consolidated special purpose entities, or notes payable to unconsolidated special purpose entities issuing trust preferred securities, are to be reported as other liabilities and not as subordinated notes and debentures or as minority interest.
(7) *Schedule HC-G, item 4.* Modified instructions to indicate that trust preferred securities of consolidated special purpose entities, or notes payable to unconsolidated special purpose entities issuing trust preferred securities, are to be reported as other liabilities.
(8) *Schedule HC-R, Examples.* Modified to reflect references to new item 6.b, and to indicate that for bank holding companies that have deconsolidated special purpose entities issuing trust preferred securities, the term trust preferred securities then refers to the amount of notes payable the unconsolidated subsidiary, net of their investment in the subsidiary.
(9) *Glossary:* Modified entries for "Insurance Commissions," "Insurance Premiums" and "Trust Preferred Securities Issued."
(10) *Edits:* Updates to the FR Y-9C Checklist and FR Y-9C Edits.

Revisions to the FR Y-9LP for March 2004:

Report Form

Cover page. Updated reporting date to March 31, 2004. Added line for E-mail address of contact.

Instructions

Edits. Updates to the FR Y-9LP Edits.

Revisions to the FR Y-11/S for March 2004

Report Form

Updated reporting date to March 31, 2004. No other changes for this quarter.

Instructions

(1) *Memoranda Schedule BS-M.* Clarified that memoranda items 1 through 3 and 5 through 7 exclude balances due from related institutions. Clarified that items 9 through 11 exclude balances due to related institutions.