Board of Governors of the Federal Reserve System

Supplemental Instructions September 2008

Editing of Data by Respondents

The Federal Reserve requires validation checks to be performed by respondents as part of the electronic submission process for the FR Y-9 series of reports. This process requires bank holding companies (BHCs) to perform published validity and quality checks on data (so-called edits) by the filing deadline. Respondents are encouraged to file reports electronically as soon as possible, rather than waiting until the submission deadline. Validity and quality edits are provided at the end of the reporting instructions for the FR Y-9C, FR Y-9LP, FR Y-9SP and FR Y-9ES. Additional information regarding this submission process may be found on the web site: *www.reportingandreserves.org* under the heading BHC Modernization project. For example, see this website for information on guidelines for resolving edits and a document addressing frequently asked questions (FAQ).

Limited Exemption from Leverage and Risk-Based Capital Rules

To reduce liquidity and other strains being experienced by money market mutual funds, the Federal Reserve System adopted on September 19, 2008, a special lending facility (ABCP Lending Facility) that enables depository institutions and bank holding companies to borrow from the Federal Reserve Bank of Boston on a nonrecourse basis if they use the proceeds of the loan to purchase certain types of asset-backed commercial paper (ABCP) from money market mutual funds. The ABCP must be purchased by a banking organization between September 19, 2008, and January 30, 2009 (unless extended by the Board), from an SEC-registered open-end investment company that holds itself out as a money market mutual fund under SEC Rule 2a-7 (17 CFR 270.2a-7) and pledged by the banking organization to a Federal Reserve Bank to secure financing from the ABCP Lending Facility.

To facilitate this Federal Reserve lending program, the Board of Governors of the Federal Reserve System (Board) also has adopted, on an interim final basis, an exemption from its leverage and risk-based capital rules for ABCP held by a state member bank or bank holding company as a result of its participation in this program.

Specifically, the interim final rule (i) amends the Board's risk-based capital rules for state member banks and bank holding companies to assign a zero percent risk weight to ABCP purchased by the banking organization as a result of its participation in the facility; and (ii) amends the Board's leverage capital rules for state member banks and bank holding companies to permit banking organizations to exclude from average total consolidated assets – the denominator of the leverage ratio – ABCP purchased by the banking organization as a result of its participation in the facility.

Consistent with its purpose to mitigate temporary stresses faced by U.S. money market mutual funds, the interim final rule will expire on January 30, 2009, unless extended by the Board.

Consistent with generally accepted accounting principles (GAAP), the Federal Reserve would expect bank holding companies to report purchased ABCP as an investment security (i.e., held-to-maturity or available-for-sale) on their balance sheets. These assets would be reflected at the time of purchase at the organization's best estimate of fair value. The non-recourse nature of the transaction would impact the valuation of the liability to the Federal Reserve. After reflecting any appropriate discounts on the assets and associated liabilities, organizations are not expected to report any material net gains or losses (if any) at the time of purchase. Any discounts generally would be accreted over time into income and expense.

For the September 30, 2008, FR Y-9C reporting period, bank holding companies would include the amount of asset-backed commercial paper purchased using proceeds from the ABCP Lending Facility in Schedule HC-B, item 5, "Asset-backed securities," and include in either Schedule HC-R, item 35, "Held-to-maturity securities," or Schedule HC-R, item 36, "Available-for-sale securities," as appropriate, in both Column A (Totals) and Column C (0% risk-weight category). The average of such ABCP purchased would be reported in Schedule HC-R, item 26, "LESS: Other deductions from assets for leverage capital purposes," and thus excluded from Schedule HC-R, item 27, "Average total assets for leverage capital purposes." Borrowings from the Federal Reserve Bank of Boston would be included in Schedule HC, item 16, "Other borrowed money," and included in Schedule HC-M, item 14.b, "Other borrowed money with a remaining maturity of one year or less."

Furthermore, bank holding companies must separately disclose in footnote 1 of "Notes to the Balance Sheet – Other," the amount of ABCP purchased using proceeds from the ABCP Lending Facility included in Schedule HC-R, item 35 or 36, Column C. In addition bank holding companies must separately disclose in footnote 2 of "Notes to the Balance Sheet – Other," the average amount of ABCP purchased using proceeds from the ABCP Lending Facility that were excluded from Schedule HC-R, item 27.

For more information, the interim final rule can be accessed via the Federal Reserve's Web site (www.federalreserve.gov/newsevents/press/monetary/monetary20080919b2.pdf).

Trust Preferred Securities and Limits on Restricted Core Capital Elements

On March 10, 2005, the Federal Reserve announced the amendment of its risk-based capital standards for bank holding companies to allow the continued inclusion of outstanding and prospective issuances of trust preferred securities in the tier 1 capital of bank holding companies, subject to stricter quantitative limits and qualitative standards. The Federal Reserve also revised the quantitative limits applied to the aggregate amount of qualifying cumulative perpetual preferred stock, qualifying trust preferred securities, and Class B and Class C minority interest[1] (collectively, restricted core capital elements) included in the tier 1 capital of bank holding companies. These new quantitative limits become effective on March 31, 2009. Prior to this

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[1] Class B minority interest in consolidated subsidiaries is defined as qualifying cumulative perpetual preferred stock directly issued by a consolidated U.S. depository institution or foreign bank subsidiary. Class C minority interest in consolidated subsidiaries is defined as qualifying common stockholders' equity or perpetual preferred stock issued by a consolidated subsidiary that is neither a U.S. depository institution nor a foreign bank.

time, a bank holding company with restricted core capital elements in amounts that cause it to exceed these limits must consult with the Federal Reserve on a plan for ensuring that the bank holding company is not unduly relying on these elements in its capital base and, where appropriate, for reducing such reliance to ensure that the bank holding company complies with these limits as of March 31, 2009.

The aggregate amount of restricted core capital elements that may be included in the tier 1 capital of a bank holding company that is not an internationally-active bank holding company[2] must not exceed 25 percent of the sum of all core capital elements (qualifying common stockholders' equity, qualifying noncumulative perpetual preferred stock and related surplus, Class A minority interest[3] and restricted core capital elements), net of goodwill less any associated deferred tax liability. Stated differently, the aggregate amount of a bank holding company's restricted core capital elements includable in tier 1 capital is limited to one-third of the sum of unrestricted core capital elements (i.e., common stockholders' equity, noncumulative perpetual preferred stock and Class A minority interest), net of goodwill less any associated deferred tax liability. In addition, the aggregate amount of restricted core capital elements (other than qualifying mandatory convertible preferred securities[4]) that may be included in the tier 1 capital of an internationally-active bank holding company must not exceed 15 percent of the sum of all core capital elements, including restricted core capital elements, net of goodwill less any associated deferred tax liability. Amounts of restricted core capital elements in excess of these limits generally may be included in tier 2 capital. The excess amounts of restricted core capital elements that are in the form of Class C minority interest and qualifying trust preferred securities are subject to further limitation within tier 2 capital, as discussed below.

Note that some components of qualifying restricted core capital elements (numerator to the ratio calculated to compare to the limit) and some components of qualifying core capital elements (denominator to the ratio calculated to compare to the limit) as identified below, cannot be separately identified in items currently reported on the FR Y-9C.

- Mandatorily convertible preferred securities are not separately reported on the current FR Y-9C, but are reported with other trust preferred securities until the equity securities are issued, which are then reported as common stock or perpetual preferred securities. Such securities are includable in the tier 1 capital of internationally-active bank holding companies above the 15 percent limit, up to the generally applicable 25

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[2] For this purpose, an internationally active bank holding company is a bank holding company that (1) as of its most recent year-end FR Y-9C, reports total consolidated assets equal to $250 billion or more or (2) on a consolidated basis, reports total on-balance-sheet foreign exposure of $10 billion or more on its most recent year-end FFIEC 009 Country Exposure Report.

[3] Class A minority interest is defined as qualifying common stockholders' equity of, or noncumulative perpetual preferred securities issued by, a consolidated subsidiary that is a U.S. depository institution or a foreign bank.

[4] Qualifying mandatory convertible preferred securities generally consist of the joint issuance by a bank holding company to investors of trust preferred securities and a forward purchase contract, which the investors fully collateralize with the securities, that obligates the investors to purchase a fixed amount of the bank holding company's unrestricted core capital elements, generally common or perpetual preferred securities at a price set at initial issuance of the mandatory convertible preferred securities in no more than five years.

percent limit, while they are included in the 25 percent limit (both numerator and denominator) for other bank holding companies.

- Three types of minority interest in consolidated subsidiaries (Class A, B, and C minority interest) established by the tier 1 components rule are not separately reported on the current FR Y-9C report. These classes of minority interest are treated differently under the tier 1 components rule with Class A being an unrestricted core capital element, while Class B and C minority interest are restricted core capital elements.
- The amount of goodwill deducted in computing applicable limits under the tier 1 components rule taking effect on March 31, 2009, is reduced by the amount of any associated deferred tax liability, while goodwill reported on the current FR Y-9C is not net of such deferred tax liability.

The Federal Reserve plans to propose revising Schedule HC-R, Regulatory Capital of the FR Y-9C, as of March 31, 2009, to collect information necessary to confirm that a bank holding company is in compliance with the limits on its restricted core capital elements. Until these revisions are implemented, the ratio of qualifying restricted core capital elements to qualifying total core capital elements may be approximated from information currently reported on the FR Y-9C as follows:

Numerator of the Restricted Core Capital Elements Ratio:

HC-R, item 6.b, “Qualifying trust preferred securities”
+ HC-R, memoranda item 3.b, “Cumulative perpetual preferred stock”
+ HC-R, item 6.a, “Qualifying minority interest in consolidated subsidiaries”

= Total Qualifying Restricted Core Capital Elements (proxy)

Denominator of the Restricted Core Capital Elements Ratio:

HC-R, item 6.b, “Qualifying trust preferred securities”
+ HC-R, item 6.a, “Qualifying minority interest in consolidated subsidiaries”
+ HC-R, item 1, “Total equity capital (from Schedule HC, item 28)”
- HC-R, item 2, “Net unrealized loss on available-for-sale securities (if gain, report as a positive value; if a loss report as a negative value)”
- HC-R, item 3, “Net unrealized loss on available-for-sale equity securities (report loss as a positive value)”
- HC-R, item 4, “Accumulated net gains (losses) on cash flow hedges (if a gain, report as a positive value; if a loss, report as a negative value)
- HC, item 10.a., “Goodwill”

= Total Qualifying Core Capital Elements (proxy)

Another way to approximate the maximum amount of restricted core capital elements that a non-internationally-active bank holding company may include in tier 1 capital as of March 31, 2009 is that a bank holding company’s qualifying restricted core capital elements under the revised standard is equal to one-third of its common stockholders' equity plus noncumulative perpetual preferred securities minus goodwill. This computation may be approximated from information currently reported on the FR Y-9C as follows: 0.33 * [(HC, item 28) – (HC-R, item 2) – (HC-R, item 3) – (HC-R, item 4) – (HC, item 10.a)]. For internationally active bank holding companies, substitute 0.178 for 0.33 in the preceding calculation.

Qualifying Trust Preferred Securities and Limited-life Preferred Stock

In the last five years before the maturity of the junior subordinated notes held by the trust, the outstanding amount of the associated trust preferred securities is excluded from tier 1 capital and included in tier 2 capital, where the trust preferred securities are subject to certain amortization provisions and quantitative restrictions, applicable to limited-life capital instruments (e.g., limited-life preferred stock and subordinated debt). As a limited-life capital instrument approaches maturity, it begins to take on characteristics of a short-term obligation. For this reason, the outstanding amount of term subordinated debt and limited-life preferred stock eligible for inclusion in tier 2 capital is reduced, or discounted, as these instruments approach maturity: one-fifth of the outstanding amount is excluded each year during the instrument's last five years before maturity. When remaining maturity is less than one year, the instrument is excluded from tier 2 capital.

The aggregate amount of term subordinated debt and limited-life preferred stock as well as, effective March 31, 2009, qualifying trust preferred securities and Class C minority interest in excess of the amounts includable in tier 1 capital (previously described) may be included in tier 2 capital up to an aggregate amount of 50 percent of tier 1 capital. Amounts of these instruments in excess of this limit, although not included in tier 2 capital, will be taken into account by the Federal Reserve in its overall assessment of a bank holding company's funding and financial condition.

For more information see the final rule published in the *Federal Register* on March 10, 2005.

Construction Loans

Bank holding companies should note that loans written as combination construction-permanent loans secured by real estate should be reported in Schedule HC-C, item 1.a, "Construction, land development, and other land loans," until construction is completed or principal amortization payments begin, whichever comes first. When the first of these events occurs, the loans should begin to be reported in the real estate loan category in Schedule HC-C, item 1, appropriate to the real estate collateral. All other construction loans secured by real estate should continue to be reported in Schedule HC-C, item 1.a, after construction is completed unless and until (1) the loan is refinanced into a new permanent loan by the reporting bank holding company or is otherwise repaid, (2) the bank holding company acquires or otherwise obtains physical possession of the underlying collateral in full satisfaction of the debt, or (3) the loan is charged off.

Troubled Debt Restructurings

Consistent with FASB Statement No. 15, Accounting by Debtors and Creditors for Troubled

Debt Restructurings (FAS 15), the FR Y-9C reporting instructions define a “troubled debt restructuring” (TDR) as a restructuring in which a bank holding company, for economic or legal reasons related to a borrower’s financial difficulties, grants a concession to the borrower that the bank holding company would not otherwise consider. In general, troubled debt restructurings include a modification of the terms of a loan that provides for a reduction of either interest or principal.

In the FR Y-9C report for March 31, 2008, bank holding companies began reporting the amount of 1-4 family residential mortgage loans that have undergone troubled debt restructurings and are in compliance with their modified terms in Schedule HC-C, Memorandum item 1.a. The amount of 1-4 family residential mortgages that have undergone TDRs and under their modified terms are past due 30 days or more or are in nonaccrual status also began to be reported in Schedule HC-N, Memorandum item 1.a. Furthermore, all restructured troubled loans should continue to be reported in the appropriate loan category in Schedule HC-C (Loans and Lease Financing Receivables) and, if appropriate, in Schedule HC-N (Past Due and Nonaccrual Loans, Leases, and Other Assets).

The accounting standards for TDRs are set forth in FAS 15 as amended by FASB Statement No. 114, Accounting by Creditors for Impairment of a Loan (FAS 114), and are summarized in the Glossary section of the FR Y-9C reporting instructions. All loans whose terms have been modified in a TDR, including both commercial and retail loans, must be evaluated for impairment under FAS 114. Under FAS 114, when measuring impairment on a restructured troubled loan using the present value of expected future cash flows method, the cash flows are discounted at the effective interest rate of the original loan, i.e., before the restructuring. For a residential mortgage loan with a “teaser” or starter rate that is less than the loan’s fully indexed rate, the starter rate is not the original effective interest rate. FAS 114 also permits a bank holding company to aggregate impaired loans that have risk characteristics in common with other impaired loans, such as modified residential mortgage loans that represent TDRs, and use historical statistics along with a composite effective interest rate as a means of measuring the impairment of these loans.

Split-Dollar Life Insurance Arrangements

The Financial Accounting Standards Board’s (FASB) Emerging Issues Task Force (EITF) has issued guidance on the accounting for the deferred compensation and postretirement benefit aspects of split-dollar life insurance arrangements. This guidance is effective for fiscal years beginning after December 15, 2007, including interim periods within those fiscal years, with earlier application permitted. EITF Issue No. 06-4 addresses endorsement split dollar arrangements (http://www.fasb.org/pdf/abs06-4.pdf) while EITF issue No. 06-10 covers collateral assignment split dollar arrangements (http://www.fasb.org/pdf/abs06-10.pdf). In general, in an endorsement split-dollar arrangement, the employer (such as a bank holding company or subsidiary) owns and controls the insurance policy on the employee, whereas in a collateral assignment split-dollar arrangement, the employee owns and controls the insurance policy.

According to the consensus reached by the EITF under each issue, an employer such as a bank holding company should recognize a liability for the postretirement benefit related to a split-dollar life insurance arrangement if, based on the substantive agreement with the employee, the bank holding company has agreed to maintain a life insurance policy during the employee's retirement or provide the employee with a death benefit. This liability should be measured in accordance with either FASB Statement No. 106 (if, in substance, a postretirement benefit plan exists) or Accounting Principles Board Opinion No. 12 (if the arrangement is, in substance, an individual deferred compensation contract). In addition, for a collateral assignment split-dollar arrangement, the EITF also reached a consensus that an employer such as a bank holding company should recognize and measure an insurance asset based on the nature and substance of the arrangement.

Bank holding companies with split-dollar life insurance arrangements must apply the consensuses in EITF Issues No. 06-4 and No. 06-10 for FR Y-9 reporting purposes in accordance with their effective date. Thus, a bank holding company with a calendar year fiscal year must apply the relevant guidance as of January 1, 2008, and should recognize the effects of applying the consensus as a cumulative-effect adjustment to the opening balance of retained earnings on that date. This adjustment should be reported in Schedule HI-A, item 2, "Restatements due to corrections of material accounting errors and changes in accounting principles," and may be separately disclosed in Schedule HI, Notes to the Income Statement—Other.

Measurement of Fair Values in Stressed Market Conditions

The valuation of various assets and liabilities on the balance sheet – including trading assets and liabilities, available-for-sale securities, loans held for sale, assets and liabilities accounted for under the fair value option (which is discussed in the following section), and foreclosed assets – involves the use of fair values. During periods of market stress, the fair values of some financial instruments and nonfinancial assets may decline.

Institutions are reminded that the objective of a fair value measurement is to determine the price that would be received to sell an asset or transfer a liability in an orderly transaction (e.g., not a forced or distressed sale) at the balance sheet date. Accordingly, fair values should reflect current market conditions and consider recent transaction prices, where available. This fair value objective is generally applicable to all fair value measurements, whether or not a bank holding company has early adopted FASB Statement No. 157, *Fair Value Measurements*, which is discussed in the following section.

On October 3, 2007, the Center for Audit Quality (CAQ), which is affiliated with the American Institute of Certified Public Accountants, issued a white paper entitled *Measurements of Fair Value in Illiquid (or Less Liquid) Markets* (http://www.aicpa.org/caq/download/WP_Measurements_of_FV_in_Illiquid_Markets.pdf). The white paper discusses issues associated with fair value measurement under existing generally accepted accounting principles (GAAP) in the context of the conditions that currently exist in many segments of the credit markets. Although the CAQ's white paper was directed to auditors and public companies, the paper articulates certain existing GAAP requirements related to fair value measurement issues that apply to all institutions, whether or not they are public companies. For FR Y-9 reporting purposes, bank holding companies should consider the fair value measurement information contained in the CAQ's white paper.

Fair Value Measurement and Fair Value Option

FASB Statement No. 157, *Fair Value Measurements* (FAS 157), issued in September 2006, defines fair value, establishes a framework for measuring the fair value of assets and liabilities based on a three-level hierarchy, and expands disclosures about fair value measurements. The FASB's three-level fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Level 1 inputs are quoted prices in active markets for identical assets or liabilities that the reporting bank holding company has the ability to access at the measurement date (e.g., the FR Y-9C reporting date). Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs for the asset or liability.

According to FAS 157, observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity. In contrast, unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

FAS 157 is effective for fiscal years beginning after November 15, 2007, and, with certain exceptions, is to be applied prospectively. However, on February 12, 2008, the FASB issued FASB Staff Position No. FAS 157-2, which delays the effective date of FAS 157 for all nonfinancial assets and nonfinancial liabilities, except for those items that are recognized or disclosed at fair value on a recurring basis, i.e., at least annually, in the financial statements. However, this delay does not apply to entities that have issued interim or annual financial statements or FR Y-9C reports that include the application of the measurement and disclosure provisions of FAS 157. Bank holding companies must adopt FAS 157 for FR Y-9C reporting purposes in accordance with the standard's effective date, including the delayed effective date for eligible nonfinancial assets and nonfinancial liabilities. Thus, a bank holding company with a calendar year fiscal year should have adopted FAS 157 as of January 1, 2008, except for any fair value measurements subject to the delay mentioned above.

For those financial instruments identified in FAS 157 to which the standard must be applied retrospectively upon initial application, the effect of initially applying FAS 157 to these instruments should be recognized as a cumulative-effect adjustment to the opening balance of retained earnings at the beginning of the fiscal year of adoption. This adjustment should be reported in Schedule HI-A, item 2, "Restatements due to corrections of material accounting errors and changes in accounting principles," and separately disclosed in the Notes to the Income Statement—Other, item 1.

FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (FAS 159), issued in February 2007, is effective as of the beginning of a bank holding company's first fiscal year that begins after November 15, 2007, and generally should not be applied retrospectively to prior fiscal years. FAS 159 allows bank holding companies to report certain financial assets and liabilities at fair value with the changes in fair value included in earnings. In general, a bank holding company may elect the fair value option for an eligible financial asset or liability when it first recognizes the instrument on its balance sheet or enters into an eligible firm commitment. A bank holding company may also elect the fair value option for eligible items that exist on the effective date of FAS 159. A bank holding company's decision to elect the fair value option for an eligible item is irrevocable. Because FAS 159 creates a fair value option, a bank holding company is not required to adopt FAS 159 for FR Y-9[5] reporting purposes. A bank holding company that elects the fair value option is expected to apply sound risk management and control practices to the assets and liabilities that will be accounted for at fair value under the option.

If, in connection with its substantive adoption of FAS 159, a bank holding company elects the fair value option for eligible items that exist on the effective date of its adoption of this accounting standard, the bank holding company must report the effect of the first remeasurement of these existing items to fair value as a cumulative-effect adjustment to the opening balance of retained earnings at the beginning of the fiscal year of adoption. The difference between the carrying amount and the fair value of eligible items for which the fair value option is elected at the effective date should be removed from the balance sheet (Schedule HC) and included in the cumulative-effect adjustment. This adjustment should be reported in Schedule HI-A, item 2, "Restatements due to corrections of material accounting errors and changes in accounting principles," and separately disclosed in the Notes to the Income Statement—Other, item 1. For available-for-sale securities that exist on the effective date of adoption for which the bank holding company elects the fair value option, the net unrealized gains (losses) on these securities would no longer be included in "Accumulated other comprehensive income" [FR Y-9C: Schedule HC, item 26.b; FR Y-9LP: Schedule PC, item 20.e; FR Y-9SP: Schedule SC, item 16.d]. At the effective date of the election, the net unrealized gains (losses) on these securities should be included in Schedule HI-A, item 2, as described above, and an offsetting amount should be reported as a reduction (increase) in Schedule HI-A, item 12, "Other comprehensive income."

On April 17, 2007, the Center for Audit Quality (CAQ) issued Alert No. 2007-14, *FAS 159 Early Adoption Date Approaching – Factors to Consider* (http://www.thecaq.org/newsroom/pdfs/CAQPressRelease_041807a.pdf). The Alert summarized the principles and objectives of the fair value option as set forth in FAS 159 and provides factors to consider in determining whether an entity has substantively adopted FAS 159 on a go forward basis. Although the CAQ's Alert was directed to auditors and public companies, the factors concerning the evaluation of an entity's purported early adoption of FAS 159 are equally appropriate for nonpublic institutions. For regulatory reporting purposes, bank holding companies are expected to meet the principles and objectives of FAS 159 when applying the fair value option and should consider the information contained in the CAQ's Alert.

[5] Consolidated Financial Statements for Bank Holding Companies (FR Y-9C), Parent Company Only Financial Statements for Large Bank Holding Companies (FR Y-9LP), Parent Company Only Financial Statements for Small Bank Holding Companies (FR Y-9SP)

The Federal Reserve is considering the regulatory capital implications of the use of a fair value option, including the fair value option in FASB Statement No. 155 on certain hybrid financial instruments (FAS 155) and FASB Statement No. 156 on servicing assets and liabilities (FAS 156). Except as discussed below, changes in the fair value of assets and liabilities to which a fair value option is applied that are recognized in earnings should be reflected in Tier 1 capital, pending further guidance from the Federal Reserve. For a liability to which a fair value option is applied, bank holding companies should consider the effect of a change in their own creditworthiness on the fair value of the liability. The Federal Reserve has determined that bank holding companies should exclude from Tier 1 capital the cumulative change in the fair value of liabilities accounted for under a fair value option that is included in retained earnings (Schedule HC, item 26.a) and is attributable to changes in the bank holding company's own creditworthiness. For regulatory capital purposes, this excluded portion of the change in fair value is, in essence, an adjustment to the bank holding company's reported retained earnings and should be reported in Schedule HC-R, item 7.b, so that it is taken into account in determining the Tier 1 capital subtotal (reported in Schedule HC-R, item 8) that is used to determine the regulatory capital limits on such items as servicing assets, deferred tax assets, and credit-enhancing interest-only strips.

Schedule HC-Q, Financial Assets and Liabilities Measured at Fair Value

FR Y-9C Schedule HC-Q, Financial Assets and Liabilities Measured at Fair Value, is to be completed by bank holding companies that are required to have adopted FAS 157 and either (1) have elected to apply a fair value option under FAS 155, 156, or FAS 159, or (2) are required to complete Schedule HC-D, Trading Assets and Liabilities (bank holding companies that meet this criteria but do not meet criteria (1) must complete *only* Schedule HC-Q items 2 and 5, and leave items 1, 2.a, 3, 4, 6 and 7 blank). This schedule captures fair value data on total trading assets and liabilities and on those other assets, liabilities, and loan commitments to which the fair value option is being applied. Accordingly, bank holding companies should not include data in Schedule HC-Q on securities reported as available-for-sale on the FR Y-9C balance sheet (Schedule HC, item 2(b)) or on derivatives held for purposes other than trading that are reported as "Other assets" or "Other liabilities" (Schedule HC, item 11, or item 20). Schedule HC-Q includes columns for Level 1, Level 2, and Level 3 fair value measurements as well as a column for the fair values of assets and liabilities that have been netted for balance sheet purposes in accordance with FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts*, and FASB Interpretation No. 41, *Offsetting of Amounts Related to Certain Repurchase and Reverse Repurchase Agreements*.

Under FAS 159, securities that a bank holding company has elected to report at fair value under the fair value option are reported as trading securities even though management did not acquire the securities principally for the purpose of selling them in the near term or for other trading purposes. Thus, such securities, whether held on the date of adoption of FAS 159 or acquired thereafter, should be reported in Schedule HC-Q in both item 2, "Trading assets," and item 2.a, "Nontrading securities at fair value with changes in fair value reported in current earnings."

FASB Interpretation No. 48 on Uncertain Tax Positions

FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48), was issued in June 2006 as an interpretation of FASB Statement No. 109, *Accounting for Income Taxes.* Under FIN 48, the term "tax position" refers to "a position in a previously filed tax return or a position expected to be taken in a future tax return that is reflected in measuring current or deferred income tax assets and liabilities." FIN 48 further states that a "tax position can result in a permanent reduction of income taxes payable, a deferral of income taxes otherwise currently payable to future years, or a change in the expected realizability of deferred tax assets."

According to FIN 48, a bank holding company should initially recognize the effects of a tax position in its financial statements when, based on the technical merits, it is more likely than not (i.e., a likelihood of more than 50 percent) that the position will be sustained upon examination by the taxing authority, including the resolution of any related appeals or litigation. The more-likely-than-not evaluation must consider the facts, circumstances, and information available at the report date. When a tax position meets the more-likely-than-not recognition threshold, it should initially and subsequently be measured as the largest amount of tax benefit greater than 50 percent likely of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. FIN 48 also provides guidance on subsequent recognition, derecognition, and measurement of tax positions, including the effect of changes in judgment, and on the recognition of interest and penalties. The June 2007 FR Y-9C reporting instructions were updated to include a revised Glossary entry for "Income Taxes" that includes guidance on FIN 48.

Bank holding companies must adopt FIN 48 for FR Y-9 reporting purposes in accordance with the interpretation's effective date. As originally issued, FIN 48 was effective for fiscal years beginning after December 15, 2006. However, for eligible nonpublic enterprises the FASB has deferred the effective date of FIN 48 to annual periods beginning after December 15, 2007. A nonpublic enterprise is eligible for this deferral provided it (a) has not issued a full set of annual financial statements incorporating the recognition, measurement, and disclosure requirements of FIN 48 and (b) is not a subsidiary of a public enterprise. A nonpublic enterprise that meets these conditions is eligible for the deferral even if it has issued interim or quarterly financial information in 2007 that reflected the adoption of FIN 48.

Thus, eligible nonpublic bank holding companies must adopt FIN 48 for FR Y-9 reporting purposes for annual periods beginning after December 15, 2007, based on their respective fiscal years. For example, an eligible nonpublic bank holding company with a calendar year fiscal year must adopt FIN 48 as of January 1, 2008, but is not required to reflect the effect of its adoption of FIN 48 for FR Y-9 reporting purposes until it prepares its FR Y-9 for the December 31, 2008, report date. An eligible nonpublic bank holding company that applied the recognition and measurement provisions of FIN 48 in its FR Y-9 reports for 2007 report dates can either: (a) choose not to adopt the effective date deferral and continue to apply FIN 48 in its FR Y-9 reports going forward; or (b) choose to adopt the effective date deferral and its December 2007 FR Y-9 report should have been prepared without reflecting the application of FIN 48. As noted above, a nonpublic bank holding company that is a subsidiary of a public company does not meet the eligibility conditions for the deferral of the effective date of FIN 48 and at present should be preparing its FR Y-9 reports in accordance with FIN 48.

FASB Statement No. 158 on Defined Benefit Postretirement Plans

FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (FAS 158), issued in September 2006, requires a bank holding company that sponsors a single-employer defined benefit postretirement plan, such as a pension plan or health care plan, to recognize the funded status of each such plan on its balance sheet. An overfunded plan is recognized as an asset while an underfunded plan is recognized as a liability. As of the end of the fiscal year when a bank holding company initially applies FAS 158, the postretirement plan amounts recognized on the bank holding company's balance sheet before applying FAS 158 must be adjusted to recognize gains or losses, prior service costs or credits, and transition assets or obligations that have not yet been included in the net periodic benefit cost of its plans. These adjustment amounts are recognized directly in equity capital as components of the ending balance of accumulated other comprehensive income (AOCI), net of tax. Thereafter, a bank holding company must recognize certain gains and losses and prior service costs or credits that arise during each reporting period, net of tax, as a component of other comprehensive income (OCI) and, hence, AOCI. Postretirement plan amounts carried in AOCI are adjusted as they are subsequently recognized in earnings as components of the plans' net periodic benefit cost. For further information on accounting for defined benefit postretirement plans, bank holding companies should refer to FAS 158; FASB Statement No. 87, *Employers' Accounting for Pensions* (FAS 87); and FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions* (FAS 106).

Currently, FAS 87 and FAS 106 permit bank holding companies that sponsor single-employer defined benefit postretirement plans to choose to measure plan assets and obligations either as of the end of the fiscal year or as of a date not more than three months before the end of the fiscal year. FAS 158 eliminates this choice by generally requiring that, for fiscal years ending after December 15, 2008, plan assets and obligations must be measured as of the end of the fiscal year.

Bank holding companies that sponsor single-employer defined benefit postretirement plans must adopt FAS 158 for FR Y-9C reporting purposes in accordance with the standard's effective date and transition provisions with respect to both funded status and measurement date. In this regard, all bank holding companies should now have adopted the funded status provisions of FAS 158. For FR Y-9C reporting purposes, bank holding companies should report the adjustments to the ending balance of AOCI from initially recognizing the funded status of their plans in accordance with FAS 158 as of the end of their fiscal year of adoption, net of tax, in item 12, "Other comprehensive income," of Schedule HI-A, Changes in Equity Capital. In the fiscal year that the measurement date provisions of FAS 158 are initially applied, bank holding companies should report the adjustment of the opening balance of retained earnings and any adjustment of the opening balance of AOCI in Schedule HI-A, item 2, "Restatements due to corrections of material accounting errors and changes in accounting principles," and should consider disclosing this total amount in Notes to the Income Statement—Other.

In addition, according to an interim decision announced by the banking agencies on December 14, 2006, bank holding companies should reverse the effects on AOCI of FAS 158 for regulatory capital purposes, including for purposes of reporting and measuring the numerators and denominators for the leverage and risk-based capital ratios. The intent of the reversal is to neutralize the effect on AOCI of the application of FAS 158 on regulatory capital. Bank holding companies should exclude from regulatory capital any amounts recorded in AOCI resulting from the initial and subsequent application of both the funded status and measurement date provisions of FAS 158. For FR Y-9C reporting purposes, these excluded amounts should be reported in item 4 of Schedule HC-R, Regulatory Capital, together with the accumulated net gains (losses) on cash flow hedges. If the sum of the amounts included in AOCI (Schedule HC, item 26.b) for defined benefit postretirement plans under FAS 158 and for cash flow hedges represents a net gain (i.e., a net increase) in reported equity capital, this sum should be reported as a positive value in item 4 of Schedule HC-R. If the sum represents a net loss (i.e., a decrease) in reported equity capital, it should be reported as a negative number in item 4 of Schedule HC-R.

For purposes of reporting and measuring the denominators for the risk-based and leverage ratios, bank holding companies should also adjust their assets for any amounts recorded in AOCI affecting assets resulting from the initial and subsequent application of the funded status and measurement date provisions of FAS 158. Specifically, assets recognized or derecognized as an adjustment to AOCI as part of the incremental effect of applying FAS 158 should be reported as an adjustment to assets in item 42 of Schedule HC-R, column B, and should also be reported in item 26 of Schedule HC-R. For example, derecognition of an asset recorded as an offset to AOCI as part of the initial incremental effect of applying FAS 158 should be recorded as a negative amount in item 42, column B, of Schedule HC-R and as a positive amount in item 42, column F. This amount should also be added back to average total assets for leverage capital purposes by reporting it as a negative number in item 26 of Schedule HC-R. As another example, the portion of a benefit plan surplus asset that is included in Schedule HC, item 26.b as an increase to AOCI and is included in item 42, column A, of Schedule HC-R should be excluded from risk-weighted assets by reporting the amount as a positive number in item 42, column B. This amount should also be deducted from average total assets for leverage capital purposes by reporting the amount as a positive number in item 26 of Schedule HC-R. In addition, the adjustments for purposes of calculating risk-based capital and the leverage ratio described above should be adjusted for subsequent amortization of such amounts from AOCI into earnings.

Reporting of Maturity Data on Credit Derivative Contracts in Schedule HC-R

Bank holding companies report the remaining maturities of credit derivative contracts that are subject to risk-based capital requirements in Schedule HC-R, Memorandum items 2.g.(1) and (2), based on the rating of the underlying reference asset. Bank holding companies should report the full gross notional amount of all such credit derivative contracts in these Memorandum items. For credit derivative contracts that are subject to the market risk capital guidelines and for which the bank holding company is the protection seller (guarantor), bank holding companies should ensure that they report the notional amount rather than an amount based on the unpaid or unearned premiums on these derivatives.

FASB Statement No. 123 (Revised 2004) and Share-Based Payments

Bank holding companies should continue to follow the guidance on accounting for share-based payments under FASB Statement No. 123 (Revised 2004), *Share-Based Payment* (FAS 123(R)), that was included in the FR Y-9C Supplemental Instructions for December 31, 2006. These instructions can be accessed via the Federal Reserve's Web site (www.federalreserve.gov/boarddocs/reportforms/supplemental/SI_FRY9_200612.pdf).

Tobacco Transition Payment Program

Bank holding companies should continue to follow guidance on the tobacco buyout program included in the FR Y-9C Supplemental Instructions for June 30, 2006, which can be accessed via the Federal Reserve's Web site (www.federalreserve.gov/boarddocs/reportforms/supplemental/SI.FRY9.200606.pdf).

FASB Interpretation No. 46 (Revised), *Consolidation of Variable Interest Entities*

Bank holding companies should continue to follow the guidance provided on this subject in the FR Y-9C Supplemental Instructions provided for December 31, 2005. These Supplemental Instructions can be accessed via the Federal Reserve's Web site (www.federalreserve.gov/boarddocs/reportforms/supplemental.cfm?WhichFormID=FR_Y-9C).

Reporting of Trust Preferred Securities

Bank holding companies should continue to follow the guidance provided on this subject in the FR Y-9C Supplemental Instructions provided for December 31, 2005. These Supplemental Instructions can be accessed via the Federal Reserve's Web site (www.federalreserve.gov/boarddocs/reportforms/supplemental.cfm?WhichFormID=FR_Y-9C).

Commitments to Originate and Sell Mortgage Loans

Bank holding companies should continue to follow the guidance provided on this subject in the FR Y-9C Supplemental Instructions provided for December 31, 2005. These Supplemental Instructions can be accessed via the Federal Reserve's Web site (www.federalreserve.gov/boarddocs/reportforms/supplemental.cfm?WhichFormID=FR_Y-9C).