Supplemental Instructions September 2006

Editing of Data by Respondents

The Federal Reserve has made changes to the FR Y-9 series to require validation checks to be performed by respondents as part of the electronic submission process. These changes were implemented as of September 30, 2004, for the FR Y-9C and FR Y-9LP reports and implemented as of December 31, 2004, for the FR Y-9SP and FR Y-9ES reports. This new 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).

FASB Statement No. 156 on Servicing

FASB Statement No. 156, Accounting for Servicing of Financial Assets (FAS 156), issued in March 2006, requires all separately recognized servicing assets and liabilities to be initially measured at fair value. It then permits an entity to choose to subsequently measure each class of servicing assets and liabilities at fair value with changes in fair value recognized in earnings. If fair value is not elected, each class of servicing is subsequently accounted for using the amortization method that applied to all servicing assets and liabilities prior to the issuance of FAS 156. An entity identifies its classes of servicing assets and liabilities based on the availability of market inputs for estimating their fair value, its method for managing the risks of its servicing assets and liabilities, or both. An entity’s election of the fair value option for a class of servicing is irreversible. The election can be made for an individual class of servicing assets and liabilities upon adoption of FAS 156 or at the beginning of any subsequent fiscal year.

Bank holding companies must adopt FAS 156 for FR Y-9 series reporting purposes as of the beginning of their first fiscal year that begins after September 15, 2006. Earlier adoption of FAS 156 is permitted as of the beginning of an earlier fiscal year, provided the bank holding company has not yet issued a financial statement or filed a FR Y-9 report for any period of that fiscal year. Thus, a bank holding company with a calendar year fiscal year must adopt FAS 156 as of January 1, 2007, unless it elected earlier adoption and applied FAS 156 in its originally filed March 31, 2006, FR Y-9C/FR Y-9LP, or its June 30, 2006, FR Y-9SP.

When reporting the carrying amount of mortgage servicing assets (FR Y-9C: Schedule HC-M, item 12.a; FR Y-9LP: Schedule PC, item 7.b; FR Y-9SP: included in Schedule SC, item 7) and nonmortgage servicing assets in FR Y-9C Schedule HC-M, item 12.b, bank holding companies should include all classes of servicing accounted for under the amortization method as well as all classes of servicing accounted for at fair value. The fair value of all recognized mortgage servicing assets should be reported in FR Y-9C Schedule HC-M, item 12.a.(1), regardless of the
measurement method applied to these assets. The servicing asset carrying amounts reported in Schedule HC-M, items 12.a and 12.b, even if these amounts include fair values, should be used when determining the lesser of 90 percent of the fair value of these assets and 100 percent of their carrying amount for regulatory capital calculation purposes in Schedule HC-R. Changes in the fair value of any class of servicing assets to which the fair value option is applied should be included in earnings in Schedule HI, item 5.f, “Net servicing fees.”

**FASB Statement No. 155 on Hybrid Financial Instruments**

FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments* (FAS 155), issued in February 2006, requires bifurcation of certain derivatives embedded in interests in securitized financial assets and permits fair value measurement (i.e., a fair value option) for any hybrid financial instrument that contains an embedded derivative that would otherwise require bifurcation under paragraphs 12 and 13 of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (FAS 133). Bifurcation is required when the economic characteristics and risks of the embedded derivative are not clearly and closely related economically to the economic characteristics and risks of the host contract and certain other conditions are met. Under the fair value option in FAS 155, a bank holding company may irrevocably elect to initially and subsequently measure an eligible hybrid financial instrument in its entirety at fair value, with changes in fair value recognized in earnings, rather than bifurcating the instrument and accounting for the embedded derivative separately from the host contract. The election can be made on an instrument-by-instrument basis, but must be supported by appropriate documentation. In addition, FAS 155 clarifies which interest-only and principal-only strips are not subject to FAS 133. For further information on embedded derivatives and FAS 133, refer to the Glossary entry for “Derivative Contracts” in the Y-9C Instructions.

For FR Y-9 series reporting purposes, FAS 155 must be applied to all financial instruments acquired, issued, or subject to a remeasurement event (as defined in the standard) occurring after the beginning of a bank holding company’s first fiscal year that begins after September 15, 2006. The fair value option may also be applied upon adoption of FAS 155 to a bank holding company’s existing hybrid financial instruments that had been bifurcated prior to adoption. Earlier adoption of FAS 155 is permitted as of the beginning of an earlier fiscal year, provided the bank holding company has not yet issued a financial statement or filed a FR Y-9 series report for any period of that fiscal year. Thus, a bank holding company with a calendar year fiscal year must adopt FAS 155 as of January 1, 2007, unless it elected earlier adoption and applied FAS 155 in its originally filed March 31, 2006, FR Y-9C/FR Y-9LP report, or in its originally filed June 30, 2006, FR Y-9SP report.

Following a bank holding company’s adoption of FAS 155, hybrid financial instruments to which the fair value option has been applied should not be reclassified as trading assets or trading liabilities for FR Y-9 reporting purposes solely due to the election of this option. Such hybrid financial instruments should continue to be reported in the asset or liability category appropriate to the instrument. If a hybrid financial instrument to which the fair value option has been applied is an available-for-sale security, it should be included in available-for-sale securities on the balance sheet (FR Y-9C: Schedule HC, item 2.b; FR Y-9LP: Schedule PC, item 2; FR Y-9SP: Schedule SC, item 2) and the security’s fair value should be reported in (FR Y-
Changes in the fair value of hybrid financial instruments to which the fair value option is applied should be aggregated and reported consistently in the income statement either as “Other noninterest income” (FR Y-9C: Schedule HI, item 5.l; FR Y-9LP: Schedule PI, item 1.e; FR Y-9SP: Schedule SI, item 4) or “Other noninterest expense” (FR Y-9C: Schedule HI, item 7.d; FR Y-9LP: Schedule PI, item 2.d; FR Y-9SP: Schedule SI, item 7).

The Federal Reserve is considering the regulatory capital implications of FAS 155, and more broadly, the use of the fair value option. Except as discussed below, changes in the fair value of hybrid instruments that are recognized in earnings should be reflected in Tier 1 capital, pending further guidance from the Federal Reserve. In the interim, for a hybrid financial instrument to which the fair value option is applied that is an asset, the embedded derivative should not be bifurcated from the host contract for risk-based capital purposes in Schedule HC-R. For a hybrid financial instrument for which the embedded derivative is bifurcated, a bank holding company should treat the host contract and the embedded derivative separately for risk-based capital purposes. For a hybrid financial instrument to which the fair value option is applied that is a liability, a bank holding company should exclude the portion of the change in the fair value of the instrument that is attributable to a change in the bank’s own creditworthiness from Tier 1 capital. 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 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. However, as an interim measure until the Federal Reserve revises Schedule HC-R, the excluded portion of the change in fair value should be reported in item 10 of the schedule.

Reporting Securities Borrowing and Lending Transactions on the Balance Sheet

Bank holding companies are permitted to offset assets and liabilities in the FR Y-9C balance sheet (Schedule HC) when a “right of setoff” exists. FASB Interpretation No. 39, Offseting of Amounts Related to Certain Contracts, defines “right of setoff” and specifies what conditions must be met to have that right. FASB Interpretation No. 41 modifies Interpretation No. 39 to permit offsetting in the balance sheet of payables and receivables that represent repurchase agreements and reverse repurchase agreements when the agreements meet specified conditions. According to the AICPA Audit and Accounting Guide for Depository and Lending Institutions, Interpretation No. 41 does not apply to securities borrowing or lending transactions. Therefore, for FR Y-9C purposes, bank holding companies should not offset securities borrowing and lending transactions in the balance sheet unless all the conditions set forth in Interpretation No. 39 are met.

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

FASB Statement No. 123 (Revised 2004), Share-Based Payment (FAS 123(R)), requires all entities to recognize compensation expense in an amount equal to the fair value of share-based payments, e.g., stock options and restricted stock, granted to employees. Bank holding
companies must adopt FAS 123(R) for FR Y-9C purposes in accordance with the standard's effective date and transition provisions. Public companies other than small business issuers, including bank holding companies that are subsidiaries of such public companies, must adopt FAS 123(R) as of the beginning of their first fiscal year beginning after June 15, 2005. All other companies, including small business issuers and bank holding companies that are not subsidiaries of public companies, must adopt FAS 123(R) as of the beginning of their first fiscal year beginning after December 15, 2005. Thus, all bank holding companies with a calendar year fiscal year must implement FAS 123(R) as of January 1, 2006.

Under FAS 123(R), the "compensation cost for an award of share-based employee compensation classified as equity shall be recognized over the requisite service period," which is typically the same as the vesting period, "with a corresponding credit to equity (generally, paid-in capital)." The recording of the compensation cost also gives rise to deferred tax consequences, i.e., a deferred tax asset, that must be recognized (and evaluated for realizability). For FR Y-9C purposes, the compensation expense should be included in Schedule HI, item 7.a., "Salaries and employee benefits," and reported in Schedule HI, memoranda item 15, “Stock-based employee compensation expense (net of tax effects) calculated for all awards under the fair value method,” with the corresponding credit included in Schedule HC, item 25, "Surplus.” Note that once FAS 123(R) is implemented, Schedule HI, memoranda item 14, “Stock-based employee compensation expense (net of tax effects)” need no longer be reported. In Schedule HI-A, Changes in Equity Capital, this credit should be included in item 5, "Sale of perpetual preferred stock," or in item 6, “Sale of common stock.” This reporting treatment applies regardless of whether the shares awarded to the employee are shares of bank stock or shares of the bank’s parent holding company.

Privatization of the Student Loan Marketing Association

On December 29, 2004, the Student Loan Marketing Association (SLMA), a government-sponsored enterprise created in 1972, was dissolved. On that date, SLMA defeased its remaining debt obligations by transferring them into a special and irrevocable trust and depositing U.S. Treasury securities with the trustee in amounts sufficient to pay the principal of and interest on its debt obligations. For FR Y-9C purposes, bank holding companies should continue to report SLMA debt obligations held for purposes other than trading as securities issued by U.S. Government-sponsored agencies in Schedule HC-B, item 2.b. Similarly, SLMA debt obligations held for trading purposes (in domestic offices) should continue to be reported as U.S. Government agency obligations in Schedule HC-D, item 2. Bank holding companies should refer to the guidance in the Federal Reserve’s risk-based capital standards on the treatment of collateralized claims to determine the appropriate risk weight for these SLMA debt securities.

SLM Corporation, the successor to SLMA, is a private-sector corporation that has issued debt securities, including commercial paper. Bank holding companies should report SLM Corporation debt securities held for purposes other than trading as "Other domestic debt securities" in Schedule HC-B, item 6.a. SLM Corporation debt securities held for trading purposes (in domestic offices) should be reported as "Other debt securities" in Schedule HC-D, item 5. Bank holding companies should report holdings of securitized student loans issued by SLM Corporation (or its affiliates) as asset-backed securities in Schedule HC-B, item 5, unless
Agency Prepayment-Linked Notes

In 2004, the Federal National Mortgage Associations (Fannie Mae) and the Federal Home Loan Banks began to issue a type of fixed rate debt securities known as prepayment-linked or index amortizing notes. Principal and interest on the notes are paid monthly, with the principal payments indexed to the prepayment performance of a reference pool of mortgages or a reference mortgage-backed security. However, the notes are not collateralized by the mortgages or mortgage-backed security and they have stated final maturity dates that are generally 5 to 12 years from the date of issuance.

Because these securities are direct unsecured obligations of the issuing government-sponsored agency, bank holding companies should report their holdings of these prepayment-linked notes in Schedule HC-B, item 2.b, if they are not held for trading purposes. In addition, these securities are considered structured notes because of their repayment characteristics and, if not held for trading purposes, must also be reported in Schedule HC-B, Memorandum item 4. For risk-based capital purposes, these agency prepayment-linked notes are a claim on a U.S. government-sponsored agency and should be assigned a 20 percent risk weight.

Tobacco Transition Payment Program

The Fair and Equitable Tobacco Reform Act, commonly referred to as the "Tobacco Buyout," established the Tobacco Transition Payment Program, which is administered by the U.S. Department of Agriculture (USDA). Under this program, the Commodity Credit Corporation (CCC) makes annual payments to eligible tobacco quota holders (i.e., landowners) and tobacco producers (i.e., farmers) from 2005 through 2014. The CCC will not make a lump-sum payment to an individual quota holder or producer in lieu of annual payments. However, a quota holder or producer can obtain a lump-sum payment from a bank or other party by executing an "assignment" of tobacco buyout payments or a "successor-in-interest" contract.

Bank holding companies that enter into CCC-approved assignment contracts and successor-in-interest contracts and make lump-sum payments to tobacco quota holders or producers should report these financing arrangements as "Loans to finance agricultural production and other loans to farmers" in Schedule HC-C, item 3. The discount reflected in these lump-sum payments should be recognized as interest income over the life of the contract using the interest method. For risk-based capital purposes, assignment contracts should be risk weighted at 100 percent because of the potential exposure to payment reductions for any debt owed by the quota holder or producer to an agency of the United States as outlined above. Successor-in-interest contracts from both quota holders and producers are, in essence, unconditionally guaranteed by the U.S. Government and should be risk weighted at zero percent. For further information on the tobacco buyout program, please refer to the guidance on this subject in the FR Y-9C.

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).

GNMA Mortgage Loan Optional Repurchase Program

A seller-servicer must report all delinquent residential mortgage loans backing Government National Mortgage Association mortgage-backed securities that must be rebooked as assets in accordance with FASB Statement No. 140 (GNMA loans), whether they have been repurchased or are eligible for repurchase, as loans held for sale (Schedule HC, item 4.a) or loans held for investment (Schedule HC, item 4.b), based on facts and circumstances, in accordance with generally accepted accounting principles. In addition, if a bank holding company services GNMA loans, but was not the transferor of the loans that have been securitized, and purchases individual delinquent loans out of the GNMA securitization, the bank holding company must also report the purchased loans as loans held for sale or held for investment. All GNMA loans recognized as assets should be reported as past due in Schedule HC-N in accordance with their contractual repayment terms. Such delinquent GNMA loans should be reported in items 1.c, 11, and 11.b of Schedule HC-N. An institution that forecloses on real estate backing a delinquent GNMA loan should report the property as “other real estate owned” and not as an “other asset” on the FR Y-9C balance sheet.

Commitments to Originate and Sell Mortgage Loans

Commitments to originate mortgage loans that will be held for resale, which are referred to as derivative loan commitments, are derivatives and must be accounted for at fair value on the balance sheet by the issuer. All loan sales agreements, including both mandatory delivery and best efforts contracts, must be evaluated by both the seller and the purchaser to determine whether the agreements meet the definition of a derivative under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended by FASB Statement No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities. Institutions must also account for loan sales agreements that meet the definition of a derivative, which are referred to as forward loan sales commitments, at fair value on the balance sheet. The
banking agencies provided guidance on the appropriate accounting and reporting for these commitments in their May 2005 Interagency Advisory on Accounting and Reporting for Commitments to Originate and Sell Mortgage Loans, which can be accessed on the Federal Reserve Board’s Web site at www.federalreserve.gov/boarddocs/srletters/2005/sr0510.htm.

According to the advisory, under a typical derivative loan commitment, the borrower can choose to (1) “lock-in” the current market rate for a fixed-rate loan, i.e., a fixed derivative loan commitment; (2) "lock-in" the current market rate for an adjustable-rate loan that has a specified formula for determining when and how the interest rate will adjust, i.e., an adjustable derivative loan commitment; or (3) wait until a future date to set the interest rate and allow the interest rate to “float” with market interest rates until the rate is set, i.e., a floating derivative loan commitment.

Bank holding companies are expected to apply the guidance in the advisory when preparing their FR Y-9C reports. However, until certain questions that have been raised about floating derivative loan commitments are resolved, institutions should follow their existing reporting policies for floating derivative loan commitments and need not account for and report these commitments as derivatives for FR Y-9C reporting purposes. All other derivative loan commitments should be reported as over-the-counter written interest rate options in Schedule HC-L, Derivatives and Off-Balance Sheet Items, not as unused commitments in item 1 of Schedule HC-L. For further information on the reporting of loan commitments, please refer to 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).
Listing of Revisions

Revisions to the FR Y-9C for September 2006:

Report Form and Corresponding Instructions

(1) **Cover page.** Updated reporting date to September 30, 2006. Revised attestation language and designated the Certified Financial Officer (or individual performing this equivalent function) as the signer of the BHCs report.

(2) **Schedule HC-M, items 23.a and 23.b.** Added new items for the Amount of “Federal funds purchased in domestic offices” that are secured, and for the Amount of “Other borrowings” that are secured.

(3) **Schedule HC-P.** Added new schedule to collect information on closed-end 1-4 family residential mortgage banking activities in domestic offices.

Instructions

(1) **Contents.** Added references to new Schedule HC-P and new Glossary entry for “Securities Activities.” Updated page number references.


(3) **General Instructions.** Modified “How to Prepare the Reports,” section B, “Report Form Captions, Non-applicable Items and Instructional Detail,” to remove reference of possibility of BHCs leaving Schedule HC-R blank.

(4) **General Instructions.** Revised “How to Prepare the Reports,” section F, “Verification and Signatures,” to update the attestation language and designated the Certified Financial Officer (or individual performing this equivalent function) as the signer of the BHCs report.

(5) **Schedule HI, memoranda item 8.** Removed listing of extraordinary items and other adjustments included in this memoranda item. This listing is provided in the instructions for Schedule HI, item 12, “Extraordinary items, net of applicable income taxes and minority interest.”

(6) **Schedule HI, memoranda item 13.** Revised the maximum number of qualifying shareholders of from 75 to 100 for Subchapter S corporations to federal income tax purposes.

(7) **Schedule HC-B, item 2.** Clarified to exclude debt securities of SLM Corporation (successor to Student Loan Marketing Association.

(8) **Schedule HC-B, item 7.** Clarified by adding reference to include Class A and C nonvoting common stock of the Federal Agricultural Mortgage Corporation (Farmer Mac), exclude Class B voting common stock of Farmer Mac, and updated reference to SLM Corporation.

(9) **Schedule HC-B, memoranda item 4.** Clarified by adding reference to Prepayment Linked Notes.

(10) **Schedule HC-F, item 4.** Clarified that Class B voting common stock of Farmer Mac is included in this item.

(11) **Schedule HC-N, memoranda items 7 and 8.** Clarified language for each instruction.
(12) Schedule HC-R, item 6.a. Added example and clarification regarding the treatment of minority interest.
(13) Schedule HC-R, Balance-sheet asset categories subject to risk-weighting. Added paragraph to address the treatment of asset-backed commercial paper conduits.
(14) Schedule HC-R, Derivatives and off-balance sheet items subject to risk-weighting. Added paragraph to address the treatment of liquidity facilities for asset-backed commercial paper conduits.
(15) Glossary. “Offsetting.” Clarified that FASB Interpretation No. 41 does not apply to securities borrowing or lending transactions, and can only offset such transactions if all conditions of FASB Interpretation No. 39 are met.

**Revisions to the FR Y-9LP for September 2006:**

**Report Form**

*Cover page.* Updated reporting date to September 30, 2006. Revised attestation language and designated the Certified Financial Officer (or individual performing this equivalent function) as the signer of the BHCs report.

**Instructions**

*General Instructions.* Revised “How to Prepare the Reports,” section F, “Verification and Signatures,” to update the attestation language and designated the Certified Financial Officer (or individual performing this equivalent function) as the signer of the BHCs report.

**Revisions to the FR Y-11/S for September 2006**

**Report Form and Corresponding Instructions**

*Cover page.* Revised the reporting date to September 30, 2006.

**Instructions Only**

*Income Statement, item 10.* Updated instructions to remove one item from a list of inclusions that is no longer applicable, and corrected reference of APB Opinion No. 30 to FASB Statement No. 144.
SUMMARY OF EDIT CHANGES EFFECTIVE
FOR September 30, 2006, FR Y-9C CHECKLISTS

FR Y-9C
(Validity - V, Quality - Q, Intraseries - I)

New Edits:
Quality: 5705, 5792, 6222, 6383, 6390, 6400, 6408, 6415, 6423, 6428, 6435, 6562, 6564, 6778, 6896, 7590, 9520 (HC-M23a and HC-M23b), 9550 (HC-P1a, HC-P1b, HC-P2a, HC-P2b, HC-P3a, HC-P3b, HC-P4a, and HC-P4b)
Intraseries: 6316, 6317, 6736, 6737, 6738, 6739, 6741, 6742, 6743, 6744, 6745, 6746, 6747, 6748, 6749, 6751, 6752, 6753, 6754, 6756, 6760, 6762, 6763, 6764, 6766, 6767, 6768, 6769, 6960

Revised Edits (if renumbered, old edit # is in parenthesis):
Quality: 6210, 6212, 6281, 6283, 6380, 6385, 6395, 6405, 6410, 6420, 6425, 6430
Intraseries: 6210, 6212, 6281, 6283

Deleted Edits:
Quality: 5410, 5430

Renumbered Edits:
Quality EDCK 5785 was renumbered to Quality EDCK 5781
Intraseries EDCK 5790 was renumbered to Intraseries EDCK 5782
Intraseries EDCK 5793 was renumbered to Intraseries EDCK 5783
Quality EDCK 5794 was renumbered to Quality EDCK 5784
Intraseries EDCK 5795 was renumbered to Intraseries EDCK 5786
Intraseries EDCK 5796 was renumbered to Intraseries EDCK 5787
Quality EDCK 6735 was renumbered to Quality EDCK 6733
Intraseries EDCK 6740 was renumbered to Intraseries EDCK 6757
Quality EDCK 6750 was renumbered to Quality EDCK 6770
Quality EDCK 6755 was renumbered to Quality EDCK 6772
Quality EDCK 6761 was renumbered to Quality EDCK 6774
Quality EDCK 6765 was renumbered to Quality EDCK 6776
Quality EDCK 6897 was renumbered to Quality EDCK 6894

Revised NOTE on Schedule HC-R (last page) to reflect renumbered edits.

FR Y-9LP
(Validity - V, Quality - Q, Intraseries - I, Interseries - R)

New Edits:
Quality: 0990