FEDERAL RESERVE BANK OF NEW YORK

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KENNETH LAMAR
VICE PRESIDENT

March 31, 2004

To: The Chief Executive Officer of Each U.S. Branch and Agency of a Foreign Bank Located in the Second Federal Reserve District

Enclosed are copies of forms for the following reports for the quarter ending March 31, 2004:

- Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks (FFIEC 002);
- Supplemental Report of Assets and Liabilities of a Non-U.S. Branch that is Managed or Controlled by a U.S. Branch or Agency of a Foreign (Non-U.S.) Bank (FFIEC 002S); and
- The Country Exposure Report for U.S. Branches and Agencies of Foreign Banks (FFIEC 019).

There are no changes to the FFIEC 002S or FFIEC 019 reporting forms or instructions for March 31, 2004 report date. However, there are changes to the FFIEC 002 reporting forms and instructions. In addition, there is Supplemental Guidance for the FFIEC 002 addressing the reporting of the Financial Accounting Standards Board Interpretations No. 46 and 149.

Reports Monitoring

Please note that, under the Regulatory Reports Monitoring Program, the timeliness of receipt of each of these reports will be monitored. Submission of initial data via facsimile, even if prior to the deadline, does not constitute timely filing.

An original and one copy of the completed FFIEC 002 and FFIEC 002S report(s) (if applicable) must be returned to this Bank, by mail or messenger, no later than April 30, 2004. Any FFIEC 002/002S report received after 5:00 p.m. on April 30, 2004 will be considered late unless postmarked by April 28 or sent by overnight service by April 29.

An original and one copy of the completed FFIEC 019 must be returned to this Bank, by mail or messenger by Monday, May 17, 2004. Any FFIEC 019 received after 5:00 p.m. on May 17 will be considered late unless postmarked by May 15 or sent by overnight service by May 16. Completed reports should be submitted to:

Federal Reserve Bank of New York
Statistics Function
33 Liberty Street, 4th Floor
New York, NY 10045

We will also continue to monitor the accuracy of the periodic regulatory reports submitted for the March 31, 2004 report date. The staff of this Reserve Bank will monitor whether banking organizations are meeting their basic reporting requirements through the use of "validity edits." The current edits for the FFIEC 002/002S and FFIEC 019 reports that are subject to monitoring are unchanged and sent to you in a previous mailing.

FFIEC 002 Report Changes

Schedule L—Derivatives and Off-Balance-Sheet Items

- The requirement that only branches or agencies with total assets of $100 million or more are required to complete item 12, "Gross fair values of derivative contracts," has been deleted. The exemption from reporting the fair values of derivative contracts for branches and agencies with less than $100 million in assets originated predates FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (FAS 133). FAS 133 requires all derivatives to be measured at fair value and reported on the balance sheet as assets or liabilities. Because branches and agencies with less than $100 million in assets that have derivatives now have to regularly report the fair value derivative contracts, they have the information necessary to disclose the fair value of their derivatives in Schedule L.

Schedule M—Due from/Due to Related Institutions in the U.S. and in Foreign Countries (CONFIDENTIAL)

- Removed the exemption for branches and agencies with total assets of $100 million or more, to report "Gross fair values of derivative contracts,' (item 12).
- Added "Gross positive fair value," (Memoranda item 1.a) and 1.b, "Gross negative fair value" (Memoranda item 1.b) to Memoranda item 1, "Notional amount of all credit derivatives on which the reporting branch or agency is the guarantor," and added "Gross positive fair value," (Memoranda item 2.a) and "Gross negative fair value,"

(Memoranda item 2.b.) to Memoranda item 2, "Notional amount of all credit derivatives on which the reporting branch or agency is the beneficiary." The new items will provide a better measure of credit and market risk for credit derivatives entered into with related depository institutions, particularly for branches and agencies with large positions in such credit derivatives.

Schedule RAL-Assets and Liabilities & Glossary

The instructions and Glossary entries for "Federal funds sold," "Federal funds purchased," "Securities purchased under agreements to resell" and "Securities sold under agreements to repurchase" were revised to be consistent with the domestic bank Call Report (FFIEC 031-041). That is security resale and repurchase agreements that mature in one business day or roll over under a continuing contract are no longer reported in "Federal funds sold/purchased", they are reported in "Securities purchased under agreements to resell" or "Securities sold under agreements to repurchase" regardless of maturity.

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

FASB Statement No. 133 Implementation Issue No. C13 provides guidance on the circumstances in which a loan commitment must be accounted for as derivative. This guidance applies to commitments issued before July 1, 2003. **Commitments issued after June 30, 2003, are addressed by FASB Statement No. 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities. U.S. branches or agencies*** must follow the guidance in Issue No. C13 and Statement No. 149 for FFIEC 002 reporting purposes.

Issue No. C13, states that loan commitments that relate to the origination or purchase of mortgage loans that will be held for sale must be accounted for as derivative instruments in accordance with Statement No. 133. However, loan commitments that relate to the origination or purchase of mortgage loans that will be held for investment, i.e., loans for which the U.S. branch or agency has the intent and ability to hold for the foreseeable future or until maturity or payoff, are not considered derivatives. In addition, commitments that relate to the origination of other types of loans (that is, other than mortgage loans) are not considered derivatives.

FASB Statement No. 149 differs from Issue No. C13. Under Statement No. 149, loan commitments that relate to the origination of mortgage loans that will be held-for-sale must be accounted for as derivatives by the issuer of the commitment. Commitments to originate mortgage loans that will be held for investment purposes and other types of loans are not derivatives. However, for commitments to purchase or sell existing loans, the definition of a derivative in Statement No. 133 (see page GL-15 of the Glossary section of the FFIEC 002 instructions) should be applied to these commitments to determine whether they meet this definition and are subject to the provisions of Statement No. 133.

Mortgage loan commitments that must be accounted for as derivatives are considered over-the-counter written interest rate options. Therefore, because they are derivatives, these commitments should be excluded from item 1 of Schedule L, Derivative and Off-Balance Sheet Items. Instead, mortgage loan commitments that are derivatives must be reported on the balance sheet (Schedule RAL) at fair value. In addition, the par value of the mortgage loans to be acquired under these commitments must be reported in Schedule L, item 9.d (1), column A, and in Schedule L, item 11, column A. The fair value of these mortgage loan commitments must be reported in the appropriate subitem of Schedule L, item 12.b. The unused portion of loan commitments that are not derivatives should continue to be reported in Schedule L, item 1.

FASB Interpretation No. 46

Accounting Issues

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" (VIE) (previously referred to as a "special purpose entity") and how an organization should assess its interests in a VIE to decide whether to consolidate that entity. VIEs often are created for a single specified purpose, for example, to facilitate securitization, leasing, hedging, research and development, and reinsurance.

In general, a VIE 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 VIE'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 FFIEC 002 purposes, U.S. branches and agencies with variable interests in VIEs 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. (This applies only to VIEs of the U.S. branch or agency and not to the VIEs of the parent bank or any of the parent bank's other offices).

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 U.S. branches or agencies whose parents are U.S. public companies that have interests in VIEs or potential VIEs commonly referred to as special-purpose entities beginning December 31, 2003. Application of Interpretation No. 46 (Revised) by U.S. branches or agencies whose parents are U.S. public companies, for all other types of variable interest entities is required beginning March 31, 2004. Application of Interpretation No. 46 (Revised) for a U.S. branch or agency whose parent is not a U.S. public company is required immediately for VIEs created after December 31, 2003, and for all other VIEs at the beginning of the first fiscal year beginning after December 15, 2004.

Reporting Asset-Backed Commercial Conduits

U.S. branches or agencies 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 on Memorandum item 1 of Schedule S, Servicing, Securitization, and Asset Sale Activities. Thus, whether or not a U.S. branch or agency must consolidate the conduit for reporting purposes in accordance with FASB Interpretation No. 46, the U.S. branch or agency must report its maximum credit exposure arising from and its unused commitments to conduit structures in Memorandum items 1.a and 1.b, respectively on Schedule S.

For those asset-backed commercial paper programs that a U.S. branch or agency consolidates, any credit enhancements and liquidity facilities the bank provides to the conduit should not be reported in Schedule 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 L.

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

Many U.S. branches and agencies 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 the 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 U.S. branch or agency should continue to report the deposits as interest-bearing accounts in item 4.a of Schedule RAL, Balance Sheet, and include them in the appropriate deposit items in Schedule K, Quarterly Averages.

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. U.S. branches or agencies must follow this Statement of Position for FFIEC 002 reporting purposes in accordance with its effective date based on their fiscal years.

Electronic Submission Option

Electronic submission of the FFIEC 002/002S reports is available to all U.S. branches and agencies. We encourage you to take advantage of this method of reporting submission. Vendors have developed a software package that provides the means to submit the FFIEC 002/002S electronically. Submitting reports electronically using the software package provides the following key benefits:

- A timely and efficient alternative to sending the report forms by mail;
- Data are checked automatically for miscalculated totals and blank fields; and
- A printed report is generated that can serve as your institution's permanent record of the report.

For information on filing the FFIEC 002/002S report electronically, please contact Carolyn Polite at (212) 720-5415.

Website

The FFIEC 002/002S and the FFIEC 019 forms and instructions are available on the FFIEC web site at http://www.ffiec.gov/ffiec_report_forms.htm.

Questions regarding the FFIEC 002, FFIEC 002S & FFIEC 019 reports should be directed to Brian Goodwin at (212) 720-8316, Doug Herold at (212) 720-8591 or Peter Drake, Team Leader in the Regulatory Reports Division at (212) 720-2695.

Sincerely,

-- Signed by --
Kenneth P. Lamar
Vice President
Statistics Function