

# FEDERAL RESERVE BANK OF NEW YORK

NEW YORK, N.Y. 10045-0001

AREA CODE 212-720-5000

October 3, 2007

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

The following report forms and instructions for the September 30, 2007 reporting date have been posted to the Federal Reserve Board's website at [www.federalreserve.gov](http://www.federalreserve.gov) under "Reporting Forms":

- 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 002, 002S or 019 reporting forms or instructions for the September 30, 2007 report date.

Below is supplemental guidance for the FFIEC 002 addressing the reporting treatment of the Financial Accounting Standards 157, 159, and 155.

## **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 recent market stress events, the fair values of some financial instruments and nonfinancial assets have declined.

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 branch or an agency has early adopted FASB Statement No. 157, Fair Value Measurements, which is discussed in the following section.

#### **FASB Statement No. 157 on Fair Value Measurement**

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 branch or agency has the ability to access at the measurement date (e.g., the FFIEC 002 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.

FAS 157 is effective for financial statements issued by the parent bank for fiscal years beginning after November 15, 2007, and, with certain exceptions, is to be applied prospectively. Earlier adoption of FAS 157 is permitted as of the beginning of an earlier fiscal year, provided that no financial statements have been filed for any period of that fiscal year.

#### **FASB Statement No. 159 on Fair Value Option**

FASB Statement No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (FAS 159), issued in February 2007, would allow to report certain financial assets and liabilities at fair value with the changes in fair value included in earnings. In general, a branch or agency 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 branch or agency may also elect the fair value option for eligible items that exist on the effective date of FAS 159. A branch or agency's decision to elect the fair value option for an eligible item is irrevocable.

A branch or agency 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.

FAS 159 is effective for financial statements issued by the parent bank for fiscal years that begin after November 15, 2007, and should not be applied retrospectively to prior fiscal years, except as permitted in the standard's early adoption provisions. A branch or agency may adopt FAS 159 and elect the fair value option for existing eligible items as of the beginning of a fiscal year that begins on or before November 15, 2007, subject to the conditions set forth in the standard, one of which is a requirement to adopt all of the requirements of FAS 157 at the early adoption date of FAS 159 or earlier.

On April 17, 2007, the Center for Audit Quality (CAQ), which is affiliated with the American Institute of Certified Public Accountants, issued Alert No. 2007-14, *FAS 159 Early Adoption Date Approaching - Factors to Consider* ([http://www.thecaq.org/newsroom/pdfs/CAQPressRelease\\_041807a.pdf](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, branches and agencies 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.

### **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 FASB Statement No. 133 (FAS 133) on derivatives. 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 branch or agency 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. 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.

FAS 155 should be applied to all financial instruments acquired, issued, or subject to a remeasurement event (as defined in the standard) occurring after the beginning of the parent bank's first fiscal year that begins after September 15, 2006. The fair value option may also be applied upon adoption of FAS 155 to 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 that the parent bank did not issue financial statements for any period of that fiscal year.

Following the 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 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 a security, it should be included in available-for-sale securities on the balance sheet (FFIEC 002, Schedule RAL, item 1.b or 1.c) and the security's fair value should be reported in (FFIEC 002, memo item 3 and 4).

### **Subscription Service**

We are offering a new subscription service which enables you to receive recent news and updates on our reporting forms and instructions and upcoming Bank events. You can sign up for this new service at the following website:

[http://service.govdelivery.com/service/subscribe.html?code=USFRBN  
EWYORK\\_8](http://service.govdelivery.com/service/subscribe.html?code=USFRBN<br/>EWYORK_8)

### **Reports Monitoring**

Please note that the timeliness of receipt of each of these reports will be monitored and the 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 October 30, 2007. Any FFIEC 002/002S report received after 5:00 p.m. on

October 3, 2007

October 30, 2007 will be considered late unless postmarked by October 26 or sent overnight service by October 29.

An original and one copy of the completed FFIEC 019 must be returned to this Bank, by mail or messenger by November 14, 2007. Any FFIEC 019 received after 5:00 p.m. on November 14, 2007 will be considered late unless postmarked by November 9 or sent by overnight service by November 13. Completed reports should be submitted to:

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

We will also continue to monitor the accuracy of the periodic regulatory reports submitted for the September 30, 2007 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 were sent to you in a previous mailing.

### **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 benefits:

- A timely and efficient alternative to sending the report forms by mail; 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 website at:  
[http://www.ffiec.gov/ffiec\\_report\\_forms.htm](http://www.ffiec.gov/ffiec_report_forms.htm).

October 3, 2007

Questions regarding the FFIEC 002, FFIEC 002S and FFIEC 019 reports should be directed to Carolina Reyes, Senior Reports Analyst in the Regulatory Reporting Division at (212) 720-2695, or Doug Herold, Team Leader in the Division at (212) 720-8591.

Sincerely,

-- Signed by Richard Molloy --

Richard Molloy  
Statistics Officer  
Statistics Function

Enclosures