

FEDERAL RESERVE BANK *of* NEW YORK

33 LIBERTY STREET, NEW YORK, NY 10045-0001

PATRICIA SELVAGGI
ASSISTANT VICE PRESIDENT

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To: The Individual Responsible for Filing the Consolidated Report of Condition and Income for Edge and Agreement Corporations (FR 2886b) located in the Second Federal Reserve District.

Subject: Edge and Agreement Corporation reporting requirements for December 31, 2014

The report forms and instructions for the Consolidated Report of Condition and Income for Edge and Agreement Corporations (FR 2886b) for the quarter ending December 31, 2014, have been posted to the Federal Reserve Board's website at www.federalreserve.gov under "Reporting Forms." There are no changes to the reporting forms for the FR 2886b for this quarter.

Supplemental instructions concerning current accounting and reporting issues affecting the FR 2886b are provided in this letter.

Pushdown Accounting

On November 18, 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-17, "Pushdown Accounting." Pushdown accounting is an acquirer's establishment of a new accounting basis under ASC Topic 805, Business Combinations (formerly FASB Statement No. 141 (revised 2007), "Business Combinations"), in its separate financial statements upon a change-in-control event, i.e., when an acquirer obtains control of an acquiree. Also on November 18, 2014, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 115 to remove Topic 5.J, "New Basis of Accounting Required in Certain Circumstances," from the Codification of Staff Accounting Bulletins. Under Topic 5.J, pushdown accounting generally was permitted when 80 percent or more of an entity's ownership was acquired, required when 95 percent or more was acquired, and prohibited when less than 80 percent was acquired. Prior to the issuance of ASU 2014-17, U.S. generally accepted accounting principles (GAAP) offered limited guidance on pushdown accounting. In accordance with ASU 2014-17, U.S. GAAP now allows reporting entities to elect to apply pushdown accounting in certain business combinations.

Edge and agreement corporations should follow the Call Report (FFIEC 031/41) Glossary entry for "Business Combinations" which mirror the SEC's pushdown guidance in

Topic 5.J. Consequently, with the FASB's issuance of ASU 2014-17 and the SEC's removal of Topic 5.J, the Federal Reserve is rescinding its existing requirements for pushdown accounting and adopting the recognition and measurement provisions of ASU 2014-17 for FR 2886b purposes in accordance with the guidance discussed below.

Key aspects of ASU 2014-17 include the following:

- An acquiree that retains its separate corporate existence may apply pushdown accounting upon a change-in-control event (generally, an acquirer's acquisition of more than 50 percent ownership in the acquiree). The election to apply, or not apply, pushdown accounting is irrevocable so long as the acquirer maintains control of the acquiree.
- An acquiree that elects pushdown accounting must reflect in its separate financial statements the new basis of accounting established by the acquirer under which essentially all of the acquiree's individual assets and liabilities are stated at fair value, including any goodwill arising from the business combination. Recognition of any bargain purchase gain in the acquiree's net income is prohibited; rather, the gain is recognized in income by the acquirer. Consequently, any bargain purchase gain is reflected by the acquiree as additional paid-in capital.

The Federal Reserve notes that the pushdown accounting election available under ASU 2014-17 can be used to produce a particular result in the FR 2886b that may not be reflective of the economic substance of the underlying business combination. Therefore, consistent with the existing FR 2886b instructions on pushdown accounting which can be referenced in the Call Report (FFIEC 031/41) Glossary entry for "Business Combinations," the Federal Reserve reserves the right to require, or prohibit, the institution's use of pushdown accounting for FR 2886b purposes based on the regulator's evaluation of whether the election appears not to be supported by the facts and circumstances of the business combination.

For FR 2886b purposes, an acquired institution that retains its separate corporate existence may apply the pushdown accounting election in ASU 2014-17 if the change-in-control date for its acquisition in a business combination is on or after October 1, 2014. An institution acquired in a business combination before October 1, 2014, in which it retained its separate corporate existence should not change the basis of accounting it previously applied for FR 2886b purposes as a result of its acquisition.

Edge and agreement corporations should follow the Call Report (FFIEC 031/41) instructions on pushdown accounting currently included in the Glossary entry for "Business Combinations" which will be revised to reflect the issuance of ASU 2014-17.

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For additional information, institutions should refer to ASU 2014-17, which is available at <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176156316498>.

Transmission through Reporting Central

The FR 2886b reports are now available to be transmitted through the Reporting Central application. For institutions that do not choose to file this report electronically, the Federal Reserve will continue to accept paper copy submissions. For institutions that submit these reports electronically, they must maintain in their files a signed printout of the data submitted. Additional information about the Reporting Central application, including an online resource center, is available at: <http://www.frbservices.org/centralbank/reportingcentral/index.html>

Private Company Accounting Alternatives, Including Accounting for Goodwill

In May 2012, the Financial Accounting Foundation, the independent private sector organization responsible for the oversight of the Financial Accounting Standards Board (FASB), approved the establishment of a Private Company Council (PCC) to improve the process of setting accounting standards for private companies. The PCC is charged with working jointly with the FASB to determine whether and in what circumstances to provide alternative recognition, measurement, disclosure, display, effective date, and transition guidance for private companies reporting under U.S. generally accepted accounting principles (GAAP). Alternative guidance for private companies may include modifications or exceptions to otherwise applicable existing U.S. GAAP standards.

The Federal Reserve has concluded that an edge and agreement corporation that is a private company, as defined in U.S. GAAP (as discussed in the next section of these Supplemental Instructions), is permitted to use private company accounting alternatives issued by the FASB when preparing its FR 2886b report(s), except as provided in 12 U.S.C. 1831n (a) as described in the following sentence. If the Federal Reserve determines that a particular accounting principle within U.S. GAAP, including a private company accounting alternative, is inconsistent with the statutorily specified supervisory objectives, the Federal Reserve may prescribe an accounting principle for regulatory reporting purposes that are no less stringent than U.S. GAAP. In such a situation, an institution would not be permitted to use that particular private company accounting alternative or other accounting principle within U.S. GAAP for FR 2886b reporting purposes. The Federal Reserve would provide appropriate notice if they were to disallow any accounting alternative under the statutory process.

On January 16, 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-02, "Accounting for Goodwill," which is a consensus of the PCC. This ASU generally permits a

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private company to elect to amortize goodwill on a straight-line basis over a period of ten years (or less than ten years if more appropriate) and apply a simplified impairment model to goodwill. In addition, if a private company chooses to adopt the ASU's goodwill accounting alternative, the ASU requires the private company to make an accounting policy election to test goodwill for impairment at either the entity level or the reporting unit level. Goodwill must be tested for impairment when a triggering event occurs that indicates that the fair value of an entity (or a reporting unit) may be below its carrying amount. In contrast, existing U.S. GAAP does not permit goodwill to be amortized, instead requiring goodwill to be tested for impairment at the reporting unit level annually and between annual tests in certain circumstances. The ASU's goodwill accounting alternative, if elected by a private company, is effective prospectively for new goodwill recognized in annual periods beginning after December 15, 2014, and in interim periods within annual periods beginning after December 15, 2015. Goodwill existing as of the beginning of the period of adoption is to be amortized prospectively over ten years (or less than ten years if more appropriate). The ASU states that early application of the goodwill accounting alternative is permitted for any annual or interim period for which a private company's financial statements have not yet been made available for issuance.

An edge and agreement corporation that meets the private company definition in ASU 2014-02, as discussed in the following section of these Supplemental Instructions (i.e., a private institution), is permitted, but not required, to adopt this ASU for FR 2886b reporting purposes and may choose to early adopt the ASU. If a private institution issues U.S. GAAP financial statements and adopts the ASU, it should apply the ASU's goodwill accounting alternative in its FR 2886b reports in a manner consistent with its reporting of goodwill in its financial statements. Thus, for example, a private institution with a calendar year fiscal year that chooses to adopt ASU 2014-02 must apply the ASU's provisions in its December 31, 2015, and subsequent quarterly FR 2886b reports unless early application of the ASU is elected. If a private institution with a calendar year fiscal year is adopting ASU 2014-02 for 2014 financial reporting purposes, the institution may implement the provisions of the ASU in its FR 2886b reports for December 31, 2014. This would require the private institution to report in its year-end 2014 FR 2886b one full year's amortization of goodwill existing as of January 1, 2014, and the amortization of any new goodwill recognized in 2014. For the FR 2886b, goodwill amortization expense should be reported in item 7.c.(3) of the income statement (Schedule RI) unless the amortization is associated with a discontinued operation, in which case the goodwill amortization should be included within the results of discontinued operations and reported in Schedule RI, item 11, "Extraordinary items, net of tax effect."

Private institutions choosing to early adopt the goodwill accounting alternative in ASU 2014-02 that have a fiscal year or an early application date other than the one described in the examples above should contact their Federal Reserve District Bank for reporting guidance.

For additional information on the private company accounting alternative for goodwill, institutions should refer to ASU 2014-02, which is available at <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176156316498>.

Definitions of Private Company and Public Business Entity

According to ASU No. 2014-02, “Accounting for Goodwill,” a private company is a business entity that is not a public business entity. ASU No. 2013-12, “Definition of a Public Business Entity,” which was issued in December 2013, added this term to the Master Glossary in the Accounting Standards Codification. This ASU states that a business entity, such as an edge and agreement corporation, that meets any one of five criteria set forth in the ASU is a public business entity for reporting purposes under U.S. GAAP, including FR 2886b reporting purposes. An institution that is a public business entity is not permitted to apply the private company goodwill accounting alternative discussed in the preceding section when preparing its FR 2886b reports.

As defined in ASU 2013-12, a business entity is a public business entity if it meets any one of the following criteria:

- It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
- It is required by the Securities Exchange Act of 1934 (the Act), as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency other than the SEC (such as one of the federal banking agencies).
- It is required to file or furnish financial statements with a foreign or domestic regulatory agency in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.
- It has issued securities that are traded, listed, or quoted on an exchange or an over-the-counter market, which includes an interdealer quotation or trading system for securities not listed on an exchange (for example, OTC Markets Group, Inc., including the OTC Pink Markets, or the OTC Bulletin Board).
- It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including footnotes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

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ASU 2013-12 also explains that if an entity meets the definition of a public business entity solely because its financial statements or financial information is included in another entity's filing with the SEC, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC, but not for other reporting purposes.

If an edge and agreement corporation does not meet any one of the first four criteria, it would need to consider whether it meets both of the conditions included in the fifth criterion to determine whether it would be a public business entity. A mutual institution does not meet the fifth criterion. With respect to the first condition under the fifth criterion, a stock institution must determine whether it has a class of securities not subject to contractual restrictions on transfer, which the FASB has stated means that the securities are not subject to management preapproval on resale. A contractual management preapproval requirement that lacks substance would raise questions about whether the stock institution meets this first condition.

For additional information on the definition of a public business entity, institutions should refer to ASU 2013-12, which is available at

<http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176156316498>.

Accounting for a Subsequent Restructuring of a Troubled Debt Restructuring

When a loan has previously been modified in a troubled debt restructuring (TDR), the lending institution and the borrower may subsequently enter into another restructuring agreement. The facts and circumstances of each subsequent restructuring of a TDR loan should be carefully evaluated to determine the appropriate accounting by the institution under U.S. generally accepted accounting principles. Under certain circumstances it may be acceptable not to account for the subsequently restructured loan as a TDR. The Federal Reserve will not object to an institution no longer treating such a loan as a TDR if at the time of the subsequent restructuring the borrower is not experiencing financial difficulties and, under the terms of the subsequent restructuring agreement, no concession has been granted by the institution to the borrower. To meet these conditions for removing the TDR designation, the subsequent restructuring agreement must specify market terms, including a contractual interest rate not less than a market interest rate for new debt with similar credit risk characteristics and other terms no less favorable to the institution than those it would offer for such new debt. When assessing whether a concession has been granted by the institution, the Federal Reserve considers any principal forgiveness on a cumulative basis to be a continuing concession. When determining whether the borrower is experiencing financial difficulties, the institution's assessment of the borrower's financial condition and prospects for repayment after the restructuring should be supported by a current, well-documented credit evaluation performed at the time of the restructuring.

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If at the time of the subsequent restructuring the institution appropriately demonstrates that a loan meets the conditions discussed above, the impairment on the loan need no longer be measured as a TDR in accordance with ASC Subtopic 310-10, Receivables – Overall (formerly FASB Statement No.114), and the loan need no longer be disclosed as a TDR in the FR 2886b report, except as noted below. Accordingly, going forward, loan impairment should be measured under ASC Subtopic 450-20, Contingencies – Loss Contingencies (formerly FASB Statement No. 5). Even though the loan need no longer be measured for impairment as a TDR or disclosed as a TDR, the recorded investment in the loan should not change at the time of the subsequent restructuring (unless cash is advanced or received). In this regard, when there have been charge-offs prior to the subsequent restructuring, consistent with longstanding FR 2886b instructions, no recoveries should be recognized until collections on amounts previously charged off have been received. Similarly, if interest payments were applied to the recorded investment in the TDR loan prior to the subsequent restructuring, the application of these payments to the recorded investment should not be reversed nor reported as interest income at the time of the subsequent restructuring.

If the TDR designation is removed from a loan that meets the conditions discussed above and the loan is later modified in a TDR or individually evaluated and determined to be impaired, then the impairment on the loan should be measured under ASC Subtopic 310-10 and, if appropriate, the loan should be disclosed as a TDR.

For a subsequently restructured TDR loan on which there was principal forgiveness and therefore does not meet the conditions discussed above, the impairment on the loan should continue to be measured as a TDR. However, if the subsequent restructuring agreement specifies a contractual interest rate that, at the time of the subsequent restructuring, is not less than a market interest rate for new debt with similar credit risk characteristics and the loan is performing in compliance with its modified terms after the subsequent restructuring, the loan need not continue to be reported as a TDR in Schedule RC-N, Memorandum item 1, in calendar years after the year in which the subsequent restructuring took place. To be considered in compliance with its modified terms, a loan that is a TDR must be in accrual status and must be current or less than 30 days past due on its contractual principal and interest payments under the modified repayment terms.

Institutions may choose to apply this guidance prospectively to TDR loans that, upon a subsequent restructuring on or after October 1, 2014, meet the conditions discussed above for removing the TDR designation. Institutions also may choose to apply this guidance to loans outstanding as of September 30, 2014, for which there has been a previous subsequent

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restructuring that met the conditions discussed above at the time of the subsequent restructuring. However, prior FR 2886b reports should not be amended.

Reporting Certain Government-Guaranteed Mortgage Loans upon Foreclosure

In August 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-14, “Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure,” to address diversity in practice for how government-guaranteed mortgage loans are recorded upon foreclosure. The ASU updates guidance contained in ASC Subtopic 310-40, Receivables – Troubled Debt Restructurings by Creditors (formerly FASB Statement No. 15, “Accounting by Debtors and Creditors for Troubled Debt Restructurings,” as amended), because U.S. generally accepted accounting principles (GAAP) previously did not provide specific guidance on how to categorize or measure foreclosed mortgage loans that are government guaranteed. The new ASU clarifies the conditions under which a creditor must derecognize a government-guaranteed mortgage loan and recognize a separate “other receivable” upon foreclosure (that is, when a creditor receives physical possession of real estate property collateralizing a mortgage loan in accordance with the guidance in ASC Subtopic 310-40).

Under the new guidance, institutions should derecognize a mortgage loan and record a separate other receivable upon foreclosure of the real estate collateral if the following conditions are met:

- The loan has a government guarantee that is not separable from the loan before foreclosure.
- At the time of foreclosure, the institution has the intent to convey the property to the guarantor and make a claim on the guarantee and it has the ability to recover under that claim.
- At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed (that is, the real estate property has been appraised for purposes of the claim and thus the institution is not exposed to changes in the fair value of the property).

This guidance is applicable to fully and partially government-guaranteed mortgage loans. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. This other receivable should be reported in Schedule RC, item 8, “Other assets.” Other real estate owned would not be recognized by the institution.

For institutions that are public business entities, as defined under U.S. GAAP (as discussed in the preceding section of these Supplemental Instructions), ASU 2014-14 is effective

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for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. For example, institutions with a calendar year fiscal year that are public business entities must apply the ASU in their FR 2886b reports beginning March 31, 2015. However, institutions that are not public business entities (i.e., that are private companies) are not required to apply the guidance in ASU 2014-14 until annual periods ending after December 15, 2015, and interim periods beginning after December 15, 2015. Thus, institutions with a calendar year fiscal year that are private companies must apply the ASU in their December 31, 2015, and subsequent quarterly FR 2886b reports. Earlier adoption of the guidance in ASU 2014-14 is permitted if the institution has already adopted the amendments in ASU No. 2014-04, “Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure” (which is discussed in the following section of these Supplemental Instructions).

Entities can elect to apply ASU 2014-14 on either a modified retrospective transition basis or a prospective transition basis. However, institutions must use the method of transition that is elected for ASU 2014-04 (that is, either modified retrospective or prospective). Applying ASU 2014-14 on a prospective transition basis should be less complex for institutions than applying the ASU on a modified retrospective transition basis. Under the prospective transition method, an institution should apply the new guidance to foreclosures of real estate property collateralizing certain government-guaranteed mortgage loans (based on the criteria described above) that occur after the date of adoption of the ASU. Under the modified retrospective transition method, an institution should apply a cumulative-effect adjustment to affected accounts existing as of the beginning of the annual period for which the ASU is adopted. The cumulative-effect adjustment for this change in accounting principle should be reported in Schedule RI-A, item 6.

For additional information, institutions should refer to ASU 2014-14, which is available at <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176156316498>.

Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans Upon a Foreclosure

In January 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-04, “Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans. Upon Foreclosure” to address diversity in practice for when certain loan receivables should be derecognized and the real estate recognized. The ASU updated guidance contained in Accounting Standards Codification Subtopic 310-40, Receivables - Troubled Debt Restructurings by Creditors.

Under prior accounting guidance, all loan receivables were reclassified to other real estate owned (OREO) when the institution, as creditor, obtained physical possession of the

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property, regardless of whether formal foreclosure proceedings had taken place. The new ASU clarifies when a creditor is considered to have received physical possession (resulting from an in-substance repossession or foreclosure) of residential real estate collateralizing a consumer mortgage loan. Under the new guidance, physical possession for these residential real estate properties is considered to have occurred and a loan receivable would be reclassified to OREO only upon:

- The institution obtaining legal title through foreclosure even if the borrower has redemption rights whereby it can legally reclaim the real estate for a period of time, or
- Completion of a deed-in-lieu of foreclosure or similar legal agreement under which the borrower conveys all interest in the residential real estate property to the institution to satisfy the loan.

Real estate-secured loans other than consumer mortgage loans collateralized by residential real estate should continue to be reclassified to OREO when the institution has received physical possession of a borrower's assets, regardless of whether formal foreclosure proceedings take place.

The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. However, nonpublic entities, as defined under generally accepted accounting principles, are not required to apply the guidance in the ASU to interim periods in the year of adoption.

Early adoption is permitted under the standard. Edge and agreement corporations electing to early adopt should include as other real estate owned on Schedule RC, item 8, all residential real estate collateral underlying consumer mortgage loans when the institution has obtained physical possession of the collateral as defined under ASU 2014-04. Edge and agreement corporations should report the cumulative effect of a change in accounting principle¹ in Schedule RI-A, item 6. Edge and agreement corporations can elect to apply the ASU on either a modified retrospective transition basis or a prospective transition basis. Under the modified retrospective transition method, an institution should apply a cumulative-effect adjustment to residential consumer mortgage loans and OREO existing as of the beginning of the annual period for which the amendments are effective. As a result of adopting the ASU, assets reclassified from OREO to loans should be measured at the carrying value of the real estate at the date of adoption while assets reclassified from loans to OREO should be measured at the lower of the

¹ The cumulative effect of a change in accounting principle is the difference between (1) the balance in the retained earnings account at the beginning of the year in which the change is made and (2) the balance in the retained earnings account that would have been reported at the beginning of the year had the newly adopted accounting principle been applied in all prior periods.

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net amount of loan receivable or the OREO property's fair value less costs to sell at the time of adoption. Under the prospective transition method, an institution should apply the new guidance to all instances where the institution receives physical possession of residential real estate property collateralized by consumer mortgage loans that occur after the date of adoption.

For additional information, institutions should refer to ASU 2014-04, which is available at <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176156316498>.

Secured Consumer Debt Discharged in a Chapter 7 Bankruptcy Order

Questions have arisen regarding the appropriate accounting and regulatory reporting treatment for certain secured consumer loans where (i) the loan has been discharged in a Chapter 7 bankruptcy under the U.S. Bankruptcy Code², (ii) the borrower has not reaffirmed the debt, (iii) the borrower is current on payments, and (iv) the loan has not undergone a troubled debt restructuring (TDR) before the bankruptcy.

When a debtor files for Chapter 7 bankruptcy, a trustee is appointed to liquidate the debtor's assets for the benefit of creditors. Generally, Chapter 7 bankruptcy results in a discharge of personal liability for certain debts that arose before the petition date. A bankruptcy discharge acts as a permanent injunction of claims against the debtor, but does not extinguish certain secured debt or any existing liens on the property securing the debt.

In general, for certain secured debt, the loan agreement (including the promissory note and, depending on the state, the security interest) entered into before bankruptcy remains in place after the debt has been discharged in a Chapter 7 bankruptcy. However, the lender may no longer pursue the borrower personally for a deficiency due to nonpayment. In addition, the institution's ability to manage the loan relationship is restricted. For example, after a borrower has completed Chapter 7 bankruptcy, an institution is limited with regard to collection efforts, communications with the borrower, loss mitigation strategies, and reporting on the discharged debt to credit bureaus.

The accounting and regulatory reporting issues that arise for secured consumer loans discharged in a Chapter 7 bankruptcy include: (1) whether the discharge is a TDR, (2) the measure of impairment, (3) whether the loan should be placed in nonaccrual status, and (4) charge-off treatment.

² 11 USC Chapter 7

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TDR Determination

In determining whether a secured consumer debt discharged in a Chapter 7 bankruptcy constitutes a troubled debt restructuring, an edge and agreement corporation needs to assess whether the borrower is experiencing financial difficulties and whether a concession has been granted to the borrower. Under Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Subtopic 310-40, a bankruptcy filing is an indicator of a borrower's financial difficulties. Determining whether an edge and agreement corporation has granted a concession in a Chapter 7 bankruptcy requires judgment. In assessing whether a concession has been granted, institutions should consider all relevant facts and circumstances, including the effect of changes to the legal rights and obligations of the lender and the borrower resulting from Chapter 7 bankruptcy. Changes taken as a whole that are not substantive may not be considered a concession. Edge and agreement corporations should refer to the Glossary section of the *Instructions for Preparation of Consolidated Financial Statements for Holding Companies* for additional information on TDRs.

Measure of Impairment

If an edge and agreement corporation has concluded that the completion of a Chapter 7 bankruptcy filing has resulted in a TDR, the loan should be measured for impairment under ASC Section 310-10-35 (formerly FASB Statement No. 114, "Accounting by Creditors for Impairment of a Loan"). Under this guidance, impairment shall be measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, an edge and agreement corporation may measure impairment based on a loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. For regulatory reporting purposes, edge and agreement corporations must measure impairment based on the fair value of the collateral when an impaired loan is determined to be collateral dependent. A loan is considered to be collateral dependent if repayment of the loan is expected to be provided solely by the underlying collateral and there are no other available and reliable sources of repayment. Judgment is required to determine whether an impaired loan is collateral dependent, and an edge and agreement corporation should assess all available credit information and weigh all factors pertaining to the loan's repayment sources.

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If repayment of an impaired loan is not solely dependent upon the underlying collateral, impairment would be measured based on the present value of expected future cash flows. ASC Section 310-10-35 allows impaired loans to be aggregated and measured for impairment with other impaired loans that share common risk characteristics.

Discharged secured consumer debts that are not TDRs (or are not otherwise determined to be in the scope of ASC 310-10 and held for investment) should be measured collectively for impairment under ASC Subtopic 450-20 (formerly FASB Statement No. 5, “Accounting for Contingencies”). In estimating the allowance for loan and lease losses (ALLL) under ASC Subtopic 450-20, edge and agreement corporations should consider all available evidence and weigh all factors that affect the collectability of the loans as of the evaluation date. Factors can include the bankruptcy filing, delinquent senior liens, negative equity in the collateral, and sustained timely payment performance by the borrower.

Edge and agreement corporations should ensure that loans are properly segmented based upon similar risk characteristics when calculating the allowance under ASC Subtopic 450-20. Borrowers of secured consumer debt discharged in a Chapter 7 bankruptcy generally are considered to have a higher credit risk profile than those borrowers that have not filed for Chapter 7 bankruptcy. For edge and agreement corporations with significant holdings of these loans to borrowers who have completed a Chapter 7 bankruptcy, it is appropriate to segment these mortgage loans separately from pools of mortgage loans to borrowers who have not filed for Chapter 7 bankruptcy when calculating the allowance. Edge and agreement corporations should follow existing regulatory guidance in calculating the ALLL including, if applicable, the *Interagency Supervisory Guidance on Allowance for Loan and Lease Losses Estimation Practices for Loans and Lines of Credit Secured by Junior Liens on 1-4 Family Residential Properties*, which can be accessed at <http://fedweb.frb.gov/fedweb/bsr/srltrs/sr1203.shtm>.

Regardless of the impairment method used, when available information confirms that specific loans, or portions thereof, are uncollectible, these amounts should be promptly charged off against the allowance for loan and leases losses.

Accrual Status

Edge and agreement corporations should follow the Call Report (FFIEC 031/41) Glossary entry under “Nonaccrual Status” when determining whether secured consumer debt discharged in a Chapter 7 bankruptcy should be on accrual status. These instructions also address the restoration of nonaccrual assets, including any loans identified as TDRs that are in nonaccrual status, to accrual status.

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Consistent with GAAP and regulatory guidance, institutions are expected to follow revenue recognition practices that do not result in overstating income. For a secured consumer loan discharged in a Chapter 7 bankruptcy, whether or not it is a TDR, placing the loan on nonaccrual when payment in full of principal and interest is not expected is one appropriate method to ensure income is not overstated.

Charge-off Treatment

GAAP states that loans shall be charged off in the period in which the loans are deemed uncollectible. Because of heightened risk that loans discharged through bankruptcy may be uncollectible, the interagency *Uniform Retail Credit Classification and Account Management Policy* (Uniform Retail Credit Policy) requires such loans to be charged down to collateral value (less costs to sell) within 60 days of notification from the bankruptcy court unless the institution can clearly demonstrate and document that repayment is likely to occur. To assess whether such a loan should be deemed uncollectible, an edge and agreement corporation should perform a credit analysis at the time a borrower whose loan is current completes Chapter 7 bankruptcy (hereafter, a post-discharge analysis). If the post-discharge analysis indicates repayment of principal and interest is likely to continue, then immediate charge down to collateral value and full application of payments to reduce the recorded investment in the loan is not required.

If a credit analysis does not support that repayment of principal and interest is likely to continue, the loan should be charged down to the collateral's fair value (less costs to sell). Any balance not charged off should be placed on nonaccrual when full collection of principal and interest is not expected. The Uniform Retail Credit Policy can be accessed at <http://fedweb.frb.gov/fedweb/bsr/srltrs/SR0008.htm>.

As discussed in the Uniform Retail Credit Policy, evaluating the quality of a retail credit portfolio on a loan-by-loan basis is inefficient and burdensome for the institution being examined and for examiners given the generally large number of relatively small-balance loans in a retail credit portfolio. Therefore, the type of credit analysis that is performed to assess whether repayment is likely to continue may vary depending on whether the loans are managed individually or on a homogenous pool basis.

For loans managed in pools, edge and agreement corporations may choose to evaluate the likelihood of continued repayment on a pool basis. In order for a pool analysis to be used, an edge and agreement corporation must identify various credit risk indicators that signify likelihood of continuing repayment. Such indicators might include measures of historical payment performance, loan structure, lien position, combined loan-to-value ratios, amounts paid over the minimum payment due and other pertinent factors that have been associated with

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payment performance in the past. Such credit risk indicators should then be considered as a whole when determining whether objective evidence supports the likelihood of continuing repayment. An edge and agreement corporation using pool-based analysis should also conduct ongoing monitoring to ensure the appropriateness of the credit risk indicators used to support the likelihood of continuing repayment.

For all loans managed individually and any loans managed on a pool basis where the pool analysis does not support likelihood of continuing repayment, a loan-level, post-discharge credit analysis would be necessary to support likelihood of continuing repayment. A loan-level, post-discharge analysis should demonstrate and document structured orderly collection, post-discharge repayment capacity, and sustained payment performance. If likelihood of continuing repayment cannot be supported, the loan should be deemed uncollectable and charged down to collateral value (less costs to sell) within 60 days of notification from the bankruptcy court.

Determining the Fair Value of Derivatives

ASC Topic 820, Fair Value Measurement (formerly FASB Statement No. 157, “Fair Value Measurements”), defines fair value and establishes a framework for measuring fair value. As stated in ASC Topic 820, fair value is a market-based measurement, not an entity-specific measurement, and the fair value of a derivative position should be measured using the assumptions that market participants would use when pricing that position, including assumptions about risks. An entity should select inputs that are consistent with the characteristics of the derivative position that market participants would take into account in a transaction for the derivative asset or liability. In the absence of a Level 1 input, an entity should apply an adjustment, such as a premium or discount, when market participants would do so when determining the fair value of a derivative position, consistent with the unit of account. For derivatives, the unit of account generally is the individual transaction unless an entity has made an accounting policy decision to apply the exception in ASC Topic 820 pertaining to measuring the fair value of a group of financial instruments the entity manages on the basis of its net exposure to either market risks or credit risks.

When measuring the fair value of a derivative position that has a bid-ask spread, ASC Topic 820 does not preclude the use of mid-market pricing or other pricing conventions as a practical expedient for measuring the fair value within the bid-ask spread. An entity should determine the price within the bid-ask spread that is most representative of fair value, which is the price that would be received to sell the asset or paid to transfer the liability (i.e., an exit price), based on assumptions a market participant would use in a similar circumstance. An institution should maintain documented policies for determining the point within the bid-ask spread that is most representative of fair value and consistently apply those policies.

An entity is expected to apply all of its valuation policies and techniques for measuring fair value consistently over time. Nevertheless, ASC Topic 820 acknowledges that a change in valuation technique from one methodology to another that results in an equally or more representative measure of the fair value of a derivative position may be appropriate. However, it would be inappropriate for an entity to alter its valuation methodology or policies to achieve a desired financial reporting outcome. An example of an inappropriate change in valuation methodology that would result in a fair value estimate not representative of a derivative position's exit price would be for an entity to migrate from using a mid-market pricing convention to using a price within the bid-ask spread that is more advantageous to the entity to offset the impact of adverse changes in market prices or otherwise mask losses.

Unless its fair value measurement is categorized within Level 1, if there has been a change in valuation technique for a derivative position, ASC Topic 820 requires an entity to disclose that change and the reasons for making it in the notes to financial statements prepared in accordance with U.S. generally accepted principles.

“Purchased” Loans Originated By Others

When acquiring loans originated by others, institutions should consider whether the transaction should be accounted for as a purchase of the loans or as a secured borrowing in accordance with Accounting Standards Codification (ASC) Topic 860, Transfers and Servicing (formerly FASB Statement No. 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,” as amended). For the transaction to qualify for sale accounting:

- First, unless the transfer is of an entire financial asset, the transferred portion of the financial asset must meet the definition of a participating interest.
- Second, the transfer must meet all of the conditions set forth in Subtopic 860-10 to demonstrate that the transferor has surrendered control over the transferred financial assets.

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For example, some institutions have entered into various residential mortgage loan purchase programs. These programs often function like traditional warehouse lines of credit; however, in some cases, the mortgage loan transfers are legally structured as purchases by the institution rather than as pledges of collateral to secure the funding. Under these programs, an institution provides funding to a mortgage loan originator while simultaneously obtaining an interest in the mortgage loans subject to a takeout commitment. A takeout commitment is a written commitment from an approved investor (generally, an unrelated third party) to purchase one or more mortgage loans from the originator.

Although the facts and circumstances of each program must be carefully evaluated to determine the appropriate accounting, an institution should generally account for a mortgage purchase program with continuing involvement by the originator, including takeout commitments, as a secured borrowing with pledge of collateral, i.e., a loan to the originator secured by the residential mortgage loans, rather than a purchase of mortgage loans.

When loans obtained in a mortgage purchase program do not qualify for sale accounting, the financing provided to the originator (if not held for trading purposes) should be reported on the FR 2886b Report Schedule RC-C, item 5, "All other loans", and on the balance sheet Schedule RC, item 4.a, "Loans and leases, net of unearned income".

Indemnification Assets and Accounting Standards Update No. 2012-06

In October 2012, the FASB issued Accounting Standards Update (ASU) No. 2012-06, "Subsequent Accounting for an Indemnification Asset Recognized at the Acquisition Date as a Result of a Government-Assisted Acquisition of a Financial Institution," to address the subsequent measurement of an indemnification asset recognized in an acquisition of a financial institution that includes a loss-sharing agreement. This ASU amends ASC Topic 805, Business Combinations (formerly FASB Statement No. 141 (revised 2007),"Business Combinations").

Under the ASU, when an institution experiences a change in the cash flows expected to be collected on a loss-sharing indemnification asset because of a change in the cash flows expected to be collected on the assets covered by the loss-sharing agreement, the institution should account for the change in the measurement of the indemnification asset on the same basis as the change in the assets subject to indemnification. Any amortization of changes in the value of the indemnification asset should be limited to the lesser of the term of the indemnification agreement and the remaining life of the indemnified assets.

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The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2012. For institutions with a calendar year fiscal year, the ASU takes effect January 1, 2013. The ASU's provisions should be applied prospectively to any new indemnification assets acquired after the date of adoption and to indemnification assets existing as of the date of adoption arising from a government-assisted acquisition of a financial institution. Institutions with indemnification assets arising from loss-sharing agreements are expected to adopt ASU 2012-06 for FR 2886b reporting purposes in accordance with the effective date of this standard.

For additional information, institutions should refer to ASU 2012-06, which is available at <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176156316498>.

True-up Liability under an FDIC Loss-Sharing Agreement

As discussed above, an institution that acquires a failed insured institution may enter into a loss-sharing agreement with the FDIC under which the FDIC agrees to absorb a portion of the losses on a specified pool of the failed institution's assets during a specified time period. The acquiring institution typically records an indemnification asset representing its right to receive payments from the FDIC for losses during the specified time period on assets covered under the loss-sharing agreement.

Since 2009, most loss-sharing agreements have included a true-up provision that may require the acquiring institution to reimburse the FDIC if cumulative losses in the acquired loss-share portfolio are less than the amount of losses claimed by the institution throughout the loss-sharing period. Typically, a true-up liability may result because the recovery period on the loss-share assets (e.g., eight years) is longer than the period during which the FDIC agrees to reimburse the acquiring institution for losses on the loss-share portfolio (e.g., five years).

Consistent with U.S. GAAP and the Glossary entry for "Offsetting" in the FR Y-9C instructions, institutions are permitted to offset assets and liabilities recognized in the Report of Condition when a "right of setoff" exists. Under ASC Subtopic 210-20, Balance Sheet – Offsetting (formerly FASB Interpretation No. 39, "Offsetting of Amounts Related to Certain Contracts"), in general, a right of setoff exists when a reporting institution and another party each owes the other determinable amounts, the reporting institution has the right to set off the amounts each party owes and also intends to set off, and the right of setoff is enforceable at law. Because the conditions for the existence of a right of offset in ASC Subtopic 210-20 normally would not be met with respect to an indemnification asset and a true-up liability under a loss-sharing agreement with the FDIC, this asset and liability should not be netted for FR 2886b reporting purposes.

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Troubled Debt Restructurings and Current Market Interest Rates

Many institutions are restructuring or modifying the terms of loans through workout programs, renewals, extensions, or other means to provide payment relief for those borrowers who have suffered deterioration in their financial condition. Such loan restructurings may include, but are not limited to, reductions in principal or accrued interest, reductions in interest rates, and extensions of the maturity date. Modifications may be executed at the original contractual interest rate on the loan, a current market interest rate, or a below-market interest rate. Many of these loan modifications meet the definition of a troubled debt restructuring (TDR).

The TDR accounting and reporting standards are set forth in ASC Subtopic 310-40, Receivables - Troubled Debt Restructurings by Creditors (formerly FASB Statement No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings," as amended). This guidance specifies that a restructuring of a debt constitutes a TDR if, at the date of restructuring, the creditor for economic or legal reasons related to a debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The creditor's concession may include a restructuring of the terms of a debt to alleviate the burden of the debtor's near-term cash requirements, such as a modification of terms to reduce or defer cash payments required of the debtor in the near future to help the debtor attempt to improve its financial condition and eventually be able to pay the creditor.

The stated interest rate charged the borrower after a loan restructuring may be greater than or equal to interest rates available in the marketplace for similar types of loans to nontroubled borrowers at the time of the restructuring. Some institutions have concluded that these restructurings are not TDRs; however, this conclusion may be inappropriate. In reaching this conclusion, these institutions may not have considered all of the facts and circumstances associated with the loan modification besides the interest rate. An interest rate on a modified loan greater than or equal to those available in the marketplace for similar credits does not in and of itself preclude a modification from being designated as a TDR. Rather, when evaluating a loan modification to a borrower experiencing financial difficulties, an analysis of all facts and circumstances is necessary to determine whether a concession was made to the borrower with respect to the market interest rate or has made some other type of concession that could trigger TDR accounting and disclosure (for example, terms or conditions outside of the institution's policies or common market practices). If TDR accounting and disclosure is appropriate, the edge and agreement corporation must determine how the modified or restructured loan should be reported.

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A loan restructured in a TDR is an impaired loan. Thus, all TDRs must be measured for impairment in accordance with ASC Subtopic 310-10, Receivables – Overall (formerly FASB Statement No. 114, “Accounting by Creditors for Impairment of a Loan,” as amended”).

Troubled Debt Restructurings and Accounting Standards Update No. 2011-02

In April 2011, the FASB issued Accounting Standards Update (ASU) No. 2011-02, “A Creditor’s Determination of Whether a Restructuring Is a Troubled Debt Restructuring,” to provide additional guidance to help creditors determine whether a concession has been granted to a borrower and whether a borrower is experiencing financial difficulties. The guidance is also intended to reduce diversity in practice in identifying and reporting TDRs.

Edge and agreement corporations are expected to apply the guidance in ASU No. 2011-02 and continue to follow the accounting and reporting guidance on TDRs in the FR 2886b Instruction book. To the extent the guidance in the ASU differs from an edge or agreement corporation’s existing accounting policies and practices for identifying TDRs, edge and agreement corporations will be expected to apply the ASU for FR 2886b reporting purposes in accordance with the standard’s effective date and transition provisions, which are outlined above. To the extent that an edge or agreement corporation’s existing accounting policies and practices are consistent with guidance in the ASU, edge and agreement corporations should continue to follow its existing policies and practices.

ASU 2011-02 reiterates that the two conditions mentioned in the preceding section on “Troubled Debt Restructurings and Current Market Interest Rates” must exist in order for a loan modification to be deemed a TDR: (1) a company must grant a concession to the borrower as part of the modification and (2) the borrower must be experiencing financial difficulties. The ASU explains that a company may determine that a borrower is experiencing financial difficulties if it is probable that the borrower will default on any of its debts in the foreseeable future. The borrower does not have to be in default at the time of the modification. Other possible factors that should be considered in evaluating whether a borrower is experiencing financial difficulties is if the borrower has declared (or is in the process of declaring) bankruptcy, the creditor does not expect the borrower’s cash flows to be sufficient to service its debt under the existing terms, or there is substantial doubt about an entity’s ability to continue as a going concern.

Another important aspect of the ASU is that it prohibits financial institutions from using the effective interest rate test included in the TDR guidance for borrowers in ASC Subtopic 470-60, Debt – Troubled Debt Restructurings by Debtors, when determining whether the creditor has granted a concession as part of a loan modification. However, as explained in ASU 2011-02, if a borrower does not have access to funds at a market rate of interest for similar

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debt, the rate on the modified loan is considered to be a below-market rate and may be an indicator that the company has granted a concession to the borrower.

Furthermore, the ASU provides guidance regarding insignificant delays in payment as part of loan modification. If, after analysis of all facts and circumstances, a creditor determines that a delay in payment is insignificant, the creditor has not granted a concession to the borrower. This determination requires judgment and should consider many factors, including, but not limited to, the amount of the delayed payments in relation to the loan's unpaid principal or collateral value, the frequency of payments due on the loan, the original contractual maturity, and the original expected duration of the loan.

For additional information, edge and agreement corporations should refer to ASU 2011-02, which is available at <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176156316498>.

Reporting Data for Term Deposits

The Term Deposit Facility (TDF) is a program through which the Federal Reserve Banks offer interest-bearing term deposits to eligible institutions. A term deposit is a deposit with a specific maturity date. For FR 2886b reporting purposes, term deposits offered through the TDF should be treated as balances due from a Federal Reserve Bank. Accordingly, term deposits should be reported in Schedule RC, Balance Sheet, item 1.b, "Cash and balances due from depository institutions: Interest bearing balances". The earnings on these term deposits should be reported in Schedule RI, item 1.a.(2), "Interest on balances due from depository institutions."

Goodwill Impairment Testing

Edge and agreement corporations should continue to follow the guidance regarding reporting related to goodwill impairment testing that was included in the FR 2886B transmittal letter for March, 31 2014. These instructions can be assessed via the Federal Reserve's Web site (<http://www.newyorkfed.org/banking/regrept/1q14fr2886.pdf>).

Subscription Service

We offer a 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 service at the following website:

https://public.govdelivery.com/accounts/USFRBNEWYORK/subscriber/new?topic_id=USFRBNEWYORK_8

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Reports Submission

Please note that the timeliness of receipt of the report will be monitored and that submission of initial data via facsimile, even if prior to the deadline, does not constitute timely filing.

The FR 2886b report must be returned to this Bank, by mail or messenger, no later than **January 30, 2015**. Any FR 2886b report received after 5:00 p.m. on **January 30, 2015** will be considered late unless postmarked by **January 27, 2015** or sent by overnight service by **January 29, 2015**.

Electronic Submission Option

Electronic submission of the FR 2886b report through Reporting Central is now available to all edge and agreement corporations. We encourage you to take advantage of this method of report submission. Submitting reports electronically 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 FR 2886b report electronically, please contact the respective Staff Directors of the Capital and Liquidity & Funding Division: Ken Aberbach at (212) 720-8234, Lesley Chao at (212) 720-5429, Morgan Norful at (212) 720-8055, or Cheryl Skillman at (212) 720-8739.

The completed report 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 December 31, 2014 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".

FEDERAL RESERVE BANK *of* NEW YORK

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Website

The FR 2886b forms and instructions are available on the FFIEC website at:
www.federalreserve.gov/boarddocs/reportforms/

Questions regarding the FR 2886b should be directed to the respective Staff Directors of the Capital and Liquidity & Funding Division: Ken Aberbach at (212) 720-8234, Lesley Chao at (212) 720-5429, Morgan Norful at (212) 720-8055, or Cheryl Skillman at (212) 720-8739.

Sincerely,

Patricia Selvaggi
Assistant Vice President

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ATTACHMENT

Revisions to the FR 2886b for the quarter ended December 31, 2014

Reporting Form

(1) *None.*

Reporting Form Instructions

(1) *None.*