

this information would likely be found in the risk management disclosure in management's discussion and analysis (MD&A) of large BHCs Form 10-K and Form 10-Q filed with the SEC and usually available on the BHC's website.

#### **Schedule HC—Regulatory Capital**

The Federal Reserve proposes to make the following changes to Schedule HC—R, Regulatory Capital.

1. Remove the caption for memoranda item 3.a, "Perpetual preferred stock eligible for inclusion in Tier 1 capital:" and modify the caption for memoranda item 3 to read "Preferred stock (including related surplus) eligible for inclusion in Tier 1 capital:."

2. Renumber memoranda item 3.a(1) as item 3.a and modify the caption to include a clarifying parenthetical note. The caption would read "Noncumulative perpetual preferred stock (included and reported in "Total equity capital," on Schedule HC)."

3. Renumber memoranda item 3.a(2) as item 3.b and modify the caption to include a clarifying parenthetical note. The caption would read "Cumulative perpetual preferred stock (included and reported in "Total equity capital," on Schedule HC)."

4. Modify current memoranda item 3.b, "Cumulative preferred stock (e.g., trust preferred securities) included and reported in "Minority interest in consolidated subsidiaries and similar items," on Schedule HC" and renumber as 3.d. The revised caption would read "Other cumulative preferred stock eligible for inclusion in Tier 1 capital (e.g., trust preferred securities) (included in Schedule HC, items 20 or 22)." This item would include trust preferred stock eligible for Tier 1 capital that is issued out of a special purpose subsidiary for which the bank holding company is the sole common shareholder, and that is reflected in Schedule HC, item 20, "Other liabilities." This item would also include any other cumulative preferred stock included in Schedule HC, item 22, "Minority interest in consolidated subsidiaries and similar items."

5. Add a new memoranda item 3.c, "Other noncumulative preferred stock eligible for inclusion in Tier 1 capital (e.g., REIT preferred securities) (included in Schedule HC, item 22)."

The Federal Reserve proposes the first three changes to clarify existing items and proposes the fourth change for consistency with the proposed changes to Schedule HC, Balance Sheet, on trust preferred securities. The Federal Reserve proposes the fifth change, the addition of new memoranda item 3.c, to collect information on real estate investment trust (REIT) preferred

securities. REIT preferred securities are a type of innovative capital instrument typically issued from a special purpose subsidiary at the bank level. Qualifying REIT preferred securities may be included in bank Tier 1 capital with a limit of up to 25 percent of Tier 1. Currently no data are collected for REIT instruments on financial reports at either the bank or BHC level. Therefore the Federal Reserve does not have comprehensive information on the amount of these instruments in banks' or BHCs' capital structures. The Federal Reserve has learned through available anecdotal information that a number of large banking organizations have made issuances of over \$500 million. This item would also include any other noncumulative preferred stock included in Schedule HC, item 22, "Minority interest in consolidated subsidiaries and similar items."

#### **Instructions**

Instructional revisions and clarifications will be made to FR Y-9C, FR Y-9LP, FR Y-9SP, and FR Y-9ES, as necessary, in an attempt to achieve greater consistency in reporting by respondents.

#### **Proposed Revisions Effective September 30, 2004 and December 31, 2004**

##### **Editing of Data by Respondents**

The Federal Reserve proposes to require data validation checks to be performed by respondents as a condition for the accepted filing of the FR Y-9 reports (except for the FR Y-9CS). Implementation of this requirement is targeted as of the September 30, 2004, reporting date for FR Y-9C and FR Y-9LP respondents, and as of the December 31, 2004, reporting date for FR Y-9SP and FR Y-9ES respondents. The proposed changes are also consistent with the proposed data validation process for the Call Report, also targeted for September 2004.

Currently, after the Federal Reserve receives a bank holding company (BHC) report, it is subjected to edit checks to assess the accuracy and reasonableness of the data submitted. "Validity" edits verify the accuracy of reported data, for example, whether the individual items in a report schedule add up to the reported total or whether an item reported in one schedule agrees with the amount reported for an equivalent item in another schedule. Validity edits include mathematical and logical tests. "Quality" edits test the reasonableness of data and include tests using historical data and other relational tests, for example, whether the amount reported for a year "to" date item is greater than or equal to the amount reported for the same item in the previous quarter or

whether the fair value reported for a category of securities falls within a specified range of the amortized cost reported for these securities. Also certain quality or "interseries" edits compare data reported on parent "only" statements (FR Y-9LP) and data reported on the consolidated bank holding company statements (FR Y-9C).<sup>1</sup>

If this validation process identifies any edit exceptions in a BHC's report, a Federal Reserve analyst may contact the BHC and explain the edit exceptions detected in the BHC's report. The BHC then reviews the reported data associated with these edit exceptions and provides the Federal Reserve analyst with any necessary corrections or describes the underlying facts and circumstances that explain why the data are correct as reported.

Under this proposal, the validation process will take place in conjunction with a BHC's submission of its FR Y-9 reports. The Federal Reserve's internet-based data collection system will subject a respondent's electronic data submission, whether by data entry or by file transfer, to published validity and quality edit checks and transmit the results of such checks to the respondent.<sup>2</sup> Companies that offer computer software to aid in the preparation of FR -9 reports or BHCs that have developed their own reporting software may also choose to incorporate validity and quality edit checks into their software. Thus edit exceptions will be identified while a BHC is preparing its report or during the submission process. The BHC will then be expected to correct its report data to eliminate any validity edit exceptions. The BHC will also be provided a method for supplying explanatory comments concerning quality edit exceptions. The Federal Reserve would not accept any submission as fulfilling reporting requirements or meeting the filing deadline that fails any validity edits or lacks explanatory comments concerning any quality edit exceptions.<sup>3</sup>

Because a BHC will be made aware of any edit exceptions while its staff is completing its FR Y-9 report, the BHC

<sup>1</sup> A list of validity and quality edits (including interseries edits) is located at the end of the instructions to the FR Y-9 reports (except for the FR Y-9CS), and validity edits are currently distributed to respondents in the form of a Reports Monitoring Checklist.

<sup>2</sup> Note that due to interseries comparisons between the FR Y-9LP and the FR Y-9C, the FR Y-9LP cannot be processed until the FR Y-9C is accepted.

<sup>3</sup> The data collection system will provide for acceptance of data that in rare situations may fail a validity edit due to unusual circumstances but have been identified as accurate.