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Although economic activity had increased substantially in 2003, the expansion nevertheless appeared somewhat tentative as 2004 opened, in large measure because businesses still seemed to be reluctant to boost hiring. Over the course of the spring, however, it became clearer that the expansion was solidifying. With slack in labor and product markets somewhat diminished, the Federal Open Market Committee at its June meeting began to reduce the substantial degree of monetary accommodation that was in place. The gradual removal of monetary policy stimulus continued in the second half of the year as the economy expanded at a healthy clip on balance. The fundamental factors underlying the continued strength of the economy last year should carry forward into 2005 and 2006, promoting both healthy expansion of activity and low inflation.

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175 *BACKGROUND ON FOMC MEETING MINUTES*

On December 14, 2004, the Federal Open Market Committee (FOMC) decided to move up the publication of its minutes to three weeks after the end of each meeting. That action has cut in half the average time between the meeting and publication of the minutes. It has also apparently heightened public attention to the FOMC minutes. To give additional context to the Committee's decision, this article outlines previous changes to the release schedule for the minutes and provides a brief overview of the content of the minutes and the way they are now produced.

180 *TRENDS IN THE USE OF PAYMENT INSTRUMENTS IN THE UNITED STATES*

In 2003, for the first time, the number of electronic payments in the United States exceeded the number of check payments—a result of sub-

stantial growth in electronic payments (especially by debit card) and a decline in check payments. The shift toward electronic payments suggests that, as with other large economies, many payments formerly made by check are now being made with electronic payment instruments. As in past years, however, the value of checks far exceeded the value of commonly used electronic payments.

Comparisons among groups of depository institutions of different types and sizes suggest that the distribution of payments of different types is linked in part to the types of customers those institutions tend to serve. For example, at credit unions, which generally serve individuals rather than businesses, checks accounted for a smaller proportion of account debits, and debit card payments and ATM withdrawals accounted for a larger proportion, than at institutions of other types.

Overall, "on us" check payments, those for which the payer and payee used the same institution, declined slightly. The rate at which checks are returned also declined, while the rate of returned ACH payments—almost twice that of checks—increased, in part because of new types of ACH payments, including ACH transactions initiated with a check.

Data gathered in 2004 also reveal some differences among geographic regions. Debit card use was substantially greater, and check use substantially lower, in the West than in other regions. In contrast, debit card use was considerably less common in the Northeast, and the decline in check payments since 2000 was less pronounced in that region.

Indirect evidence—data on ATM withdrawals and cash back from debit card payments—suggests that cash remains a popular means of making payments. Industry data showing increases in ATMs and ATM transactions appear to reflect a shift toward greater use of ATMs and less use of checks to obtain cash, and do not necessarily indicate an increase in the use of cash.

202 *COMMUNITY BANKS AND RURAL DEVELOPMENT: RESEARCH RELATING TO PROPOSALS TO REVISE THE REGULATIONS THAT IMPLEMENT THE COMMUNITY REINVESTMENT ACT*

Since 1977, the Community Reinvestment Act (CRA) has required that federally insured banking institutions be evaluated on their records of helping to meet the credit needs of their local communities. In 1995, the agencies responsible for bank supervision substantially revised the regulations that implement the CRA. The revisions were intended to emphasize performance rather than process, to reduce unnecessary regulatory burden, and to increase consistency in CRA evaluations. Since 1995, "large" institutions, generally those with assets of $250 million or more, have been evaluated under a three-part test, whereas "small" institutions, generally those with assets of less than $250 million, have been subject to comparatively streamlined evaluations.

In 2004 and 2005, the agencies put forth several proposals to extend the eligibility for streamlined examinations and an exemption from data reporting to more institutions by raising the asset-size threshold from $250 million to $500 million or $1 billion. A related issue that the agencies raised was how to define which bank activities in rural areas should be considered community development in CRA evaluations. In this article, the authors, having evaluated data to gain insight into the potential effects of these proposals, report the findings of their research.

236 *REPORT ON THE CONDITION OF THE U.S. BANKING INDUSTRY: FOURTH QUARTER, 2004*

Assets of reporting bank holding companies rose $393.2 billion (or 4.0 percent), exceeding $10.0 trillion for the first time. Loans, which accounted for roughly half the increase, rose 3.5 percent, led by the commercial real estate, home equity, and credit card categories. Nearly all the growth occurred at the fifty large institutions. The increase of 4.7 percent in securities and money market assets was largely attributable to the addition of a single large foreign-owned securities-oriented firm with significant portfolios of trading and short-term money market assets.

Deposits increased 3.7 percent, while nondeposit borrowings increased 2.5 percent; the latter influenced by the addition of the large securities-oriented bank holding company. Net income declined 1.4 percent from the previous quarter despite the increases in loans and other interest-earning assets, in part because a flatter yield curve and heightened competitive pressure in

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Monetary Policy Report to the Congress

Report submitted to the Congress on February 16, 2005, pursuant to section 2B of the Federal Reserve Act

MONETARY POLICY AND THE ECONOMIC OUTLOOK

The year 2004 was marked by continued expansion in economic activity and appreciable gains in employment. With fiscal policy stimulative, monetary policy accommodative, and financial conditions favorable, household spending remained buoyant and businesses increased investment in capital equipment and inventories, despite the restraint imposed by sizable increases in oil prices. Labor market conditions improved significantly, albeit at an uneven pace, and productivity rose notably further. Consumer price inflation moved higher with the surge in energy prices, but core consumer price inflation (that is, excluding food and energy) remained well contained, and measures of expected inflation over longer horizons held steady or edged lower.

Although economic activity had increased substantially in 2003, the expansion nevertheless appeared somewhat tentative as 2004 opened, in large measure because businesses still seemed to be reluctant to boost hiring. Over the course of the spring, however, it became clearer that the expansion was solidifying. Businesses added appreciably to their payrolls, boosted investment in equipment and software, and started restocking inventories. While household spending growth softened somewhat, residential construction expanded rapidly. Rising energy prices boosted overall consumer price inflation, and core inflation moved up as well. In response to positive economic news and higher inflation during this period, market participants came to anticipate that monetary policy tightening would begin sooner than they had expected, and interest rates increased considerably. With the economic expansion more firmly established and slack in labor and product markets somewhat diminished, the Federal Open Market Committee (FOMC) at its June meeting began to reduce the substantial degree of monetary accommodation that was in place.

The gradual removal of monetary policy stimulus continued in the second half of the year as the economy expanded at a healthy clip on balance. Around midyear, some measures of growth in activity softened, partly because of the drain on income and the rise in business costs created by higher oil prices. The expansion of consumer spending slowed in the spring, and the pace of hiring and gains in industrial production dropped back notably during the summer. Equity prices and longer-term interest rates moved lower over this period as well. In the event, the slowdown in household spending growth proved short lived. Both hiring and increases in factory output stepped up again in the autumn, and these gains were extended early this year. With profits healthy and financial conditions still supportive, capital spending increased at a brisk pace throughout the year. Over the final quarter of 2004, short-term interest rates rose further as monetary policy was firmed at each FOMC meeting, but long-term interest rates were largely unchanged. Equity prices rose appreciably in the fourth quarter, and the dollar depreciated against most other major currencies. The FOMC increased the target federal funds rate 25 basis points again at its meeting this month, bringing the cumulative tightening over the past year to 1½ percentage points.

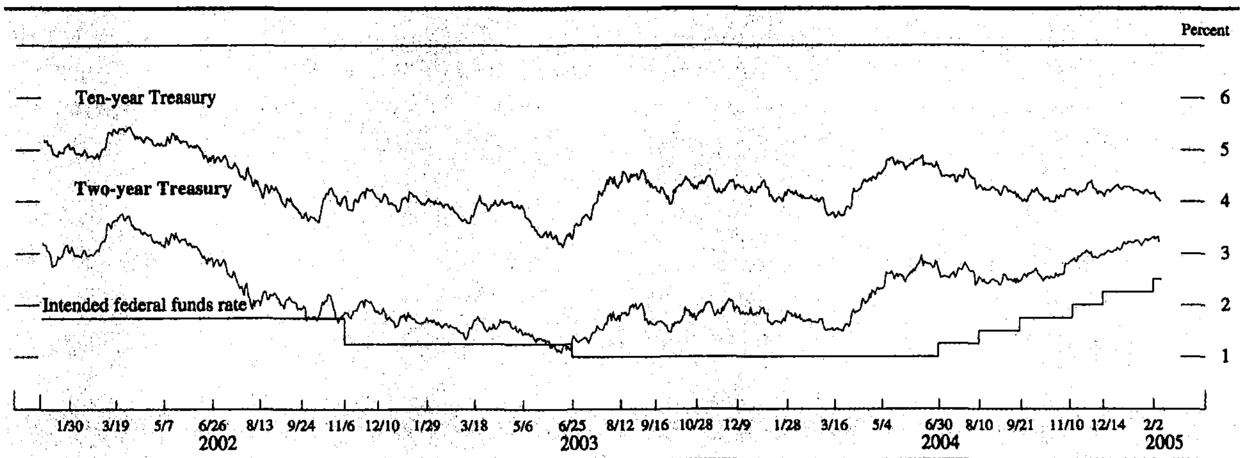
The fundamental factors underlying the continued strength of the economy last year should carry forward into 2005 and 2006, promoting both healthy expansion of activity and low inflation. Monetary policy is still accommodative, and financial conditions more generally continue to be advantageous for households and firms. Profits have been rising briskly, and corporate borrowing costs are low. Household net worth has increased with the continued sharp rise in the value of real estate assets as well as gains in equity prices, and this will likely help support consumer demand in the future. Absent a significant increase in oil prices from current levels, the drag from last year's run-up should wane this year. The lagged effects of the decline in the exchange value of the dollar since the autumn and sustained foreign economic growth are likely to boost the demand for U.S. exports. The prospects for the expansion of aggregate supply also appear to be quite favorable. Gains in structural labor productivity should continue, although not necessarily at the pace of recent years. Economic growth will likely be sufficient to generate notable increases in employment, although any reversal of the decline in labor force participation observed since 2001 would tend to hold up the unemployment rate. Core consumer price inflation has remained low since the larger increases posted in the early months of 2004, and long-term inflation expectations have been similarly well contained. With some slack likely remaining in labor and product markets at present and with the indirect effects of higher oil and import prices diminishing, the prospects for inflation staying low are good. A favorable economic outcome is, of course, not assured, but at the most recent FOMC meeting the Committee again assessed the risks to both output and inflation as balanced. The Committee also reaffirmed that it is prepared to respond to events as necessary in its pursuit of price stability.

Monetary Policy, Financial Markets, and the Economy in 2004 and Early 2005

In early 2004, against the backdrop of stimulative fiscal and monetary policy, continued rapid growth in productivity, and supportive financial market conditions, business outlays appeared to be firming significantly and household spending remained strong. The FOMC became more confident that the economic expansion was likely gaining traction and that the risk of significant further disinflation had been greatly reduced. In these circumstances, it recognized that a highly accommodative stance for monetary policy could not be maintained indefinitely. Nonetheless, the Committee was concerned about the persistently slow pace of hiring and viewed underlying inflation pressures as likely to remain subdued. Accordingly, the Committee left its target for the federal funds rate unchanged at 1 percent at its January and March meetings. However, beginning in January, it modified the language of its policy statement to gain greater flexibility to tighten policy should circumstances warrant by indicating that monetary policy accommodation would eventually have to be removed. At the same time, the Committee suggested that it could be patient in undertaking such actions.

By the time of the May and June FOMC meetings, incoming economic data pointed to a broader and more firmly established expansion, with continued strength in housing markets and business fixed investment. Also, the employment reports for March, April, and May had indicated strong and widespread gains in private nonfarm payrolls, and previous reports for January and February were revised upward significantly. Overall consumer price inflation in the first quarter was faster than it had been a year earlier, and core inflation also increased, in part because of the indirect effects of higher energy prices. The Committee maintained its target for the federal funds rate at 1 percent in May, but on the basis of the evolving outlook for economic activity and prices, it revised its assessment of risks to indicate that the upside and downside risks for inflation had moved into balance. The Committee also stated that monetary policy accommodation could "be removed at a pace that is likely to be measured" to communicate its belief, given its economic outlook, that policy would probably soon need to move toward a more neutral stance, though probably not at a rapid pace. The Committee retained this language at the June meeting while raising its target for the federal funds

Selected interest rates



NOTE. The data are daily and extend through February 9, 2005. Treasury rates are constant-maturity yields based on the most actively traded securities. The dates on the horizontal axis are those of FOMC meetings.

SOURCE. Department of the Treasury and the Federal Reserve.

rate from 1 percent to 1¼ percent and noting that it would "respond to changes in economic prospects as needed to fulfill its obligation to maintain price stability."

The information that the Committee had received by the time of its August meeting indicated that economic growth had softened somewhat earlier in the summer. Although the housing market had remained strong and business outlays had continued to be healthy, consumer spending growth had slowed significantly, and industrial production had begun to level off. Also, the June and July labor market reports revealed that employment growth had slowed considerably. At the same time, core consumer price inflation had moderated in May and June even though sizable increases in food and energy prices continued. However, the Committee believed that the softness in economic activity was caused importantly by higher prices of imported oil and would prove short lived. With financial conditions remaining stimulative, the economy appeared poised to grow at a pace sufficient to trim slack in resource utilization. In that regard, given the unusually low level of the federal funds rate, especially relative to the level of inflation, policymakers noted that significant cumulative policy tightening would likely be needed to meet the Federal Reserve's long-run objectives of price stability and sustainable economic growth. The Committee's decision at the meeting to raise its target for the federal funds rate 25 basis points, to 1½ percent, and to maintain its assessment of balanced risks with respect to sustainable growth and price stability was largely anticipated by financial markets. However, market participants revised up their expectations for the path of the federal funds rate, reportedly because the announcement conveyed a somewhat more optimistic outlook for the economy than many had anticipated.

By the time of the September FOMC meeting, available information suggested that the economy had regained momentum. Real consumer spending bounced back sharply in July after a weak second quarter, and incoming data on industrial production indicated a modest strengthening. Housing activity had increased further, and business outlays had picked up significantly in the second quarter. In addition, the labor market showed signs of improvement in August, as the unemployment rate edged down and nonfarm payrolls grew moderately. Core consumer price inflation slowed in June and July, and a decline in energy prices from record levels pushed down readings on headline inflation. Although the Committee acknowledged that higher oil prices had damped the pace of economic activity around midyear, it nonetheless saw the expansion as still on solid footing. Consequently, the Committee agreed to increase its target for the federal funds rate another 25 basis points, to 1¾ percent; to reiterate its view that the risks to price stability and to sustainable growth were balanced; and to repeat its indication that the removal of policy accommodation would likely proceed at a "measured" pace. The reaction in financial markets to the policy rate decision and the accompanying statement was muted.

The information in hand at the time of the November FOMC meeting generally suggested that the economy had continued to expand at a moderate rate despite the restraint that higher oil prices imparted to real incomes and consumer confidence. Consumer and business spending stayed firm, and the housing market remained buoyant. However, industrial production was about unchanged, and the news on job growth was uneven—lackluster increases in nonfarm payrolls in September were followed by robust expansion in October. Inflation measures were moderate, although up somewhat from one year earlier. On balance, the Committee saw the economy as growing at a pace that would reduce margins of slack in the utilization of resources. The Committee also judged that inflationary pressures would likely be well contained if monetary policy accommodation were gradually withdrawn. The Committee's decision to raise its target for the federal funds rate from 1¾ percent to 2 percent with minimal change in the language in the accompanying statement was largely anticipated by financial markets and elicited little reaction.

At its December meeting, the Committee viewed available information as continuing to indicate that the pace of the economic expansion was sufficient to further reduce the underutilization of resources, despite elevated oil prices. Consumer spending remained solid, investment spending was strong, and manufacturing production showed modest growth. Also, employment gains in October and November were consistent with gradual improvement in the labor market. Meanwhile, core inflation, while above the unusually low rates of late 2003, remained subdued. Accordingly, the Committee voted to raise its target for the federal funds rate 25 basis points, to 2¼ percent, and to retain the previous statement that the removal of policy accommodation would likely be "measured." Investors had largely anticipated the policy rate decision, but a few market participants had reportedly speculated that the Committee would signal increased concern about inflationary pressures. In the absence of any such signal, implied rates on near-dated futures contracts and longer-term Treasury yields declined a few basis points after the release of the December statement.

Also at its December meeting, the Committee considered an accelerated release of the minutes of FOMC meetings. The Committee's practice had been to publish the minutes for each meeting on the Thursday after the next scheduled meeting. The Committee believed that, because the minutes contain a more nuanced explanation of policy decisions than the statement released immediately after each meeting, publishing them on a timelier basis would help market participants interpret economic developments and thereby better anticipate the course of interest rates. Earlier release would also provide a context for the public remarks of individual FOMC members. It was also recognized, however, that financial markets might misinterpret the minutes at times and that earlier release might adversely affect the Committee's discussions and, perhaps, the minutes themselves. After weighing these considerations, the Committee voted unanimously to publish the FOMC minutes three weeks after the day of the policy decision.

The information that the Committee reviewed at its February 2005 meeting indicated that the economy had continued to expand at a steady pace. The labor market showed signs of further improvement, and consumer spending and the housing market remained robust. Industrial production accelerated, particularly at the end of 2004, and growth of business fixed investment was solid in the fourth quarter. Core inflation stayed moderate, and measures of inflation expectations remained well anchored. Given the solid economic expansion and limited price pressures, the Committee voted to continue its removal of policy accommodation by raising its target for the federal funds rate from 2¼ percent to 2½ percent and to essentially repeat the language of the December statement. Futures market quotes indicated that investors had already priced in a 25 basis point increase in the target federal funds rate at the meeting, and market participants reportedly expected no substantive changes to the accompanying statement. Accordingly, the reaction in financial markets to the announcement was minimal.

Economic Projections for 2005 and 2006

Federal Reserve policymakers expect the economy to expand moderately and inflation to remain low in 2005 and 2006.[1] The central tendency of the forecasts of real GDP growth made by the members of the Board of Governors and the Federal Reserve Bank presidents is 3¾ percent to 4 percent over the four quarters of 2005. The civilian unemployment rate is expected to average about 5¼ percent in the fourth quarter of 2005. For 2006, the policymakers project real GDP to increase about 3½ percent, and they expect the unemployment rate to edge down to between 5 percent and 5¼ percent. With regard to inflation, FOMC participants project that the chain-type price index for personal consumption expenditures excluding food and energy (core PCE) will increase between 1½ percent and 1¾ percent both this year and next—about the same as the 1.6 percent increase posted over 2004.

Economic and Financial Developments in 2004 and Early 2005

The economy proved to be sufficiently resilient to maintain solid growth and moderate core inflation in 2004 even as higher oil prices drained consumers' purchasing power and boosted firms' costs. Real

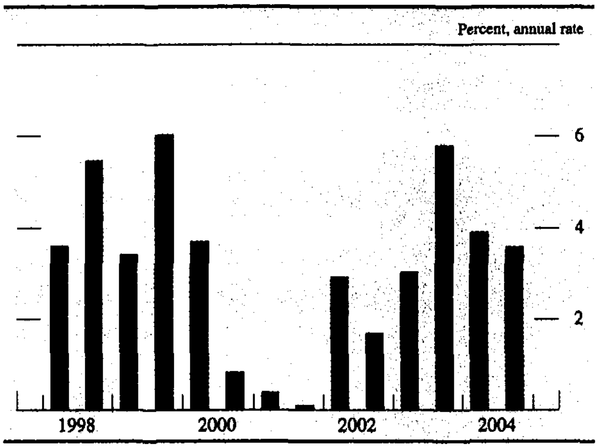
1. As a further step to enhance monetary policy communications, Federal Reserve policymakers will now provide economic projections for two years, rather than one, in the February Monetary Policy Report.

Economic projections for 2005 and 2006
Percent

Indicator	Memo: 2004 actual	Federal Reserve Governors and Reserve Bank presidents			
		2005		2006	
		Range	Central tendency	Range	Central tendency
Change, fourth quarter to fourth quarter[1]					
Nominal GDP	6.2	5–6	5½–5¾	5–5¾	5–5½
Real GDP	3.7	3½–4	3¾–4	3¼–3¾	3½
PCE price index excluding food and energy	1.6	1½–2	1½–1¾	1½–2	1½–1¾
Average level, fourth quarter					
Civilian unemployment rate	5.4	5–5½	5¼	5–5¼	5–5¼

1. Change from average for fourth quarter of previous year to average for fourth quarter of year indicated.

Change in real GDP

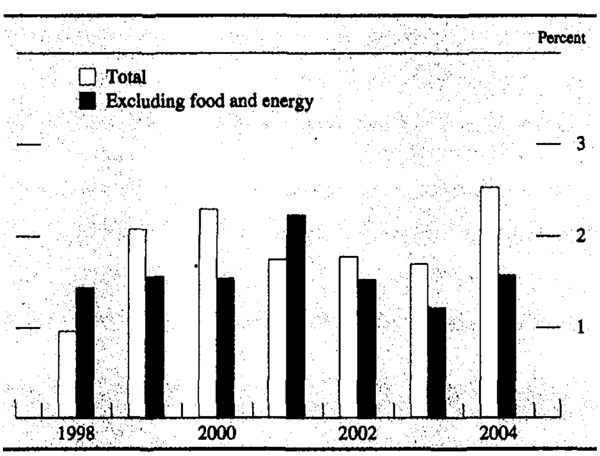


NOTE. Here and in subsequent charts, except as noted, change for a given period is measured to its final quarter from the final quarter of the preceding period.
SOURCE. Department of Commerce, Bureau of Economic Analysis.

GDP rose 3¾ percent last year after having increased 4½ percent in 2003. Activity was supported by continued robust advances in household spending. In addition, capital spending by businesses increased notably. Labor market conditions improved significantly, though at an uneven pace over the course of the year. Private payrolls, which turned up in late 2003, rose 170,000 per month last year, on average, and the unemployment rate declined below 5½ percent by year-end and to 5¼ percent in January 2005—the lowest rates since 2001.

Consumer price inflation was driven higher last year by the sharp rise in energy prices. Although core consumer price inflation moved up somewhat from unusually low levels recorded in 2003, it remained well contained. Price increases were restrained by continuing, though diminishing, slack in labor and product markets, which tended to offset the effects of higher energy and commodity prices, as well as the weaker dollar, on firms' overall costs. In addition, solid productivity gains implied that unit labor costs rose only modestly, even if up from the declines in the preceding two years. The decline in crude oil prices, on balance, since October points to some easing of cost pressures on firms from that source in the period ahead.

Change in PCE chain-type price index



NOTE. The data are for personal consumption expenditures (PCE).
SOURCE. Department of Commerce, Bureau of Economic Analysis.

Several forces likely contributed to last year's impressive economic performance in the face of the sizable adverse oil shock. The growth of real output continued to be undergirded by gains in structural labor productivity. Moreover, fiscal policy remained stimulative last year through the combination of the lagged effect of earlier cuts in personal tax rates, the rise in defense spending, and perhaps also the partial-expensing tax incentives for business investment. Monetary policy was highly accommodative in the early part of the year and remained accommodative, though progressively less so throughout the year, and credit remained readily available at favorable terms. Consumer demand was also boosted by the strong increases in asset values during the past two years.

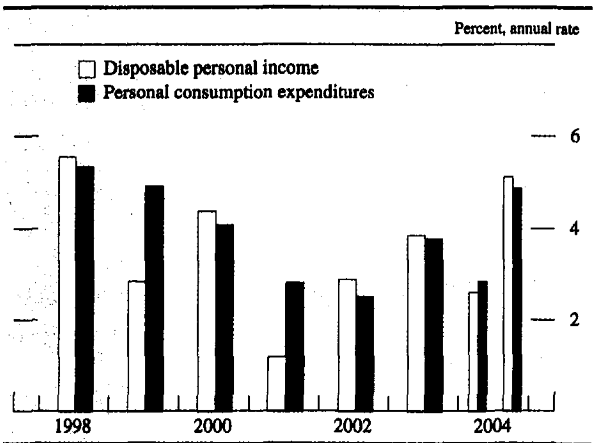
Financial conditions remained stimulative last year even as market participants revised up their expectations for the near-term path of monetary policy. Interest rates on longer-term Treasury securities remained low, risk spreads on corporate bonds narrowed, and commercial banks eased terms and standards on business loans. In this environment, household debt again increased briskly. The borrowing needs of nonfinancial businesses were damped by their strong cash flows. Equity values rose, especially toward the end of the year. At the same time, the exchange value of the dollar declined, on net, over the year as market participants apparently focused on the financing implications of the large and growing U.S. current account deficit.

The Household Sector

Consumer Spending

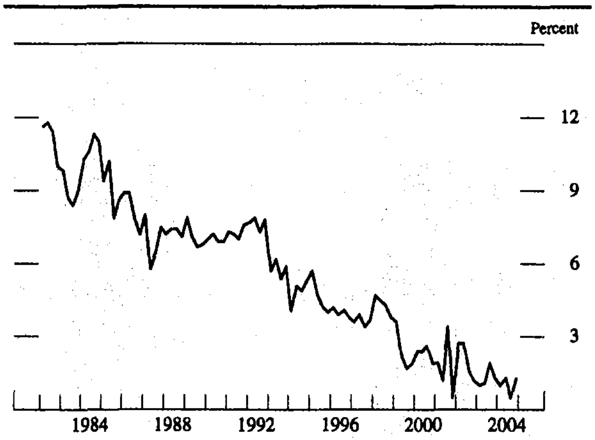
Consumer spending grew substantially last year. Personal consumption expenditures (PCE) advanced nearly 4 percent in real terms, about the same as the increase in 2003. Sales of new motor vehicles remained brisk, on average, at 16¾ million units. Excluding motor vehicles, consumer spending on most categories of durable and nondurable goods rose rapidly, as gains in real expenditures for food

Change in real income and consumption



SOURCE. Department of Commerce, Bureau of Economic Analysis.

Personal saving rate



NOTE. The data are quarterly and extend through 2004:Q4.
SOURCE. Department of Commerce, Bureau of Economic Analysis.

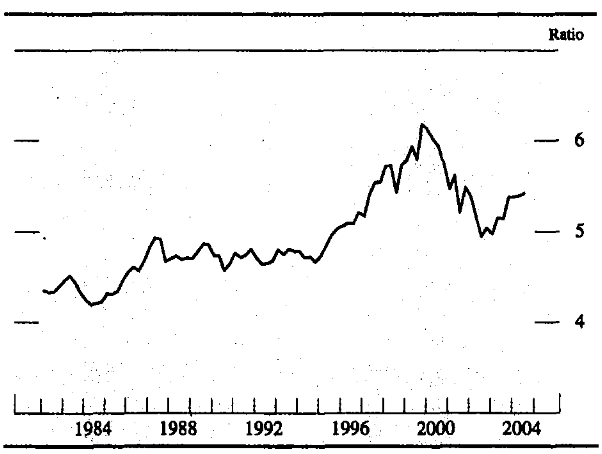
and clothing both exceeded 5 percent; however, spending on computing equipment increased less in 2004 than in preceding years, and consumers responded to the high cost of gasoline and heating fuel by cutting back on real spending for these items. Real outlays for services also increased rapidly last year, and medical services posted especially large gains.

Real disposable personal income (DPI) rose nearly 4 percent last year, but this figure is exaggerated by Microsoft's $32 billion special dividend payment in December (the bulk of which is estimated to have accrued to U.S. households). If this one-time event is excluded from the calculation, real DPI rose only 2¾ percent in 2004, well below the increase posted in 2003. Faster job growth helped to support increases in households' incomes last year in nominal terms, and the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA), which brought lower personal tax rates forward into 2003, led to larger refunds and smaller final payments in the spring of 2004. However, real income gains were held down, as higher oil prices siphoned off household purchasing power.

With the growth of real consumption spending outpacing that of real income through most of last year, the personal saving rate moved lower, from 1½ percent, on average, in 2003 to only ½ percent in the third quarter of last year. (The fourth-quarter surge in income associated with the Microsoft dividend payments pushed the saving rate back up to 1¼ percent, but this increase will likely be reversed early this year as dividend income falls back. Because the company's share price declined in step with the dividend payouts, the dividends had no effect on shareholders' overall financial resources and so probably had little effect on consumption.)

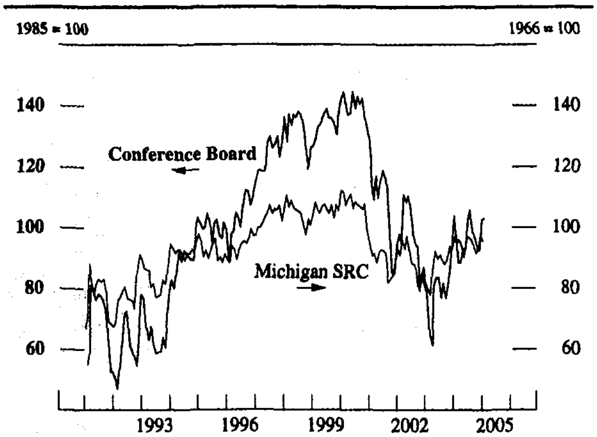
Low interest rates were one factor that helped to support consumption growth—especially for durable goods—despite comparatively slow gains in real income. Higher household wealth was also an important force that propelled consumer spending last year. According to the Federal Reserve's flow of funds accounts, the ratio of household net worth to disposable income rose sharply in 2003, as corporate equity values rebounded and home prices continued to rise. Moreover, although equity values were little changed, on net, through much of 2004 before rising notably in the final quarter, home prices continued to rise throughout the year, and the wealth-to-income ratio moved up further; by the third quarter (the most recent period for which the complete wealth data

Wealth-to-income ratio



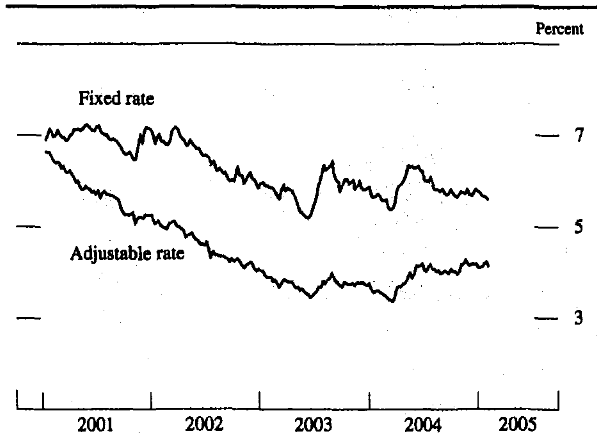
NOTE. The data are quarterly and extend through 2004:Q3. The wealth-to-income ratio is the ratio of household net worth to disposable personal income.
SOURCE. For net worth, Federal Reserve Board, flow of funds data; for income, Department of Commerce, Bureau of Economic Analysis.

Consumer sentiment



NOTE. The data are monthly and extend through January 2005.
SOURCE. The Conference Board and University of Michigan Survey Research Center.

Mortgage rates



NOTE. The data, which are weekly and extend through February 9, 2005, are contract rates on thirty-year mortgages.
SOURCE. Federal Home Loan Mortgage Corporation.

are available), the ratio had reversed nearly half its decline since the stock market peak in 2000. Because wealth feeds through into household spending over a period of several quarters, the wealth increases in both 2003 and 2004 were important in supporting consumer spending last year. The rise in house prices, together with continued low interest rates, also led consumers to extract additional equity from their homes, in particular through home equity loans. Such actions provided many households with a readily available and relatively low-cost source of funds for financing consumption.

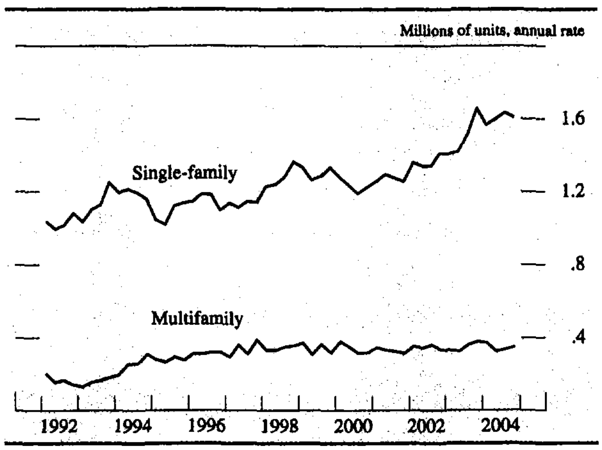
Consumer confidence, which had improved in 2003, remained at generally favorable levels last year, according to surveys by both the Michigan Survey Research Center (SRC) and the Conference Board. Confidence tended to dip at times during the year when energy prices were moving up most rapidly, but it recovered soon after those episodes.

Residential Investment

Residential investment remained robust last year. Real expenditures increased 5¾ percent in 2004—the third straight year of strong gains. Demand for housing was influenced by the same factors that affected household spending more generally, but it was especially supported by nominal mortgage interest rates that have remained near their lowest levels since the late 1960s. Rates on thirty-year fixed-rate mortgages fluctuated between about 5½ percent and 6¼ percent over the past two years; they edged up to the high end of that range during the spring but dropped back to under 6 percent by the end of summer and now stand below 5¾ percent.

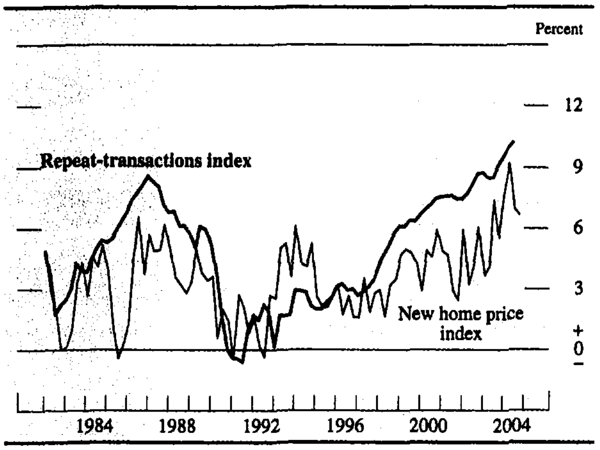
In the single-family sector, housing starts amounted to 1.6 million units last year, a rate faster than the already rapid pace of 1.5 million units started in 2003. In the multifamily sector, starts totaled a solid 350,000 units last year, a figure in line with that of the preceding several years. Sales of both new and existing single-family homes hit new highs last year, and home prices moved up sharply. The repeat-transactions price index for existing homes (limited to purchase transactions only), which is published by the Office of Federal Housing Enterprise Oversight, climbed more than 10 percent over the four quarters ending in the third quarter of last year (the latest quarter for which data are available) and is up a cumulative 65 percent since 1997, when it started to rise notably more rapidly than overall inflation. These price increases have also outstripped by a wide mar-

Private housing starts



NOTE. The data are quarterly and extend through 2004:Q4.
SOURCE. Department of Commerce, Bureau of the Census.

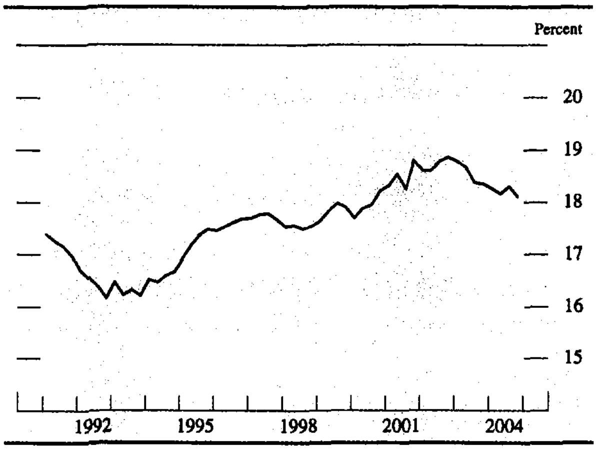
Change in house prices



NOTE. The repeat-transactions index includes purchase transactions only and extends through 2004:Q3. The new home price index extends through 2004:Q4. Change is over four quarters.

SOURCE. For repeat transactions, Office of Federal Housing Enterprise Oversight; for new home prices, Department of Commerce, Bureau of the Census.

Household financial obligations ratio



NOTE. The data are quarterly and extend through 2004:Q4. The final observation, 2004:Q4, is a projection. The financial obligations ratio equals the sum of required payments on mortgage and consumer debt, automobile leases, rent on tenant-occupied property, homeowners' insurance, and property taxes, all divided by disposable personal income.

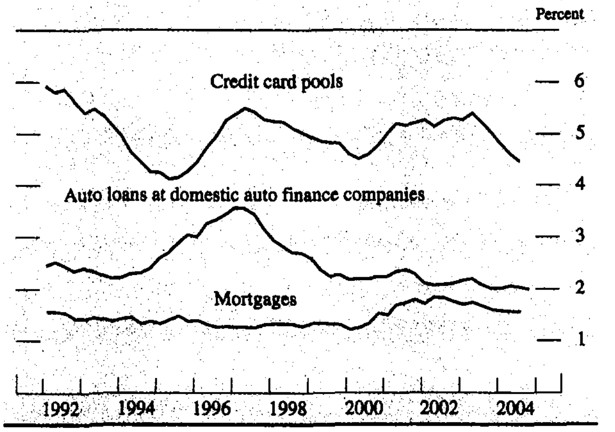
gin the increases in household incomes and rents. Another nationwide price index, the Census Bureau's constant-quality price index for new homes, rose only 6¾ percent last year. Because this index does not adjust for the location of new homes within metropolitan areas and because new homes constitute only a small fraction of the overall housing stock, this index is probably a less reliable indicator of overall home values than is the repeat-transactions index.

Household Finance

Household debt is estimated to have increased about 9¾ percent in 2004, a touch less than in the previous year. Mortgage debt again paced this advance. The brisk expansion of mortgages reflected continued strong activity in housing markets and rising house prices. However, the growth rate of mortgage debt did not quite match that registered in 2003. Refinancing activity fell off sharply last year, as the pool of outstanding mortgages with interest rates above current market rates shrank considerably. Mortgages with adjustable interest rates, including hybrids that feature both fixed and adjustable interest rate components, were increasingly popular in 2004. Consumer credit continued to expand at a moderate pace by historical standards, restrained in part by the substitution of other forms of debt, such as home equity loans. Higher interest rates on some consumer loans and credit cards in the second half of 2004 may have also damped the growth of consumer credit.

Relatively low interest rates and further gains in disposable personal income limited pressures on household balance sheets in 2004. Measures of aggregate household financial obligations and debt service, which capture pre-committed expenditures relative to disposable income, were little changed last year, on balance, though they remained high by historical standards. Nevertheless, measures of household credit quality either held steady or improved during the course of the year. The latest available data indicate that delinquency rates on credit card loans, consumer loans, and residential mortgages at commercial banks declined, while those on auto loans at captive finance companies were about unchanged at a low level.

Delinquency rates on selected types of household loans



NOTE. The data are quarterly. The rates for credit card pools and mortgages extend through 2004:Q3; the rate for auto loans extends through 2004:Q4.

SOURCE. For credit cards, Moody's Investors Service; for auto loans, Big Three automakers; for mortgages, Mortgage Bankers Association.

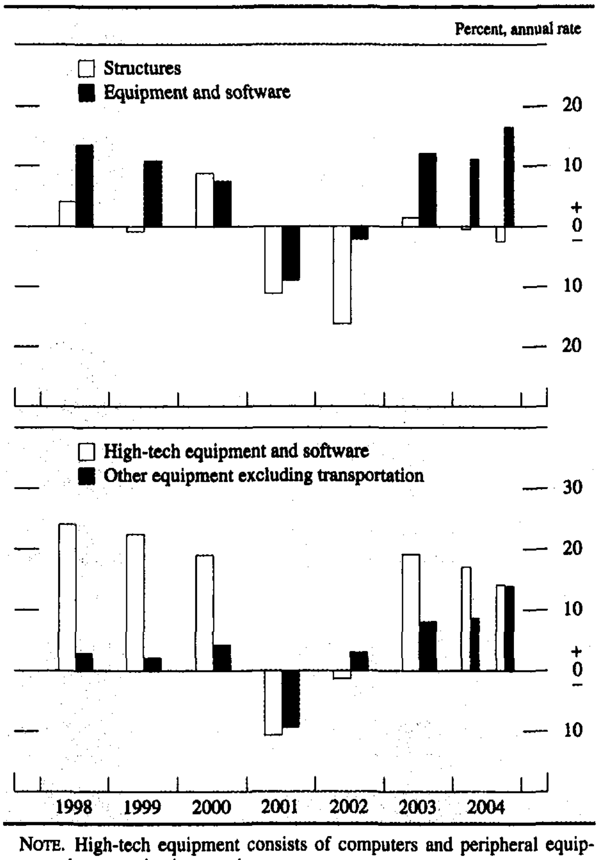
Household bankruptcy filings ran below the elevated levels of 2003, although they stayed generally above the rates posted in earlier years.

The Business Sector

Fixed Investment

Business fixed investment rose robustly for a second consecutive year in 2004. Real spending on equipment and software (E&S) increased 13½ percent, about as much as in 2003, as firms' final sales continued to increase, profits and cash flow rose further, and many businesses reported a need to replace or upgrade existing equipment and software. Although many firms had little need to seek outside financing given their flush cash situation, those that did generally found financial markets to be receptive—interest rates remained low, and other terms and conditions stayed relatively favorable. The partial-expensing tax incentives, which covered new equipment and software installed by the end of 2004, boosted profits and cash flow and may have also stimulated some investment spending.

Change in real business fixed investment



NOTE. High-tech equipment consists of computers and peripheral equipment and communications equipment.

SOURCE. Department of Commerce, Bureau of Economic Analysis.

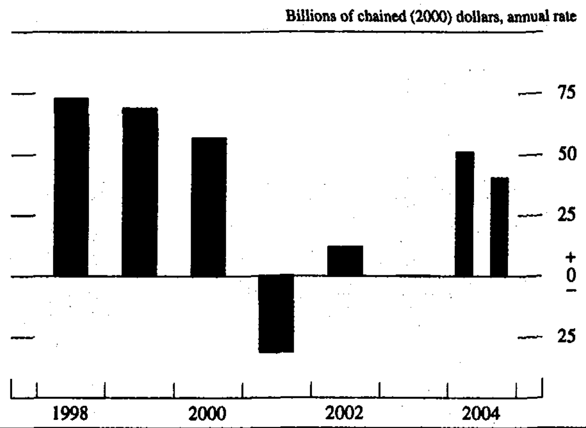
Increases in E&S spending were fairly widespread across categories of capital goods. Spending on high-technology equipment increased 15½ percent last year after having risen 19 percent in 2003; these gains followed two years of declines. Although the pattern of spending was uneven over the four quarters of 2004, for the year as a whole, business outlays for computing equipment rose 25 percent in real terms, while spending on software and communications equipment posted increases of 13 percent and 10 percent respectively. Outside of the high-tech sector, business spending on aircraft moved lower for the third consecutive year, as airlines continued to struggle with a highly competitive market environment and high fuel prices. In contrast, business outlays on motor vehicles rose substantially last year, with the demand for trucks exceptionally strong. Investment in equipment other than high-tech and transportation goods—a category that includes industrial machinery and a wide range of other types of equipment—moved up 11 percent last year, the most in more than ten years.

In contrast to the rebound in equipment spending, real outlays in the nonresidential construction sector were about unchanged for a second year in 2004 and have yet to recover from their sharp downturn during 2001 and 2002. In the office sector, where construction increased rapidly in the late 1990s, spending has remained especially weak; vacancy rates for these properties, although down a touch over the past year, are still quite elevated. Construction of industrial buildings has also remained low as a result of high vacancy rates. In contrast, demand for new retail and wholesale properties has been firmer, reportedly a reflection of the steady increases in consumer spending, and outlays for these types of buildings moved higher last year. In addition, investment in the drilling and mining sector rose last year in response to high prices for natural gas.

Inventory Investment

Businesses added appreciably to inventories last year for the first time since running down their holdings sharply in 2001. As economic activity strengthened during 2002 and 2003, many businesses chose to operate with inventories that were increasingly lean relative to sales. In 2004, when stocks had become quite spare—even after taking into account the ongoing improvements in inventory management that have allowed firms to economize on stockholding—and

Change in real business inventories



SOURCE. Department of Commerce, Bureau of Economic Analysis.

businesses had apparently grown more confident in the durability of the recovery, businesses accumulated $45 billion of inventories (in real terms), according to preliminary data. The step-up in the pace of stock-building contributed about ¼ percentage point to GDP growth last year.

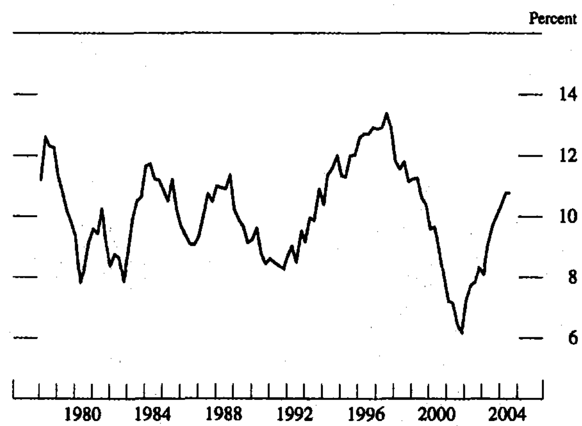
Corporate Profits and Business Finance

Strong growth of corporate profits again allowed many firms to finance capital spending with internal funds last year. As a result, nonfinancial business debt rose at only a moderate pace. Net equity issuance dropped further into negative territory in 2004, and on balance nonfinancial corporations are estimated to have raised no net funds in credit and equity markets. However, short-term business debt, including commercial paper and commercial and industrial (C&I) loans, expanded last year after three years of contraction, and commercial mortgage debt continued to increase rapidly. The credit quality of businesses remained strong.

Corporate profits held up well in 2004 after surging in the previous year. The ratio of before-tax profits of nonfinancial corporations to that sector's gross value added increased for a second consecutive year. In the fourth quarter of 2004, operating earnings per share for S&P 500 firms were nearly 20 percent above their level four quarters earlier. Analysts' earnings forecasts began to moderate somewhat in the second half of 2004 after several months of strong upward revisions.

In equity markets, net issuance of shares by nonfinancial firms turned more negative in 2004. Although initial public offerings rebounded from the sluggish pace of the past two years, ample profits and sizable

Before-tax profits of nonfinancial corporations as a percent of sector GDP



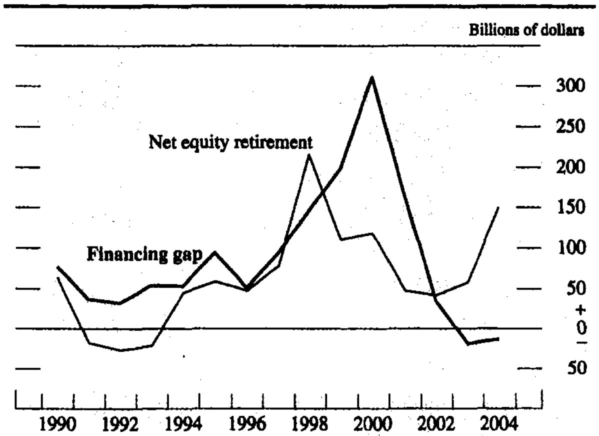
NOTE. The data are quarterly and extend through 2004:Q3. Profits are from domestic operations of nonfinancial corporations, with inventory valuation and capital consumption adjustments.

SOURCE. Department of Commerce, Bureau of Economic Analysis.

cash holdings helped boost share retirements from mergers and repurchases.

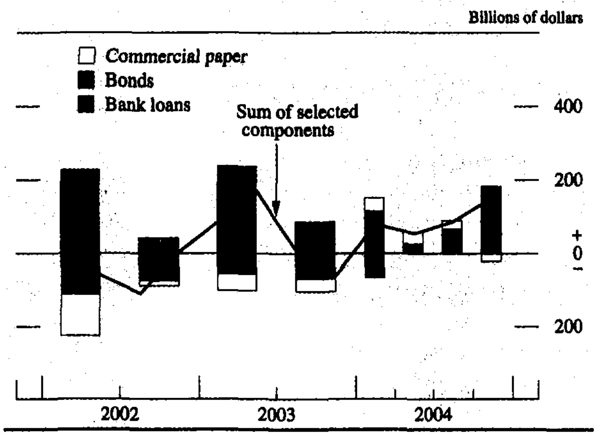
Net corporate bond issuance was sluggish in 2004, as firms evidently relied heavily on their considerable profits to fund investment in fixed capital and inventories. The timing of gross bond issuance was influenced by interest rate movements during the year, as firms took advantage of occasional dips in longer-term yields to issue bonds. Firms reportedly used a large portion of the proceeds to pay down existing debt, although some companies used the funds raised in the bond market to repurchase equity shares or to finance mergers.

Financing gap and net equity retirement at nonfinancial corporations



NOTE. The data are annual; 2004 is based on partially estimated data. The financing gap is the difference between capital expenditures and internally generated funds. Net equity retirement is the difference between equity retired through share repurchases, domestic cash-financed mergers, or foreign takeovers of U.S. firms and equity issued in public or private markets, including funds invested by venture capital partnerships.

Selected components of net business financing

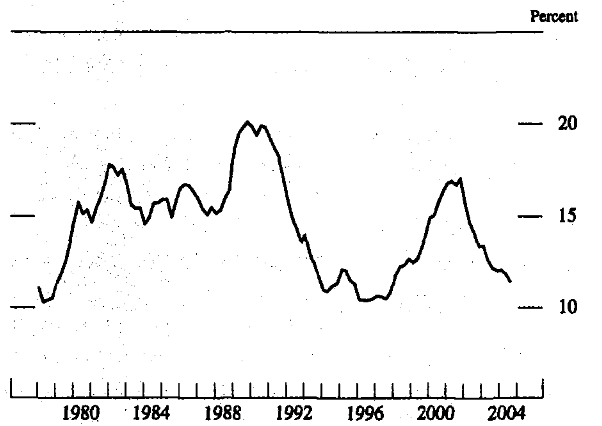


NOTE. Seasonally adjusted annual rate for nonfinancial corporate business. The data for the sum of selected components are quarterly. The data for 2004:Q4 are estimated.
SOURCE. Federal Financial Institutions Examination Council, Consolidated Reports of Condition and Income (Call Report).

Short-term business borrowing revived in 2004 after a prolonged contraction. Commercial paper outstanding turned up in the first half of the year, although it flattened out over the second half. Business loans at banks rebounded over the course of last year. According to results from the Federal Reserve's Senior Loan Officer Opinion Survey on Bank Lending Practices, commercial banks eased terms and standards on business loans during the course of 2004 in response to the improved economic outlook and to increased competition from other banks and nonbank lenders. Survey responses also indicated an increase in demand for C&I loans that reflected firms' need to fund rising accounts receivable, inventories, capital expenditures, and merger activity. Concerns over loan quality seemed to diminish further in 2004, as spreads on leveraged deals in the syndicated loan market edged down from already low levels.

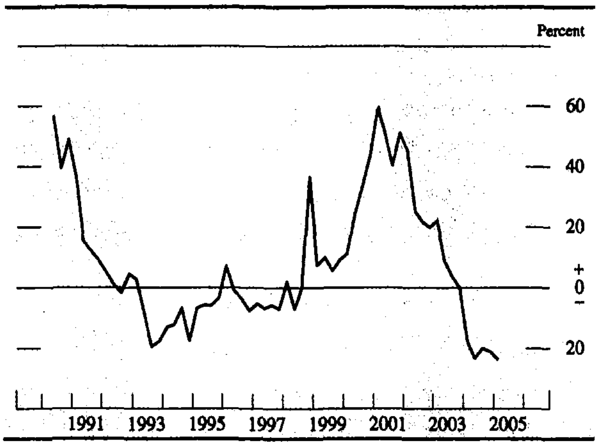
Corporate credit quality remained solid in 2004 amid strong earnings, low interest rates, and a further buildup of already substantial cash positions on firms' balance sheets. The delinquency rate on C&I loans declined further, and the twelve-month trailing default rate on corporate bonds fell to historically low levels before edging up late in the year. Net upgrades of bonds by Moody's Investors Service for both

Net interest payments of nonfinancial corporations as a percent of cash flow



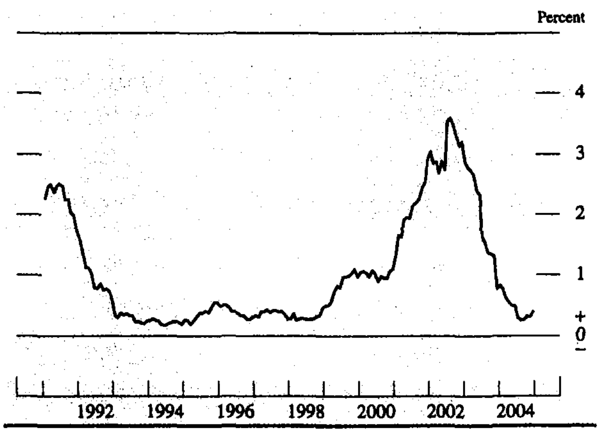
NOTE. The data are quarterly and extend through 2004:Q3.
SOURCE. Department of Commerce, Bureau of Economic Analysis.

Net percentage of domestic banks tightening standards on commercial and industrial loans to large and medium-sized firms



NOTE. The data are based on a survey generally conducted four times per year; the last reading is from the January 2005 survey. Large and medium-sized firms are those with annual sales of $50 million or more. Net percentage is the percentage reporting a tightening less the percentage reporting an easing.
SOURCE. Federal Reserve, Senior Loan Officer Opinion Survey on Bank Lending Practices.

Default rate on outstanding corporate bonds



NOTE. The data are monthly and extend through December 2004. The rate for a given month is the face value of bonds that defaulted in the twelve months ending in that month divided by the face value of all bonds outstanding at the end of the calendar quarter immediately preceding the twelve-month period.
SOURCE. Moody's Investors Service.

investment- and speculative-grade nonfinancial firms increased last year.

The stock of commercial mortgage debt outstanding grew at a rapid pace in 2004. Some firms reportedly continued to find mortgages an attractive source of long-term funding. The expansion of commercial mortgage credit helped propel issuance of commercial-mortgage-backed securities (CMBS) to near-record levels. Delinquency rates on commercial mortgages on the books of banks and insurance companies remained low throughout the year, and those on loans backing mortgage securities fell. Considerable gains in commercial real estate prices increased owners' equity and largely kept pace with the sizable increase in mortgage debt obligations. Yield spreads of CMBS over comparable Treasury securities remained moderate.

The Government Sector

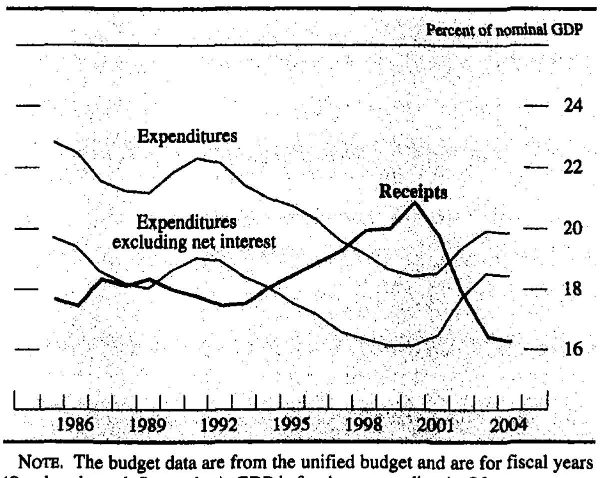
Federal Government

The federal budget position deteriorated slightly further in 2004, as spending increases and further tax reductions offset the effects of stronger economic growth on revenues. The unified budget deficit widened from $378 billion in fiscal 2003 to $412 billion in fiscal 2004. As a share of GDP, the federal unified deficit stood close to 3½ percent in both years. Receipts increased 5½ percent in fiscal 2004 after two years of declines. Corporate receipts surged more than 40 percent, or $58 billion, reflecting the improvement in corporate profits; individual tax receipts—restrained by JGTRRA, which pulled forward reductions of personal tax rates that had been scheduled for the second half of the decade—rose only about 2 percent. Overall federal receipts increased less rapidly than nominal GDP, and the ratio of receipts to GDP edged down to 16¼ percent, the lowest level in more than forty years.

Meanwhile, nominal federal outlays increased about 6 percent in fiscal 2004. Spending for national defense increased especially sharply, but spending also increased notably for Medicare and Medicaid. Debt service costs, which fell sharply from 1997 through 2003 as a result of reduced debt and declining interest rates, edged higher last year. Federal government purchases of goods and services—the part of spending that is counted in GDP—rose about 4 percent in real terms in 2004 after larger increases in the preceding two years. (Government spending on items such as interest payments and transfers is excluded from GDP because these items do not constitute a direct purchase of final production.)

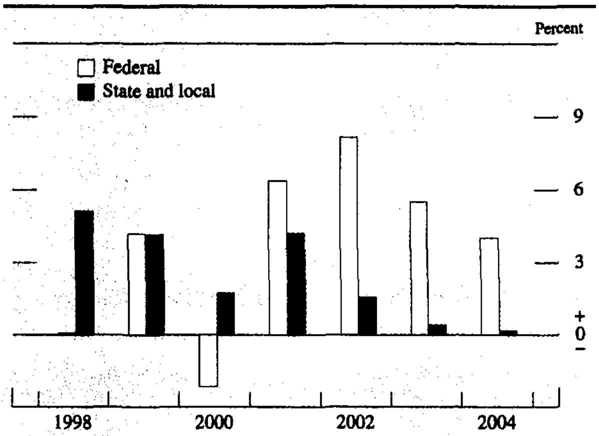
Regarding legislative initiatives, two new tax bills were enacted in the fall of 2004. First, the Working Families Tax Relief Act extended through 2010 a variety of personal tax reductions that had previously been set to expire earlier. Second, the American Jobs Creation Act replaced the exclusion of extraterritorial income (which the World Trade Organization had declared an illegal export subsidy) with numerous other tax reductions for domestic manufacturers and U.S. multinationals. The first bill is expected to have a ten-year budget cost of around $150 billion, while the second bill was scored as being revenue neutral. As for federal spending in fiscal 2005, the regular appropriations bills provided for sizable increases in spending on defense and homeland security and for modest increases in nondefense discretionary expen-

Federal receipts and expenditures



NOTE. The budget data are from the unified budget and are for fiscal years (October through September); GDP is for the year ending in Q3.
SOURCE. Office of Management and Budget.

Change in real government expenditures on consumption and investment



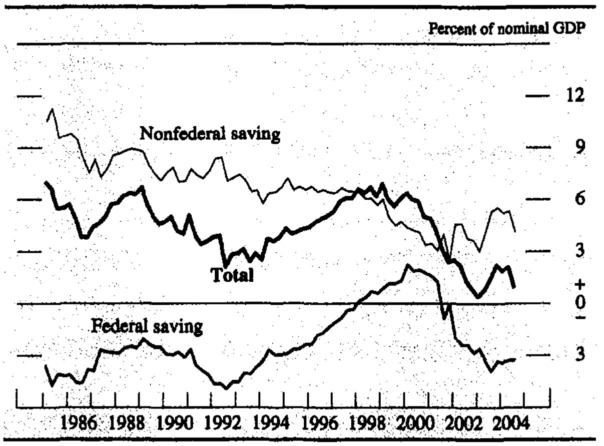
SOURCE. Department of Commerce, Bureau of Economic Analysis.

ditures. In addition, emergency legislation passed in the autumn provided disaster aid for victims of hurricanes and for ranchers and farmers affected by drought conditions.

The recent sizable deficits in the unified budget mean that the federal government, which had been contributing to the pool of national saving from 1997 through 2000, has been drawing on that pool since 2001. Net federal saving—essentially the unified budget balance adjusted to the accounting practices of the national income and product accounts (NIPA)—dropped from positive 2 percent of GDP in 2000 to a level below negative 3 percent of GDP in 2003 and 2004. Personal saving moved lower over this period as well, while business net saving rose with the rebound in corporate profits. In all, net national saving edged up in 2004 but remained near its postwar lows. Because net national saving has fallen increasingly short of net domestic investment over the past several years, the inflow of foreign funds needed to finance that investment has risen. The growing inflow of foreign capital is mirrored in the widening of the nation's current account deficit. Over time, the low national saving rate could eventually slow the rise in living standards either by increasing the burden of servicing U.S. foreign debt or by impinging on domestic capital formation.

The growth rate of Treasury debt moderated slightly last year after increasing substantially in 2003. Nonetheless, federal debt held by the public as a percentage of GDP continued to edge higher over the course of 2004 and currently stands at about 36½ percent. To help finance substantial budget deficits, the Treasury issued a considerable volume of bills as well as two-, three-, five-, and ten-year

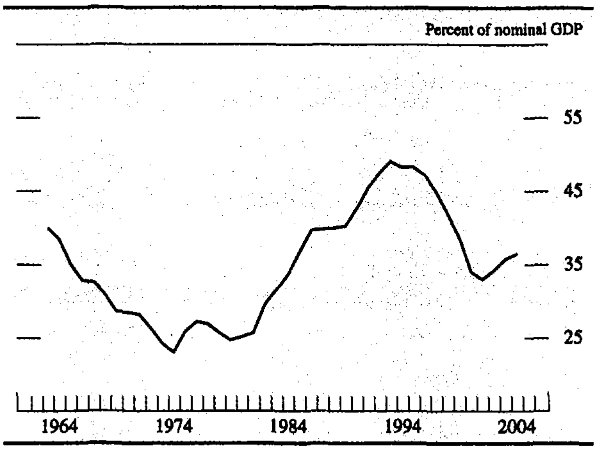
Net saving



NOTE. The data are quarterly and extend through 2004:Q3. Nonfederal saving is the sum of personal and net business saving and the net saving of state and local governments.

SOURCE. Department of Commerce, Bureau of Economic Analysis.

Federal government debt held by the public

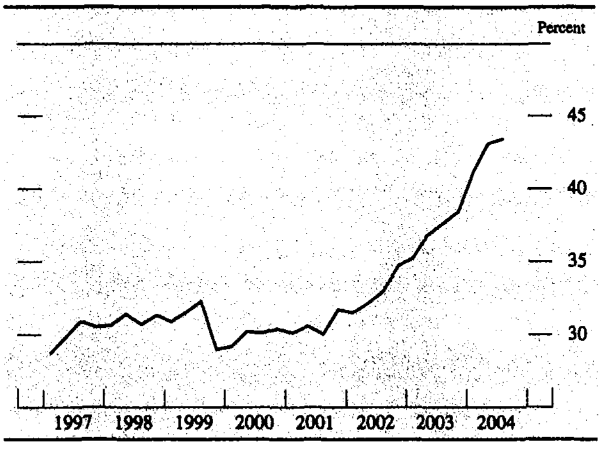


NOTE. Through 2003, the data for debt are year-end figures, and the corresponding value for GDP is for Q4 at an annual rate; the final observation is for 2004:Q3. Excludes securities held as investments of federal government accounts.

nominal notes. In addition, the Treasury expanded its borrowing program in 2004 by adding semiannual auctions of twenty-year inflation-protected bonds and five-year inflation-protected notes.

Various indicators suggested a continued strong appetite for Treasury securities among foreign investors last year. Indirect bidding at Treasury auctions, which includes bidding by the Federal Reserve Bank of New York on behalf of foreign official institutions, remained robust, and Treasury securities held in custody at the Federal Reserve Bank of New York on behalf of such institutions increased just over $200 billion in 2004. Also, data from the Treasury International Capital System showed a substantial increase in holdings of Treasury securities by foreign official and private investors, particularly those in Japan. The proportion of Treasury securities held

Treasury securities held by foreign investors as a share of total outstanding



NOTE. The data are quarterly and extend through 2004:Q3.

by foreign investors is estimated to have risen to a record 43½ percent by the third quarter of 2004.

Treasury debt reached its statutory ceiling late last year. To cope with the constraint, the Treasury temporarily resorted to accounting devices, suspended issuance of state and local government series securities, and postponed a four-week bill auction. In mid-November, Congress raised the debt ceiling from $7.4 trillion to $8.1 trillion, and the Treasury subsequently resumed normal financing operations.

State and Local Governments

Pressures on the budgets of state and local governments have eased as economic activity has strengthened. Tax receipts have been spurred by the increases in household income, consumer spending, and property values. As a result, many states seem to be on track to meet balanced budget requirements in the current fiscal year (which ends June 30 for all but a few states) without using as much borrowing or other extraordinary measures as in recent years. Nevertheless, a number of states still must deal with lingering fiscal problems, particularly depleted reserve funds, the expiration of temporary tax hikes, and rising Medicaid costs. In addition, several states still face serious structural imbalances in their budgets.

Real expenditures by state and local governments as measured in the NIPAs remained about flat for a second year in 2004. Real spending on current operations rose less than 1 percent last year, while real investment spending declined. However, even as they were holding the line on spending increases, states and localities were able to resume net hiring in 2004 after having left employment about unchanged in 2003.

Net issuance of debt by state and local governments edged down from the rapid pace set in 2003, as improved budget positions permitted some contraction in short-term debt. Advance refunding offerings were again strong during the year, as states and municipalities took advantage of low long-term interest rates and moderate credit spreads. Credit quality of tax-exempt borrowers improved in 2004. Rating upgrades of tax-exempt bonds outpaced downgrades, especially later in the year.

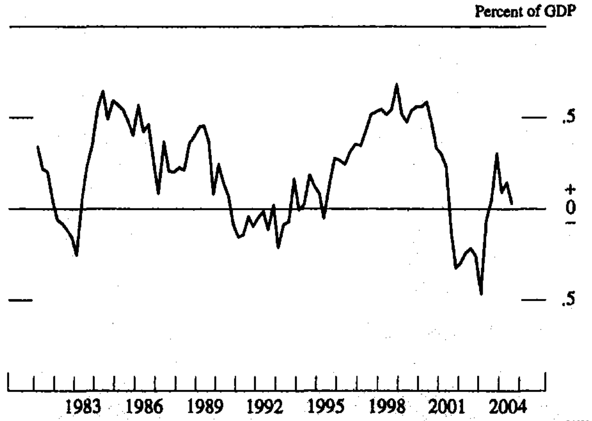
The External Sector

After narrowing in 2003, the U.S. current account deficit widened again last year and was $660 billion (annual rate), or 5.6 percent of GDP, in both the second and third quarters. Much of this widening reflected a considerable increase in the deficit on goods and services trade, as a marked rise in imports more than offset solid increases in exports. The trade deficit expanded from $500 billion during the fourth quarter of 2003 to more than $650 billion, on average, during the second half of 2004.

International Trade

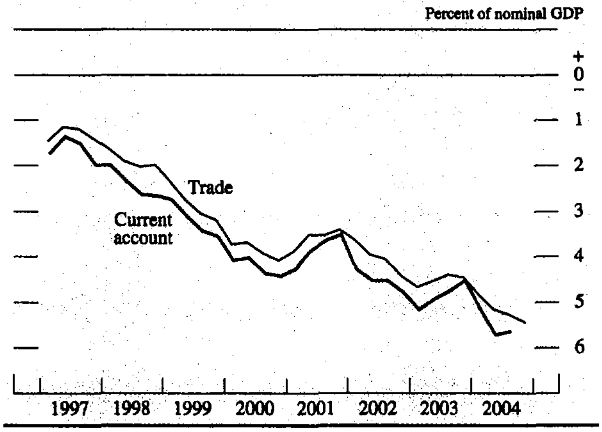
Real exports of goods and services rose an estimated 5½ percent in 2004 despite a deceleration in the fourth quarter. In the first half, exports were supported by the lagged effect of the fall in the dollar's

State and local government net saving



NOTE. The data, which are quarterly, are on a national income and product account basis and extend through 2004:Q3. Net saving excludes social insurance funds.
SOURCE. Department of Commerce, Bureau of Economic Analysis.

U.S. trade and current account balances



NOTE. The data are quarterly. The trade data extend through 2004:Q4, and the current account data extend through 2004:Q3.
SOURCE. Department of Commerce.

value in 2003. Strong expansion of foreign economic activity also helped boost exports in the first half, but that stimulus diminished in the second half of the year when foreign growth slowed. For the year as a whole, exports of industrial supplies and capital goods posted solid growth. Exports to Canada, Mexico, and western Europe rose smartly in 2004, whereas exports to Japan were relatively weak. Real exports of services increased about 3½ percent through 2004 as a whole.

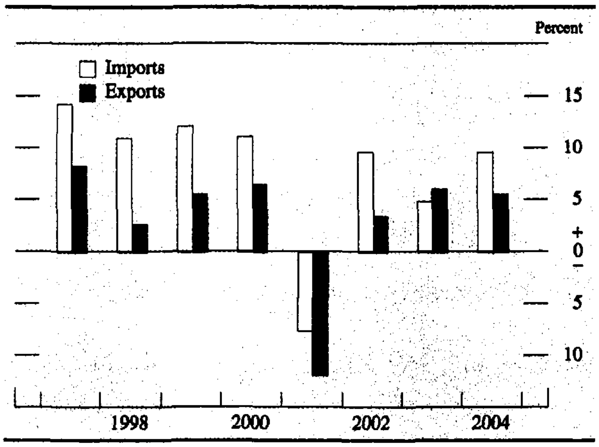
After increasing at an annual rate of almost 6 percent in the first half of 2004, prices of exported goods moved up at just a 2½ percent rate in the second half. This deceleration was due in large part to a reversal of the run-up in the prices of agricultural products that had occurred in late 2003 and early 2004. Better harvests last year returned prices of agricultural products to levels near those that had prevailed before the spike.

Solid growth in income in the United States spurred growth of real imports of 9½ percent in 2004. The increase primarily reflected higher imports of goods that occurred despite a notable rise in their prices. Real oil imports expanded almost 10 percent in 2004. Imports of capital equipment increased throughout the year, but imports of consumer goods suffered a period of weakness through the middle of the year before rebounding in the fourth quarter. Imports of services moved up only 1¾ percent in 2004.

Prices of imported non-oil goods increased at an annual rate of just over 4 percent in the first half of 2004, but the pace slowed to 2 percent in the second half. This step-down largely reflected a deceleration in the prices of industrial supplies, driven by a leveling off of nonfuel commodity prices at the elevated levels reached in March. Declines in the prices of foods offset continued price increases for metals.

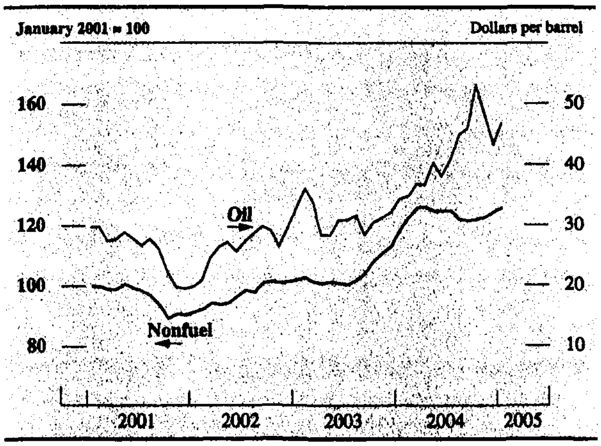
The spot price of West Texas intermediate (WTI) crude oil moved up during most of 2004 and surged temporarily to a record high of $55 per barrel in October. Since then, it has fluctuated somewhat below that peak but still at levels well above $33 per barrel, the price at which it started 2004. Oil prices were driven up by intensified concerns that oil supply would not keep pace with surprisingly strong global demand. Oil consumption in China grew nearly 15 percent in 2004, pushing that economy past Japan as the world's second-largest consumer. As oil prices rose, OPEC increased its oil production, diminishing the cartel's estimated spare capacity to historically low levels. Increased OPEC production damped particularly the rise in prices of heavier, more sulfurous grades of crude oil but had less effect on prices of lighter grades like WTI. Supply disruptions also played a role in the run-up of oil prices. In October, Hurricane Ivan extensively damaged oil and gas production facilities in the Gulf of Mexico, boosting the price of WTI relative to other grades of crude oil. Sabotage of production and distribution facilities in Iraq hindered oil exports from that country, which remain below pre-war levels. In Nigeria, ethnic violence and community protests shut down some production. Russian oil output, however, continued despite the breakup of Yukos, formerly Russia's largest oil company. Late in the year, oil prices declined from their October highs, as production recovered in the Gulf of Mexico and OPEC added new capacity. The price of the far-dated NYMEX oil futures contract (currently for delivery in December 2011) rose

Change in real imports and exports of goods and services



SOURCE. Department of Commerce and Federal Reserve staff estimates.

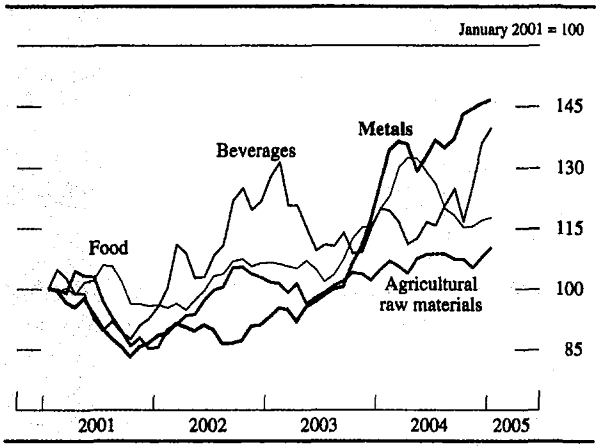
Prices of oil and of nonfuel commodities



NOTE. The data are monthly and extend through January 2005. The oil price is the spot price of West Texas intermediate crude oil. The price of nonfuel commodities is an index of forty-five primary-commodity prices.

SOURCE. For oil, *Wall Street Journal;* for nonfuel commodities, International Monetary Fund.

Prices of major nonfuel commodities



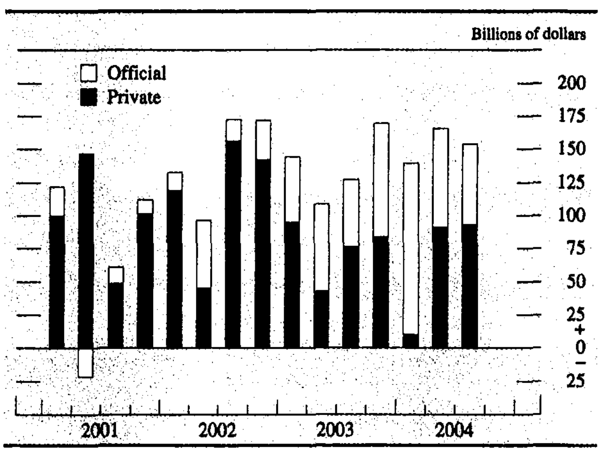
NOTE. The data are monthly and extend through January 2005. The metals category includes aluminum, copper, and iron ore; food includes cereals, vegetable oils and protein meals, seafood, and meat; agricultural raw materials consists of timber, cotton, wool, rubber, and hides; and beverages consists of coffee, cocoa beans, and tea.
SOURCE. International Monetary Fund.

about $10 per barrel during 2004, possibly reflecting expectations of greater oil demand in Asian emerging-market economies. The far-dated futures contract averaged about $38 per barrel in January 2005, while the spot price of WTI averaged about $48 per barrel.

The Financial Account

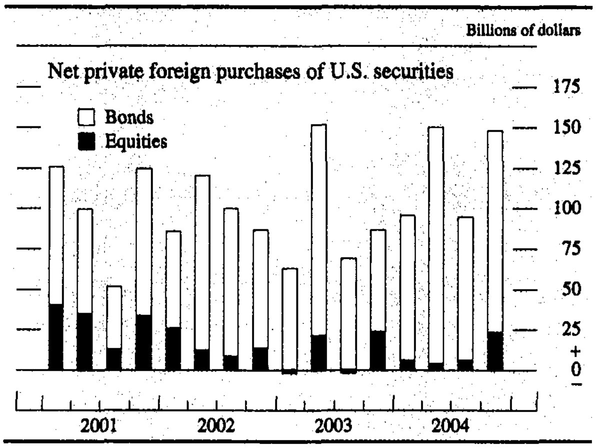
In 2004, the U.S. current account deficit was financed once again largely by foreign purchases of U.S. bonds. Foreign official inflows picked up further last year and were especially strong in the first quarter, reflecting sizable bond purchases by Asian central banks. Private foreign purchases of U.S. bonds

U.S. net financial inflows



SOURCE. Department of Commerce.

U.S. net international securities transactions



SOURCE. Department of Commerce and the Federal Reserve Bank of New York.

rebounded in 2004 from a slight decline in 2003, with especially large purchases coming late in the fourth quarter. In contrast, foreign demand for U.S. equities weakened further in 2004, although this also picked up late in the year. Net purchases of foreign securities by U.S. investors remained strong in 2004, with most of the strength coming in the second half of the year.

U.S. direct investment abroad continued at a strong pace, as reinvested earnings remained sizable. Direct investment into the United States rebounded in the first three quarters of 2004 from its anemic pace in 2003; global mergers and acquisitions revived, and reinvested earnings picked up. Overall, net direct investment outflows continued over the first three quarters of 2004 but at a lower pace than in 2003.

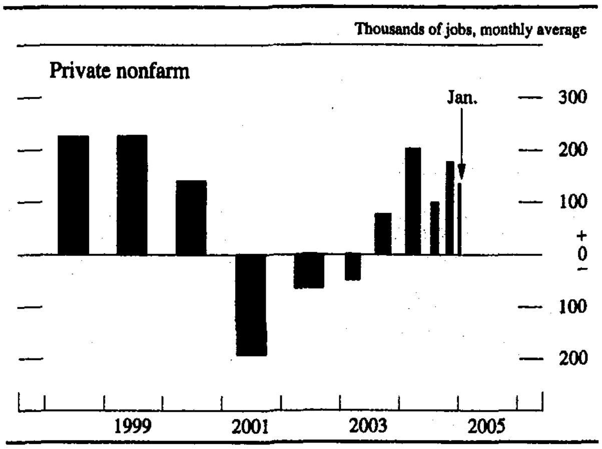
Net inflows of portfolio capital exceeded net outflows of direct investment and represented the financial counterpart to the U.S. current account deficit. These net financial inflows imply a further decline in the U.S. net international investment position, which began 2004 at a reported level of negative $2.4 trillion (22 percent of GDP).

The Labor Market

Employment and Unemployment

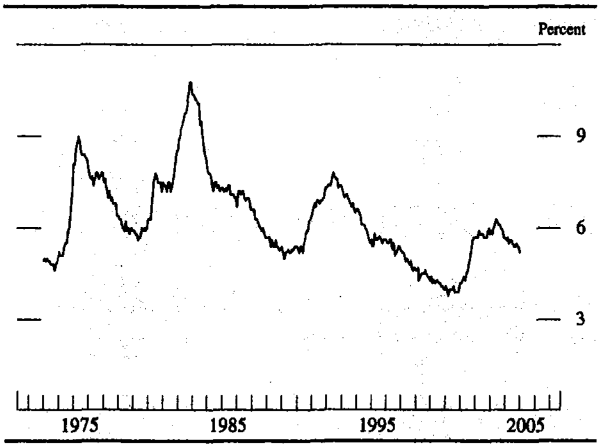
The labor market improved notably in 2004. Private payrolls, which began to post sustained increases in late 2003, rose an average of 170,000 per month last year. Progress was not steady over the course of the year, however. Employment growth stepped up sharply in the spring to a pace of almost 300,000 per month in March, April, and May; net hiring then dropped back to subpar rates of about 100,000 per

Net change in payroll employment



SOURCE. Department of Labor, Bureau of Labor Statistics.

Civilian unemployment rate



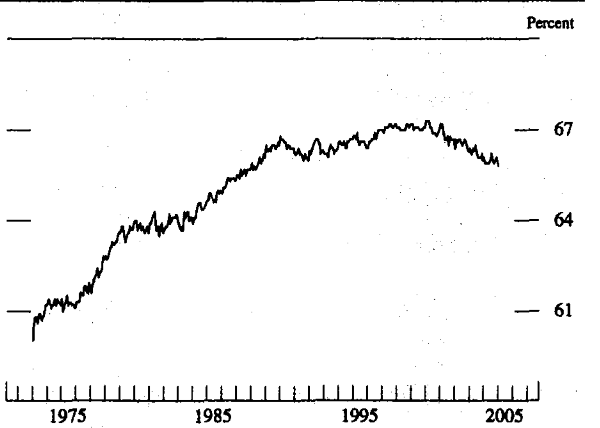
NOTE. The data are monthly and extend through January 2005.
SOURCE. Department of Labor, Bureau of Labor Statistics.

month in June through September. In the four months since then, increases in private payrolls have averaged 165,000 per month.

The improved pace of hiring was widespread, as all major industry groups contributed to faster employment growth relative to that of the latter part of 2003. The largest gains were in professional and business services and health services. The construction sector also posted substantial gains. In the manufacturing sector—where employment had declined almost continuously since early 2000—payrolls increased in the spring when overall employment was rising sharply but were about unchanged, on net, over the second half of the year. Employment gains in retail trade and in food services were also brisk over the first half of the year but tapered off in the second half. Meanwhile, state and local governments added substantially to their payrolls last year, especially for education, but civilian employment in the federal government edged lower.

The unemployment rate fell from near 6 percent in late 2003 to less than 5½ percent by late last year; joblessness fell further in January 2005, to 5¼ percent. The decline in the unemployment rate over the past year reflected both the pickup in hiring and a labor force participation rate that remained surprisingly low. From 2001 through 2003, the participation rate declined by more than would have been predicted on the basis of past relationships with indicators of labor demand, and in 2004, when the pace of hiring increased, the participation rate leveled off but failed to rise. These considerations suggest that there may be a persistent component to the recent softness in participation. However, participation had been quite strong through 2000, when the labor market was extremely tight, and the fact that participation

Labor force participation rate



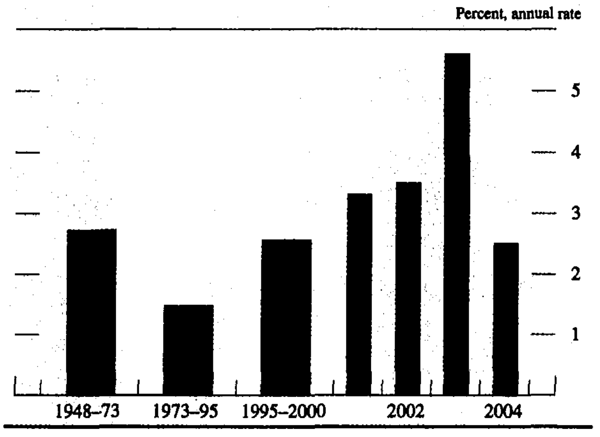
NOTE. The data are monthly and extend through January 2005.
SOURCE. Department of Labor, Bureau of Labor Statistics.

turned down at the same time that labor demand weakened suggests that at least some of the recent low participation is cyclical. To the extent that some of this low participation proves to be transitory, the resumption of more-rapid labor force growth will limit the speed at which employment gains further push down the unemployment rate.

Productivity and Labor Costs

Labor productivity rose solidly again last year. Output per hour in the nonfarm business sector increased an estimated 2½ percent over the year. This increase was somewhat below the outsized 4 percent average pace of increase from 2001 through 2003. Those earlier huge productivity gains were not associated with especially large accumulations of new capital

Change in output per hour

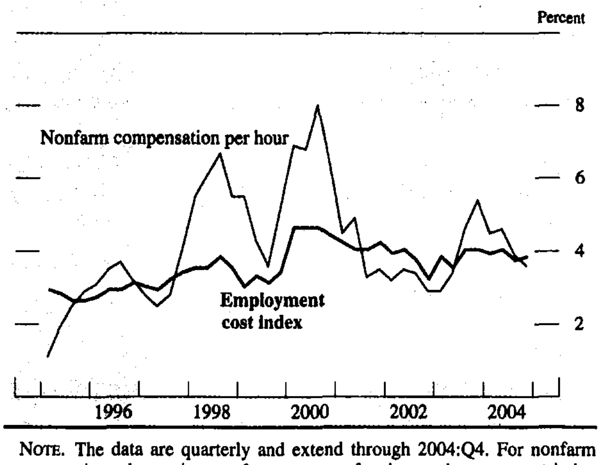


NOTE. Nonfarm business sector.
SOURCE. Department of Labor, Bureau of Labor Statistics.

equipment, as had been the case during the late 1990s; instead, to a large degree, the gains seem to have been related to more effective use of capital equipment that had been acquired earlier and to one-time organizational innovations induced by firms' earlier reluctance to commit to increased hiring. Still, last year's 2½ percent increase in productivity was impressive by long-run standards: It was in line with the pace of the late 1990s and well above rates that had prevailed during the preceding two decades.

Increases in hourly labor compensation remained moderate last year. As measured by the employment cost index (ECI), which is based on a quarterly survey from the Bureau of Labor Statistics, hourly compensation in private nonfarm businesses increased 3¾ percent in 2004, a bit less than in 2003.

Measures of change in hourly compensation



NOTE. The data are quarterly and extend through 2004:Q4. For nonfarm compensation, change is over four quarters; for the employment cost index (ECI), change is over the twelve months ending in the last month of each quarter. Nonfarm compensation is for the nonfarm business sector; the ECI is for private industry excluding farm and household workers.
SOURCE. Department of Labor, Bureau of Labor Statistics.

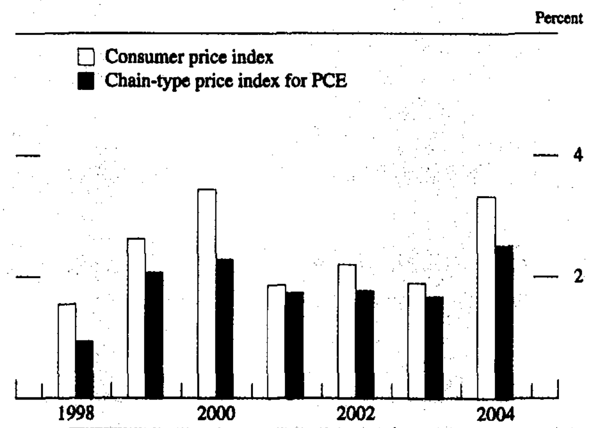
An alternative measure is compensation per hour in the nonfarm business sector as derived from compensation data in the NIPAs. This measure of hourly compensation rose 3½ percent last year, an increase similar to that in the ECI but substantially less than the 5½ percent rise in 2003.

As has been the case for several years, the cost of employee benefits rose considerably more than did wages and salaries last year. The benefits component of the ECI increased nearly 7 percent, while the wages and salaries component posted a much more moderate 3 percent increase. The rise in hourly wages and salaries was about the same as increases in the preceding two years; although probably boosted by last year's higher rate of price inflation, wages were likely held down by the continued, though diminishing, labor market slack and also by employers' attempts to offset continued large increases in benefits costs. Health insurance costs continued to rise rapidly. As measured by the ECI, employers' costs of health insurance, which account for about 6 percent of overall compensation costs, rose 7 percent last year after having increased more than 10 percent per year in 2002 and 2003.

Prices

Overall consumer prices rose notably more in 2004 than they did in 2003, and the sharp increase in energy prices accounted for much of the step-up. The chain-type price index for personal consumption expenditures (PCE) rose 2½ percent last year, compared with an increase of 1¾ percent in 2003. The increase in PCE prices excluding food and energy was considerably smaller—only 1½ percent, up a little more than ¼ percentage point from the increase in 2003. Inflation as measured by the market-based component of core PCE prices—which excludes a collection of erratic prices that are unobservable from market transactions and which the Bureau of Economic Analysis began to publish early last year—was in line with overall core PCE inflation last year. The core consumer price index (CPI) rose about 2 percent last year after having increased 1¼ percent in 2003. (The CPI differs from PCE prices in a number of respects, but one factor that boosted CPI inflation relative to PCE inflation last year was a difference in the way the two indexes measure the prices of medical services, especially physicians' services, which rose much more rapidly in the CPI than in the PCE index.) The rise in core consumer prices was largest in the early months of 2004: Core PCE prices increased at an annual rate of nearly

Change in consumer prices



SOURCE. For consumer price index, Department of Labor, Bureau of Labor Statistics; for chain-type measure, Department of Commerce, Bureau of Economic Analysis.

Alternative measures of price change

Percent

Price measure	2002	2003	2004
Chain-type			
Gross domestic product	1.6	1.7	2.4
Gross domestic purchases	1.8	1.8	2.9
Personal consumption expenditures	1.8	1.7	2.5
Excluding food and energy	1.5	1.2	1.6
Market-based PCE excluding food and energy	1.4	1.0	1.6
Fixed-weight			
Consumer price index	2.2	1.9	3.4
Excluding food and energy	2.0	1.2	2.1

NOTE. Changes are based on quarterly averages of seasonally adjusted data.

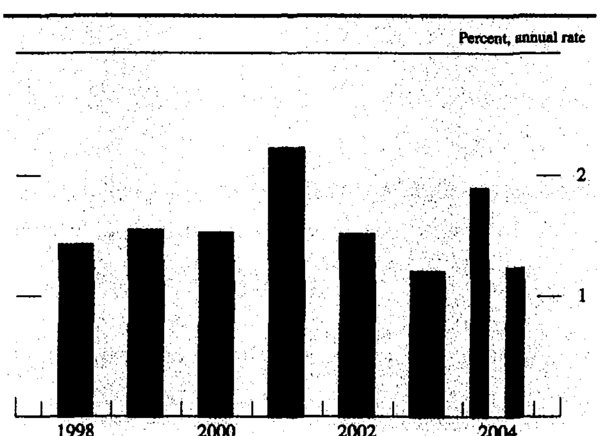
SOURCE. For chain-type measures, Department of Commerce, Bureau of Economic Analysis; for fixed-weight measures, Department of Labor, Bureau of Labor Statistics.

2 percent over the first half of the year and then decelerated to a 1¼ percent rate of increase in the second half.

The price index for GDP was less affected by last year's rise in energy prices than was the PCE measure; much of the energy price increase was attributable to the higher prices of imported oil, which are excluded from GDP because they are not part of domestic production. GDP prices increased 2½ percent last year, ¾ percentage point faster than in 2003. In addition to the rise in PCE prices (excluding the influence of imported oil), GDP prices were affected by a sizable increase in construction prices for residential and nonresidential structures.

The jump in consumer energy prices in 2004 was driven by the run-up in crude oil prices. The prices of both gasoline and fuel oil increased approximately 30 percent over the year, and higher oil costs accounted for the bulk of the increase. Prices of natural gas, which can often substitute for fuel oil in the industrial sector, rose notably as well last year despite the restraining influence of ample inventories. Electricity prices, which tend to reflect fuel costs with a lag, also moved higher through most of the year but dropped back some near year-end.

Change in PCE prices excluding food and energy

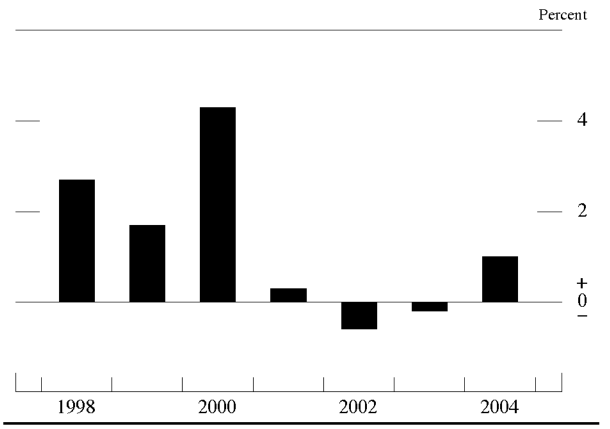


SOURCE. Department of Labor, Bureau of Labor Statistics.

Consumer food prices rose around 3 percent for a second consecutive year in 2004. Exports of beef dropped sharply last year when most of the largest importing countries placed restrictions on U.S. beef after a case of mad cow disease was discovered. Nevertheless, domestic demand was sufficiently strong to support consumer meat prices last year. Fruit and vegetable prices trended sideways through most of the year but then rose sharply in the fall because of crop damage associated with the series of hurricanes that hit the Southeast in August and September. In addition, prices for food away from home, which are driven more by labor costs than by raw food prices, increased more rapidly last year than in 2003.

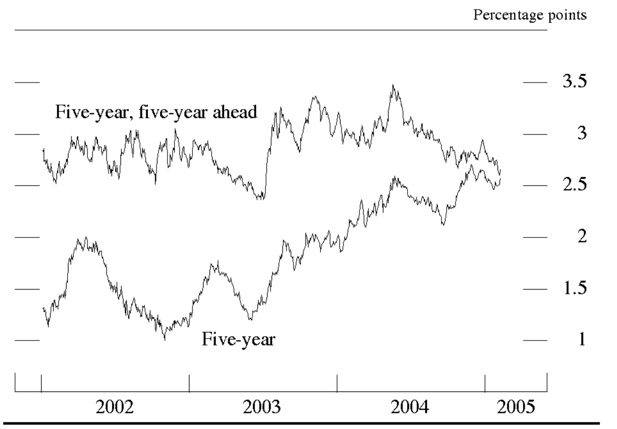
Core consumer prices were influenced by a variety of forces last year. Price increases were likely restrained by continuing slack in labor markets and in some product markets, but businesses faced considerable pressure from several sources of increased costs. First, the indirect effects of the large jump in energy prices fed through to businesses throughout the economy and were especially important for firms in energy-intensive industries, such as those that produce plastics and fertilizers. Second, prices were up sharply for a number of other industrial commodities, including lumber and a variety of metals. These price increases reflected strengthening economic activity abroad as well as in the United States. Although these non-oil commodities represent a small part of businesses' overall costs, some businesses likely felt the pinch of sustained price increases in these areas.

Change in unit labor costs



NOTE. Nonfarm business sector.
SOURCE. Department of Labor, Bureau of Labor Statistics.

TIPS-based inflation compensation



NOTE. The data are daily and extend through February 9, 2005. Based on a comparison of the yield curve for Treasury Inflation-Protected Securities (TIPS) to the nominal off-the-run Treasury yield curve.

Third, the declining exchange value of the dollar boosted import prices, including those of many inputs to production. Finally, the deceleration in labor productivity boosted unit labor costs after two years of declines; nevertheless, last year's 1 percent rise in unit labor costs was quite modest.

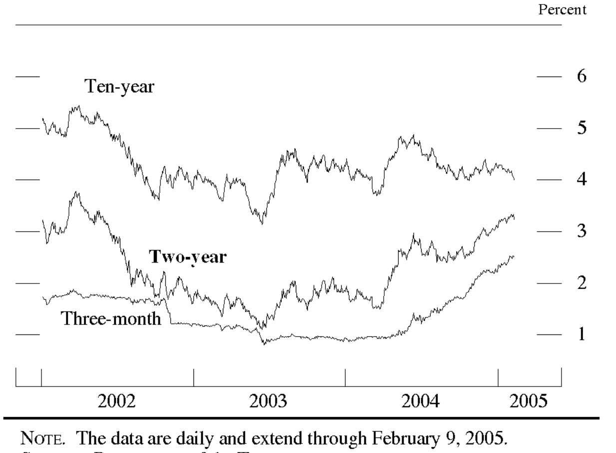
Taken together, these influences left their clearest mark on the prices of goods rather than services. Core goods prices were about unchanged, on average, last year, but this period of stability followed a period of unusually large declines in 2003. In particular, the prices of new motor vehicles leveled off after falling notably in 2003, and the prices of used vehicles reversed some of their sharp 2003 declines. Prices of non-energy PCE services rose about 2 percent in 2004—a smaller increase than in 2003.

Last year's rise in inflation showed through to short-term measures of expected inflation, but longer-term measures remained stable. According to the Michigan SRC, households' median expectations for inflation over the next year moved up considerably in the spring as inflation was rising, but then they eased back and ended the year near 3 percent—up from around 2½ percent in late 2003. In contrast, the median expectation for inflation over the next five to ten years held about steady near 2¾ percent throughout this period. Inflation compensation as measured by spreads between yields on nominal Treasury securities and inflation-indexed securities—another indicator of expected inflation, albeit one that is also influenced by perceptions of inflation risk and perhaps also by the development of the market for inflation-indexed debt—showed a similar pattern. Inflation compensation over the next five years moved up about ½ percentage point during 2004, to 2½ percent, while compensation at the five- to ten-year horizon edged lower, on net, over the year.

U.S. Financial Markets

Domestic financial conditions were supportive of economic growth in 2004. Interest rates on longer-term Treasury securities remained low, corporate risk spreads fell, and stock prices, on balance, registered gains. These developments occurred even as market participants revised up their expectations for the path of the federal funds rate. At the beginning of 2004, futures market quotes implied that investors expected a 1¾ percent target for the federal funds rate at year-end, 50 basis points below the target actually established at the FOMC meeting in December 2004.

Interest rates on selected Treasury securities



NOTE. The data are daily and extend through February 9, 2005.
SOURCE. Department of the Treasury.

Consistent with the revision in policy expectations, yields on two-year Treasury notes increased about 1¼ percentage points in 2004. Yields on longer-dated Treasury securities, however, ended the year essentially unchanged. Despite the run-up in oil prices, equity prices registered solid gains in 2004 after rising sharply the year before. Risk spreads on investment-grade corporate debt declined a touch, and those on speculative-grade debt fell more noticeably. Moreover, banks appreciably eased terms and standards for lending to businesses.

Interest Rates

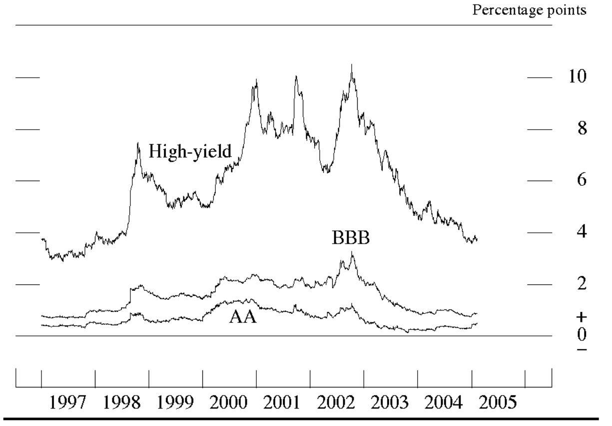
Most market interest rates rose, on balance, over the first half of 2004, particularly at shorter maturities. The FOMC's decision at its January meeting to shift from a statement that monetary policy could remain accommodative for "a considerable period" to an indication that it could be "patient" in removing policy accommodation prompted a rise in market interest rates. In early February and March, yields fell substantially in response to employment reports that indicated tepid job growth. Prices of federal funds and Eurodollar futures contracts implied that investors placed only small odds on an increase in the target funds rate before late 2004 and that they envisioned only moderate monetary policy tightening thereafter. Longer-term interest rates and the expected path for the federal funds rate were considerably marked up later in the spring in response to data suggesting a pickup in aggregate demand and hiring, readings on core inflation that came in above expectations, and rising oil prices. In the statement released after its May meeting, the Committee indicated that policy accommodation was likely to be removed at a "measured" pace. At its June meeting, the Committee raised the target for the federal funds rate from 1 percent to 1¼ percent, but it continued to assess the risks to sustainable growth and to price stability as balanced and reiterated the "measured pace" language. Interest rates across the term structure declined somewhat immediately after the announcement, reportedly because some market participants had expected the FOMC to mention upside risks to growth or inflation in its statement.

Chairman Greenspan's congressional testimony in July on monetary policy, which suggested that recent softness in consumer spending would likely prove short lived, sparked a jump in yields on Treasury securities. However, interest rates subsequently moved lower, on balance, as incoming data pointed to weaker spending and employment than investors had expected as well as to more-subdued core inflation. Apart from the August employment report, which seemed to hint that the economy was emerging from its "soft patch," incoming economic news remained somewhat lackluster through the end of the third quarter. However, investors reportedly viewed FOMC statements and comments by FOMC officials as more sanguine on near-term prospects for the economy than they had expected. In particular, the release of the minutes from the August FOMC meeting, which referenced the probable need for "significant cumulative tightening," prompted investors to mark up their expectations for the near-term path of monetary policy.

Short-term Treasury yields rose a bit further over the fall in association with actual and expected policy tightening, but long-term Treasury yields were little changed on net. Investors' expectations for the path of monetary policy firmed a bit more in the fourth quarter in response to higher-than-anticipated inflation and remarks from Federal Reserve officials that were reportedly interpreted as suggesting that an imminent pause in the tightening cycle was unlikely.

As the economic expansion gathered momentum and measures of corporate credit quality improved, investors' perception of risk seemed to diminish, and their willingness to bear risk apparently increased. Risk spreads on investment-grade corporate debt over comparable Treasuries ended the year slightly below their levels at the end of 2003. Spreads of speculative-grade yields declined further after narrowing sharply during 2003.

Spreads of corporate bond yields over comparable off-the-run Treasury yields



NOTE. The data are daily and extend through February 9, 2005. The high-yield index is compared with the five-year Treasury yield, and the BBB and AA indexes are compared with the ten-year Treasury yield.

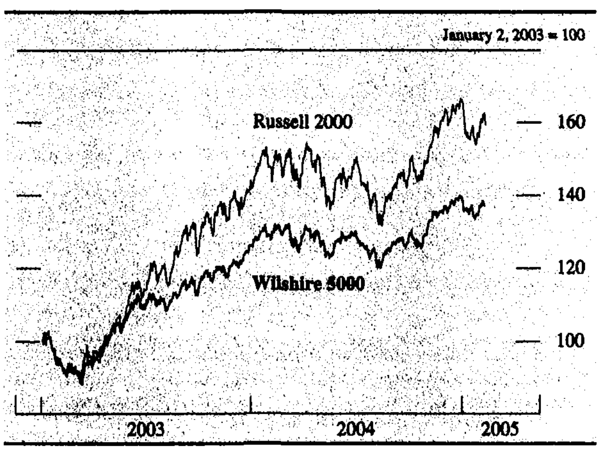
SOURCE. Merrill Lynch AA and BBB indexes and Merrill Lynch Master II high-yield index.

In early 2005, market participants boosted their expectations for the path of the federal funds rate, partly in response to the publication of the minutes of the December FOMC meeting, which investors reportedly interpreted as pointing to greater concerns about inflation than had been expected. Short- and intermediate-term Treasury yields rose along with expectations for the path of monetary policy, but longer-term yields edged lower. Yields on investment- and speculative-grade corporate bonds largely moved with those on comparable Treasury securities, and hence risk spreads remained at low levels.

Equity Markets

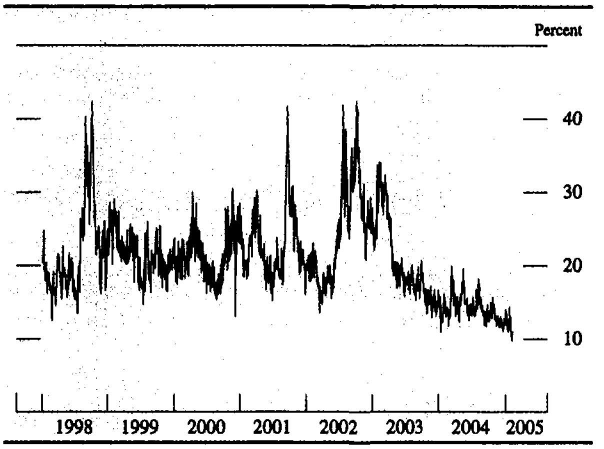
After surging as much as 30 percent in 2003, broad stock market indexes climbed modestly over the first half of 2004. The boost to equity prices from robust earnings reports and analysts' upward revisions for future profits during this period was offset in part by rising interest rates in the second quarter, worries about geopolitical developments, and sharply higher oil prices. Stock prices dipped early in the second half in response to softer economic data, further concerns about energy prices, and guidance from corporations that pointed to a less optimistic trajectory for earnings than investors had reportedly been expecting. However, as oil prices pulled back toward the end of 2004 and news on the economy improved, stock prices rebounded to post solid gains for the year. The increases were led by stocks with comparatively small market capitalizations; the Russell 2000 index climbed 17 percent in 2004 to a record high. The S&P 500 and the technology-laden Nasdaq advanced about 9 percent and 8½ percent respectively. To date in 2005, equity prices have edged lower, on balance, as investors have responded to a rebound in oil prices, lackluster earnings reports, cautious guidance for future profits, and indications of continued monetary policy tightening.

Stock price indexes



NOTE. The data are daily and extend through February 9, 2005.

Implied S&P 500 volatility



NOTE. The data are daily and extend through February 9, 2005. The series shown is the implied thirty-day volatility of the S&P 500 stock price index as calculated from a weighted average of options prices.
SOURCE. Chicago Board Options Exchange.

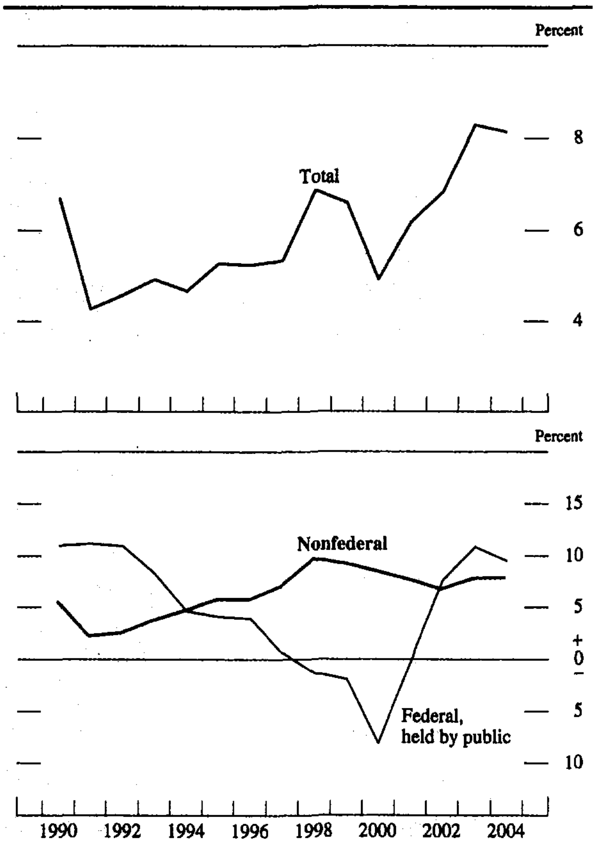
Expected volatility implied by options prices for both the Nasdaq 100 and the S&P 500 declined further in 2004 from already low levels. The difference between the earnings–price ratio and the real ten-year Treasury yield—a crude measure of the premium investors require for holding equity shares—changed little, on balance, remaining close to its average value over the past two decades but above its level during the late 1990s.

Debt, Bank Credit, and M2

The aggregate debt of domestic nonfinancial sectors is estimated to have increased about 7¾ percent in 2004, somewhat faster than nominal income but a bit slower than the pace set the year before. Household and federal debt expanded rapidly. Borrowing by nonfinancial businesses was moderate, although it picked up in the fourth quarter.

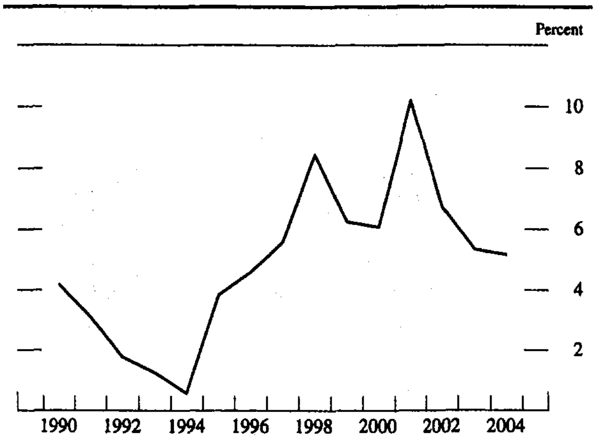
Commercial bank credit rose about 9 percent in 2004, a larger advance than in the previous year. Expansion of mortgage and home equity loans on banks' books remained strong, as activity in the housing market stayed robust while mortgage originations shifted somewhat toward adjustable-rate products. After several years of runoffs, business loans began to grow in the second quarter of the year. According to survey evidence, commercial banks eased terms and standards on business loans as the

Growth of domestic nonfinancial debt



NOTE. For 2004, change is from 2003:Q4 to 2004:Q3 at an annual rate. For earlier years, the data are annual and are computed by dividing the annual flow for a given year by the level at the end of the preceding year. The total consists of nonfederal debt and federal debt held by the public. Nonfederal debt consists of the outstanding credit market debt of state and local governments, households, nonprofit organizations, and nonfinancial businesses. Federal debt held by the public excludes securities held as investments of federal government accounts.

M2 growth rate



NOTE. The data are annual and extend through 2004. M2 consists of currency, traveler's checks, demand deposits, other checkable deposits, savings deposits (including money market deposit accounts), small-denomination time deposits, and balances in retail money market funds.

economic outlook improved and competition from other banks and nonbank lenders intensified. Also, banks reported a pickup in demand for business loans that was said to be driven by customers' needs to fund rising accounts receivable, inventories, capital expenditures, and mergers. After adjusting for certain reclassifications of securities as loans, the growth of consumer loans on banks' books remained sluggish. Despite reports of increased competition among banks and nonbank intermediaries, bank profits were again strong in 2004. Banks experienced further improvements in asset quality and, as a result, reduced their provisions for loan losses.

M2 grew at a pace roughly in line with that of nominal GDP during the first half of 2004. A resurgence of mortgage refinancing spurred by the first-quarter decline in mortgage rates likely boosted liquid deposit growth, as proceeds from refinancing were temporarily held in deposit accounts pending disbursement to the holders of mortgage-backed securities. M2 growth slowed in the second half of the year in response to a drop in mortgage refinancing activity and the increased opportunity cost of holding M2 assets, as returns available on market instruments rose more than those on M2 components. For example, yields on retail money market mutual funds moved up more slowly than did short-term market interest rates, and assets of money funds accordingly continued to shrink. Small time deposits, which had contracted over the previous three years, resumed expansion in the second half of the year, as their yields began to rise in association with the increase in other market rates. Currency grew at its slowest rate since 2000, apparently reflecting sluggish demand by both domestic and foreign holders. On balance, M2 growth from the fourth quarter of 2003 to the fourth quarter of 2004 was about 5¼ percent. The velocity of M2 rose 1 percent, on net, roughly in line with the historical relationships among money, income, and opportunity cost.

International Developments

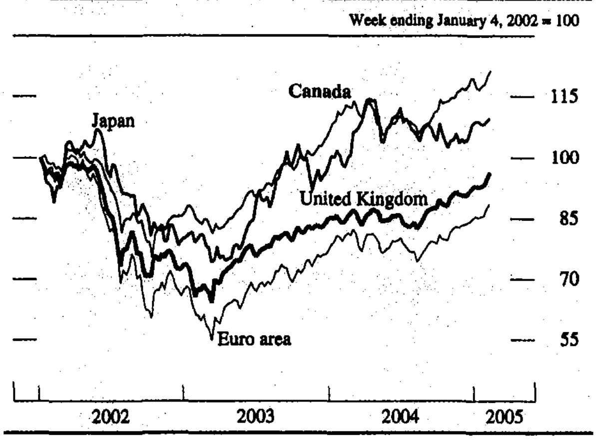
Foreign economic activity expanded in 2004 at a faster pace than in the preceding three years. The pickup in growth was widespread—global manufacturing and trade rebounded across industrial and emerging economies, in part because of strong demand from the United States and China. In the second half of the year, trade and foreign GDP growth slowed, partly as a result of higher oil prices and the appreciation of some foreign currencies against the dollar. The run-up in oil prices and other commodity prices contributed to higher, though still moderate, inflation across industrial and emerging economies.

Monetary policy in many foreign economies tightened over the course of 2004. Citing high rates of capacity utilization and mounting inflationary pressures, the Bank of England raised its target interest rate 100 basis points but has been on hold since August amid signs that housing prices and consumer spending are cooling. After cutting official interest rates earlier in the year, the Bank of Canada raised rates in the fall in response to diminishing slack in the economy. The Bank of Mexico tightened policy throughout the year to resist rising inflation, and Chinese authorities made monetary policy more restrictive to rein in soaring investment demand. In the euro area and Japan, central banks kept policy interest rates unchanged in 2004.

Foreign equity price indexes recorded moderate net gains last year after larger increases in 2003. Equity markets started the year strong, but prices declined in the spring as interest rates rose. The run-up in oil prices between July and October appeared to weigh on foreign equity prices, but the subsequent decline in oil prices helped support a rise in equity prices late in the year. Foreign long-term interest rates declined, on net, during 2004. Rates rose in the second quarter as new data (including reports from the United States) that showed faster growth and higher inflation led market participants to expect more-aggressive monetary tightening. However, foreign long-term interest rates slipped after midyear, when foreign growth slowed and foreign currencies appreciated against the dollar. Over the first half of the year, spreads on internationally issued sovereign debt of emerging-market economies over U.S. Treasuries moved up somewhat from low levels, but spreads more than reversed those increases in the second half.

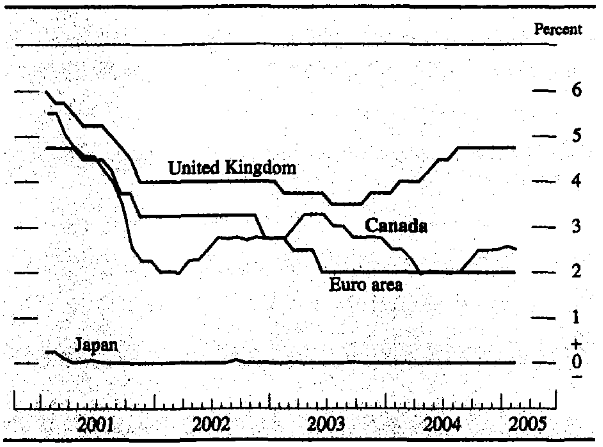
The path of the exchange rate was uneven over the course of 2004. The dollar rose slightly in the first half of the year on perceptions that monetary policy would tighten more quickly in the United States than abroad. Beginning in September, however, the dollar resumed the depreciation that had started in 2002, as market participants focused on the financing implica-

Equity indexes in selected foreign industrial countries



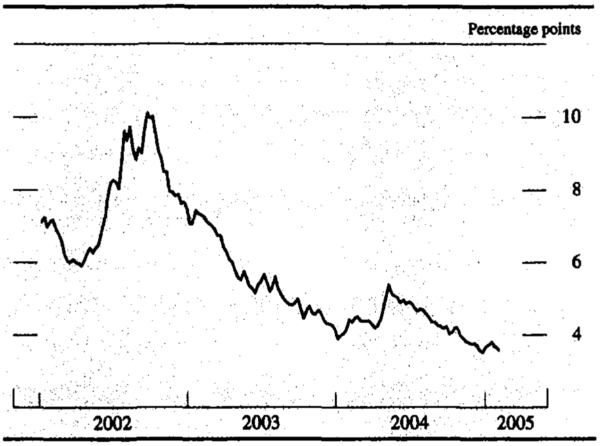
NOTE. The data are weekly. The last observation for each series is the average of trading days through February 9, 2005.
SOURCE. Bloomberg L.P.

Official interest rates in selected foreign industrial countries



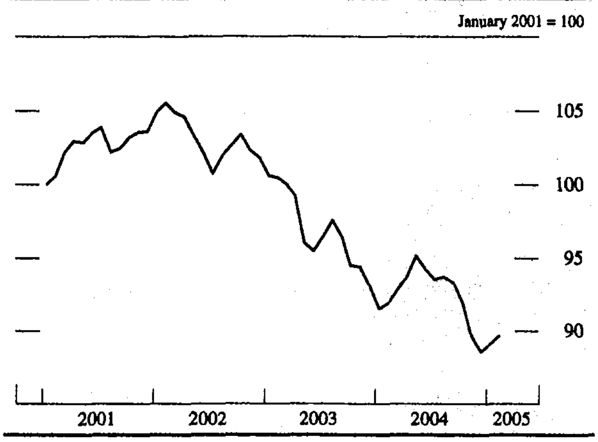
NOTE. The data are as of month-end; the last observation for each series is the average of trading days through February 9, 2005. The data shown are the call money rate for Japan, the overnight rate for Canada, the refinancing rate for the euro area, and the repurchase rate for the United Kingdom.

Spread on internationally issued sovereign debt of emerging-market economies



NOTE. The data are weekly averages. The last observation is the average of trading days through February 9, 2005. The series shown is the spread of the yield of certain dollar-denominated sovereign debt instruments of emerging-market economies over U.S. Treasury securities; over the period shown, the index encompassed nineteen countries.
SOURCE. J.P. Morgan Emerging Market Bond Index Plus (EMBI+).

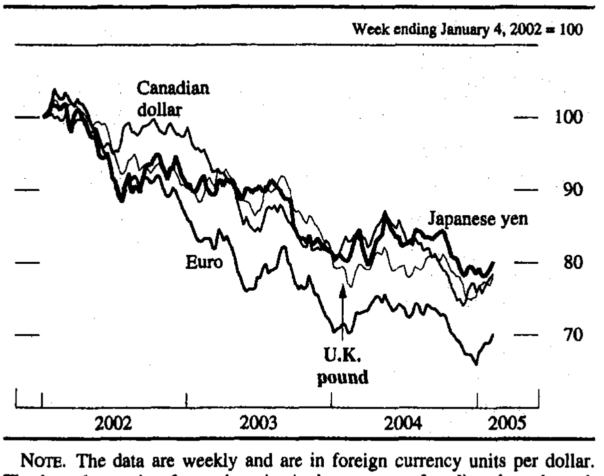
U.S. dollar nominal exchange rate, broad index



NOTE. The data are monthly and are in foreign currency units per dollar. The last observation is the average of trading days through February 9, 2005. The broad index is a weighted average of the foreign exchange values of the U.S. dollar against the currencies of a large group of major U.S. trading partners. The index weights, which change over time, are derived from U.S. export shares and from U.S. and foreign import shares.

tions of the large and growing U.S. current account deficit. In 2004, the dollar depreciated about 7 percent, on net, against the euro, the U.K. pound, and the Canadian dollar. The dollar declined 4 percent, on net, against the Japanese yen and 13 percent against the Korean won, but some other Asian central banks, most notably the People's Bank of China, kept their currencies stable against the dollar. So far in 2005, the dollar has rebounded, with market commentary focusing on the positive differential between U.S. economic growth and that in Europe and Japan.

U.S. dollar exchange rate against selected major currencies



NOTE. The data are weekly and are in foreign currency units per dollar. The last observation for each series is the average of trading days through February 9, 2005.
SOURCE. Bloomberg L.P.

Industrial Economies

After increasing strongly in the first quarter, Japanese GDP growth stagnated in the remainder of 2004. Growth in exports and business investment slowed over the year, and government investment contracted. However, corporate profits and balance sheets improved, and labor market conditions also brightened, with the job-offers-to-applicants ratio rising to a twelve-year high. Consumer prices continued to decline in 2004, though only slightly. In contrast, higher commodity prices helped push twelve-month wholesale price inflation up to 2 percent late in the year, its highest rate since 1990. The yield on the ten-year bellwether government bond rose from its June 2003 record low of about ½ percent to nearly 2 percent in midyear before retreating to about 1½ percent recently. After making substantial sales of yen for dollars in the first quarter, Japanese authorities ceased intervention in mid-March and remained on the sidelines even as the yen appreciated significantly against the dollar in the fall.

Economic conditions in the euro area firmed during the first half of 2004 but weakened in the second half. Private consumption and investment spending continued to rise, but export growth slowed after midyear. German GDP growth slowed to a crawl in the second half, as German consumer spending remained anemic, held down by a weak labor market and low consumer confidence. In contrast, French GDP growth was strong in the fourth quarter. The euro-area unemployment rate has been near 9 percent since rising to that level in early 2003. Inflation for the euro area remained just above the European Central Bank's medium-term goal of less than, but close to, 2 percent.

With the exception of a slowdown in the third quarter, economic expansion in the United Kingdom stayed strong during 2004, largely because of the brisk growth of consumption and government spending. Labor markets remained tight in 2004; the unemployment rate ticked down to its lowest level in almost three decades, and labor earnings posted solid gains. Consumer price inflation over the twelve months ending in December was 1½ percent, below the central bank's official target rate of 2 percent. Housing price rises slowed sharply from rapid rates and were muted during the second half of 2004. Household net mortgage borrowing declined to a level 20 percent below its 2003 peak.

The Canadian economy expanded at a healthy pace throughout 2004. Sizable gains in consumption and investment boosted output throughout the year. Export growth, supported by demand from the United

States, was strong in the first half of the year but stagnated in the second half as U.S. manufacturing growth slowed and the Canadian dollar's appreciation hurt Canadian trade. The unemployment rate declined moderately over the year, and employment posted strong gains. Consumer price inflation has settled at about 2 percent, the midpoint of the Bank of Canada's inflation target range, whereas inflation excluding food, energy, and indirect taxes declined to around 1½ percent by year-end.

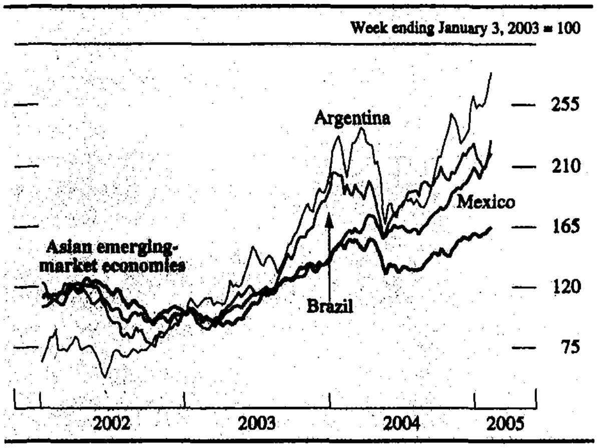
Emerging-Market Economies

Growth of real GDP in China remained very robust in 2004, supported by strong domestic demand and exports. The Chinese government took steps early in the year to slow investment spending, curbing investment approvals and lending. Investment growth slowed significantly but remained rapid. At the same time, indicators of personal consumption spending strengthened, and Chinese exports and imports continued to soar in 2004. Consumer price inflation peaked at a twelve-month change of more than 5 percent in July but has fallen since then to less than 3 percent, as food prices have moderated. Inflation excluding food is only about 1 percent.

Supported by exports to China, economic growth in other Asian emerging-market economies was generally strong in 2004. Economic expansion in Korea remained heavily dependent on external demand because high levels of consumer debt continued to weigh on consumption spending. Inflation across emerging Asia, though still moderate, was pushed up by higher energy prices and strong aggregate demand.

The Mexican economy grew rapidly in the first half of the year in response to strong demand from the United States. In the third quarter, Mexican GDP growth slowed somewhat, as manufacturing exports stagnated, but domestic demand remained buoyant. Increases in energy and food prices pushed up twelve-month consumer price inflation to more than 5 percent, above the Bank of Mexico's target range of 2 percent to 4 percent. Monetary policy tightened throughout the year, and inflation began to fall near year-end. Oil revenues boosted the Mexican public-

Equity indexes in selected emerging-market economies



NOTE. The data are weekly. The last observation for each series is the average of trading days through February 9, 2005. The Asian emerging-market economies are China, Hong Kong, India, Indonesia, Malaysia, Pakistan, the Philippines, Singapore, South Korea, Taiwan, and Thailand; the index weight for each of these economies is its market capitalization as a share of the group's total.

SOURCE. Asian emerging-market economies, Morgan Stanley Capital International (MSCI) index; for others, Bloomberg L.P.

sector fiscal surplus and allowed Mexican government spending to provide stimulus while still meeting fiscal targets.

In Brazil, economic activity continued to expand robustly in 2004. Domestic demand was supported by the monetary loosening that occurred in the second half of 2003 and early 2004. Export growth was boosted by demand for commodities and the recovery in Argentina. Brazilian asset prices declined through May on expectations that higher global interest rates would make it more difficult for the Brazilian government to finance its debt, but stock prices have moved up sharply since May, and the currency has appreciated. Concerns over inflation pressures have prompted the central bank to tighten monetary policy since September.

In Argentina, the economic recovery picked up steam last year, as exports were supported by strong demand for commodities. The country continues, however, to grapple with difficult structural problems. After more than three years in default, the government launched a debt swap in January with the goal of restructuring more than $80 billion in defaulted bonds. □

Profits and Balance Sheet Developments at U.S. Commercial Banks in 2004

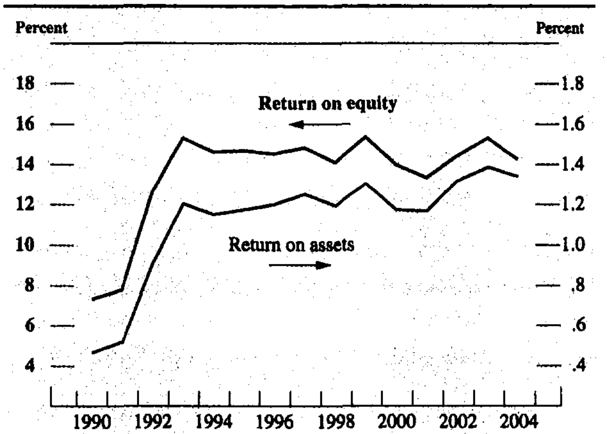
Elizabeth C. Klee and Fabio M. Natalucci, of the Board's Division of Monetary Affairs, prepared this article. Thomas C. Allard assisted in developing the database underlying much of the analysis. Arshia A. Burney provided research assistance.

U.S. commercial banks continued to be highly profitable in 2004. Return on assets and return on equity declined moderately from the previous year's levels, but they remained in the elevated range that has prevailed since the mid-1990s (chart 1). Banks' profitability and balance sheets benefited from a brisk expansion of the economy and supportive financial conditions during 2004. Although the Federal Reserve gradually raised its target for the federal funds rate over the second half of the year, the stance of policy remained accommodative (chart 2). Short- and intermediate-term interest rates rose over the course of the year, but yields on longer-term Treasury securities were little changed on net, and the Treasury yield curve flattened noticeably. Interest rates on residential mortgages ended the year a touch lower, on balance, and continued to support robust housing activity. Risk spreads on corporate bonds—particularly high-yield bonds—narrowed substantially.

Favorable financial market conditions, accompanied by a stimulative fiscal policy and continued rapid growth in productivity, supported economic activity. Buoyant consumer spending on durable and nondurable goods reflected solid income growth, improvements in labor market conditions, and greater household wealth; the greater wealth, in turn, arose from gains in the stock market and continued sharp increases in house prices. Healthy profits and cash flows encouraged business investment in equipment and software, which rose smartly throughout the year. Businesses also added considerably to inventories for the first time since 2001. With the financial obligations ratio of households stabilizing below the peak reached at the end of 2002 and the debt burden for nonfinancial corporations continuing to fall, households and businesses had relatively strong financial positions overall during 2004.

These economic and financial conditions were reflected in the changes in bank balance sheets over the year. The robust activity in the housing sector and generally low mortgage interest rates buoyed residential mortgage lending at banks despite the ebbing of the 2003 refinancing wave. Even though consumer spending was strong, consumer loans advanced at only a moderate pace and likely were restrained by the substitution of mortgage debt for higher-rate con-

1. Bank profitability, 1990–2004

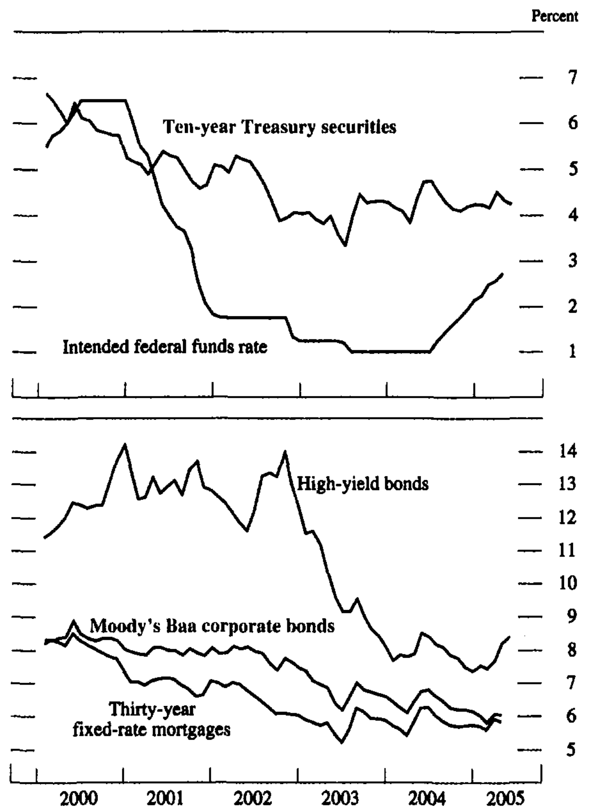


NOTE. The data are annual.

NOTE. Except where otherwise indicated, data in this article are from the quarterly Reports of Condition and Income (Call Report) for insured domestic commercial banks and nondeposit trust companies (hereafter, banks). The data consolidate information from foreign and domestic offices and have been adjusted to take account of mergers and the effects of push-down accounting. For additional information on the adjustments to the data, see the appendix in William B. English and William R. Nelson (1998), "Profits and Balance Sheet Developments at U.S. Commercial Banks in 1997," *Federal Reserve Bulletin*, vol. 84 (June), p. 408. Size categories, based on assets at the start of each quarter, are as follows: the ten largest banks, large banks (those ranked 11 through 100), medium-sized banks (those ranked 101 through 1,000), and small banks. At the start of the fourth quarter of 2004, the approximate asset sizes of the banks in those groups were as follows: the ten largest banks, more than $96 billion; large banks, $6.7 billion to $96 billion; medium-sized banks, $422 million to $6.6 billion; and small banks, less than $422 million.

Data shown in this article may not match data published in earlier years because of revisions and corrections. In the tables, components may not sum to totals because of rounding. Appendix table A.1, A–E, reports portfolio composition, income, and expense items, all as a percentage of overall net consolidated assets. Appendix table A.2 reports income statement data for all banks.

2. Selected interest rates, 2000–05



NOTE. The data are monthly and extend through March 2005.

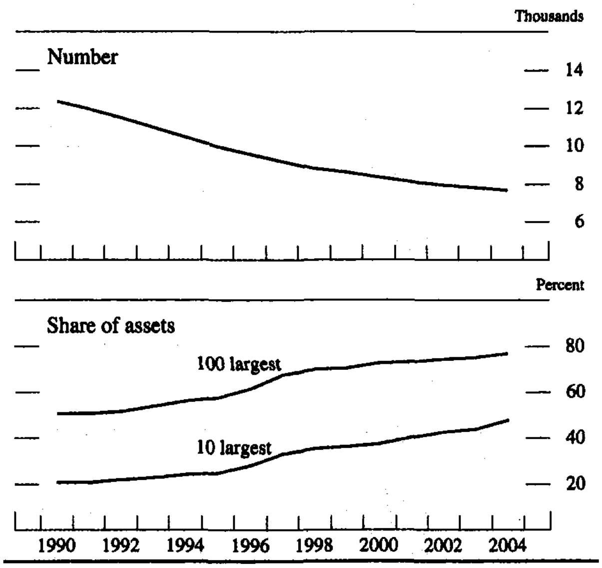
SOURCE. For Treasury securities, mortgages, and Moody's corporate bonds, Federal Reserve Board, Statistical Release H.15, "Selected Interest Rates" (www.federalreserve.gov/releases/h15); for federal funds, Federal Reserve Board (www.federalreserve.gov/fomc/fundsrate.htm); for high-yield bonds, Merrill Lynch Master II index.

sumer credit. Strong cash flows and profits allowed many nonfinancial corporations to finance capital spending with internal funds and thus reduce their borrowing needs. Nonetheless, after three years of retrenchment, short-term business debt—consisting of commercial and industrial (C&I) loans from banks and commercial paper—rose last year to meet firms' greater need to fund accounts receivable, inventories, capital expenditures, and merger and acquisition activity. C&I loans also received a boost from the supply side, as banks reported easing their lending standards and terms throughout the year. Banks also reported easing their standards and terms on commercial real estate loans, and such loans increased despite soft conditions overall in that sector. Still-low interest rates fueled the growth of core deposits, but the rise was insufficient to fund the increase in bank assets.[1] As a result, banks relied more heavily on managed liabilities, which rose strongly last year.

Economic and financial developments also strongly influenced banks' profitability in 2004. As the yield curve flattened markedly, the net interest margin narrowed a bit further. The net interest margin may also have been eroded by increased competition in the C&I loan market, which contributed to a narrowing of loan spreads over reference rates. Gains in non-interest income were less pronounced than in 2003. Despite contributions from fiduciary activities, loan-servicing fees, and securitization activities, the growth of non-interest income was restrained by weakness in investment banking revenue, a marked contraction in trading income, and a decline in gains from loan sales. Meanwhile, non-interest expense, which rose briskly, was boosted by provisions for litigation and expenses related to sizable mergers at a few large banks. However, the continued improvement in overall credit quality throughout the year allowed banks to trim their provisioning for loan and lease losses, and delinquency and charge-off rates for all loan categories trended down. Realized gains on investment-account securities declined last year but still contributed to income.

Although more new commercial banks were chartered in 2004 than in 2003, merger activity increased, and the number of banks fell to 7,678 at year-end (chart 3). Some of the merger activity involved very large banks and thus contributed to an increase in the concentration of industry assets. The share of indus-

3. Number of banks, and share of assets at the largest banks, 1990–2004



NOTE. The data are annual. For the definition of bank size, see the general note on the first page of the main text.

1. Core deposits are transaction deposits, savings deposits (including money market deposit accounts), and small time deposits.

1. Annual rates of growth of balance sheet items, 1995–2004
Percent

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	MEMO: Dec. 2004 (billions of dollars)
Assets	7.59	6.13	9.22	8.18	5.44	8.76	5.12	7.19	7.19	10.77	8,258
Interest-earning assets	7.82	5.82	8.66	8.20	5.83	8.66	3.95	7.54	7.29	11.29	7,157
Loans and leases (net)	10.61	8.17	5.32	8.76	8.03	9.24	1.82	5.90	6.52	11.21	4,736
Commercial and industrial	12.25	7.24	12.02	12.94	7.88	8.54	–6.73	–7.41	–4.56	4.40	899
Real estate	8.28	5.45	9.30	7.99	12.22	10.74	7.94	14.43	9.78	15.38	2,595
Booked in domestic offices	8.43	5.51	9.53	7.97	12.36	11.02	8.02	14.85	9.68	15.05	2,547
One- to four-family residential	10.01	4.66	9.67	6.36	9.70	9.28	5.70	19.85	10.05	15.79	1,468
Other	6.21	6.75	9.32	10.29	16.06	13.31	10.95	8.81	9.20	14.07	1,079
Booked in foreign offices	2.81	3.18	.34	8.79	6.28	–1.62	3.97	–7.41	15.74	35.59	48
Consumer	10.01	5.12	–2.19	.34	–1.49	8.04	4.16	6.58	9.31	10.12	782
Other loans and leases	14.22	22.28	–7.91	13.95	6.71	7.01	–2.02	–.02	8.30	3.64	533
Loan-loss reserves and unearned income	.46	.04	–.45	3.11	2.34	7.99	13.15	5.74	–2.68	–4.19	73
Securities	.56	.86	8.85	8.40	5.11	6.36	7.22	16.20	9.44	10.58	1,838
Investment account	–1.58	–1.10	8.66	12.06	6.68	2.86	8.88	13.54	8.70	6.15	1,510
U.S. Treasury	–19.21	–14.28	–8.85	–25.17	–1.89	–32.72	–40.27	41.92	14.18	–15.86	61
U.S. government agency and corporation obligations	6.42	3.63	14.18	17.00	1.83	3.75	12.84	18.10	9.67	9.47	989
Other	4.19	1.83	11.21	26.99	20.90	13.39	12.18	2.72	5.98	3.01	461
Trading account	18.51	14.44	10.00	–13.32	–6.93	37.16	–3.72	36.02	14.05	36.80	328
Other	8.61	1.06	38.54	3.79	–8.37	10.30	13.00	–2.92	6.83	14.31	584
Non-interest-earning assets	6.06	8.29	13.03	8.10	2.90	9.45	12.81	5.06	6.62	7.54	1,101
Liabilities	7.22	5.99	9.11	8.06	5.58	8.59	4.45	7.12	7.25	9.54	7,428
Core deposits	3.94	4.13	4.52	7.04	.23	7.53	10.55	7.58	7.30	8.24	3,974
Transaction deposits	–3.11	–3.44	–4.55	–1.41	–8.97	–1.31	10.20	–5.12	2.90	3.18	744
Savings and small time deposits	8.35	8.35	9.04	10.73	3.80	10.54	10.66	11.42	8.43	9.48	3,230
Managed liabilities[1]	10.61	9.73	13.79	9.44	15.54	8.79	–2.73	5.34	6.97	12.06	2,911
Deposits booked in foreign offices	5.13	4.27	11.13	8.71	14.60	7.84	–10.96	4.49	12.63	16.84	865
Large time	19.60	21.17	20.15	9.09	14.19	19.37	–3.65	5.05	1.43	21.82	705
Subordinated notes and debentures	6.61	17.74	21.05	17.00	5.07	13.98	9.56	–.59	5.08	10.49	109
Other managed liabilities	11.63	8.38	12.14	9.49	17.76	3.90	2.47	6.55	6.62	4.42	1,232
Federal Home Loan Bank advances	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	17.21	3.74	3.68	244
Other	20.49	2.60	23.80	8.57	–6.37	15.40	3.10	13.55	8.38	6.06	543
Equity capital	12.06	7.77	10.44	9.53	3.89	10.65	12.32	7.83	6.61	23.16	830
MEMO											
Commercial real estate loans[2]	6.32	7.67	10.13	11.37	15.42	12.16	13.10	6.82	8.99	13.81	1,075
Mortgage-backed securities	.66	2.06	14.16	22.12	–3.34	3.29	29.05	15.56	10.10	13.01	861

NOTE. Data are from year-end to year-end.

1. Measured as the sum of deposits in foreign offices, large time deposits in domestic offices, federal funds purchased and securities sold under repurchase agreements, demand notes issued to the U.S. Treasury, subordinated notes and debentures, and other borrowed money.

2. Measured as the sum of construction and land development loans secured by real estate; real estate loans secured by nonfarm nonresidential properties or by multifamily residential properties; and loans to finance commercial real estate, construction, and land development activities not secured by real estate.

try assets held by the 10 largest banks rose 3.9 percentage points, to 48.0 percent; the share held by the 100 largest banks rose 1.6 percentage points, to 76.9 percent. Three banks failed in 2004 with combined assets of just $151 million.

Merger activity also continued at the bank holding company level, and the number of top-tier bank holding companies declined by 4 in 2004, to 5,148. As they did at the bank level, mergers drove up the concentration of assets at bank holding companies. The share of assets of all bank holding companies held by fifty large bank holding companies rose to about 77 percent.[2] The Gramm–Leach–Bliley Act of 1999 created the option for bank holding companies to become financial holding companies; as such, they are allowed to engage in activities related to securities underwriting, insurance sales and underwriting, and merchant banking. During 2004 the

2. The number of bank holding companies and related statistics shown here include all top-tier bank holding companies. The fifty large bank holding companies are defined as the fifty largest bank holding companies as measured by total consolidated assets after the exclusion of a few institutions whose commercial banking operations account for only a small portion of their assets and earnings. The article "Report on the Condition of the U.S. Banking Industry: Fourth Quarter 2004," also in this issue, provides information on the fifty large bank holding companies and on the banking industry from the perspective of bank holding companies (including financial holding companies) that file reports FR Y-9C and FR Y-9LP; currently, only about 2,200 top-tier bank holding companies are required to file those reports (see "Report on the Condition," table 1, last row, and note 1).

number of financial holding companies increased to 636, and by the end of the year, more than 80 percent of assets at bank holding companies were held by financial holding companies.

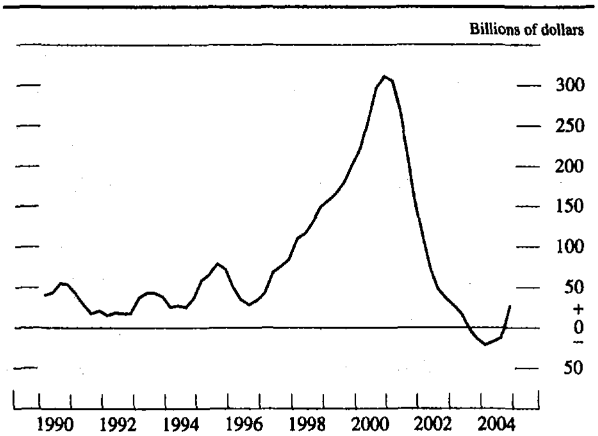
Balance Sheet Developments

Total assets of U.S. commercial banks grew 10.8 percent in 2004, about 3 percentage points faster than the growth in total debt of the domestic nonfinancial sector and the fastest rate in more than a decade (table 1). Securities expanded 10.6 percent, and loans and leases advanced 11.2 percent. Reflecting the growth in both business and household spending last year, all major loan categories advanced for the first time since the late 1990s.

Liabilities grew 9.5 percent last year. Low opportunity costs supported growth in core deposits, but the rate of increase was insufficient to meet the rise in assets. Remaining funding needs were met with a rapid expansion of managed liabilities—most notably large time deposits.

Bank capital rose to 9.4 percent of average net consolidated assets in 2004, and that gain also helped fund asset growth. Capital expanded because of the growth in retained earnings as well as increases in goodwill resulting from significant merger activity. Goodwill and other intangible assets boost reported assets and capital but are not included in regulatory capital ratios. These ratios were little changed and thus remained in the very high ranges seen in recent years.

4. Financing gap at nonfarm nonfinancial corporations, 1990–2004



Note. The data are four-quarter moving averages. The financing gap is the difference between capital expenditures and internally generated funds.

Source. Federal Reserve Board, Statistical Release Z.1, "Flow of Funds Accounts of the United States," table F. 102 (www.federalreserve.gov/releases/z1).

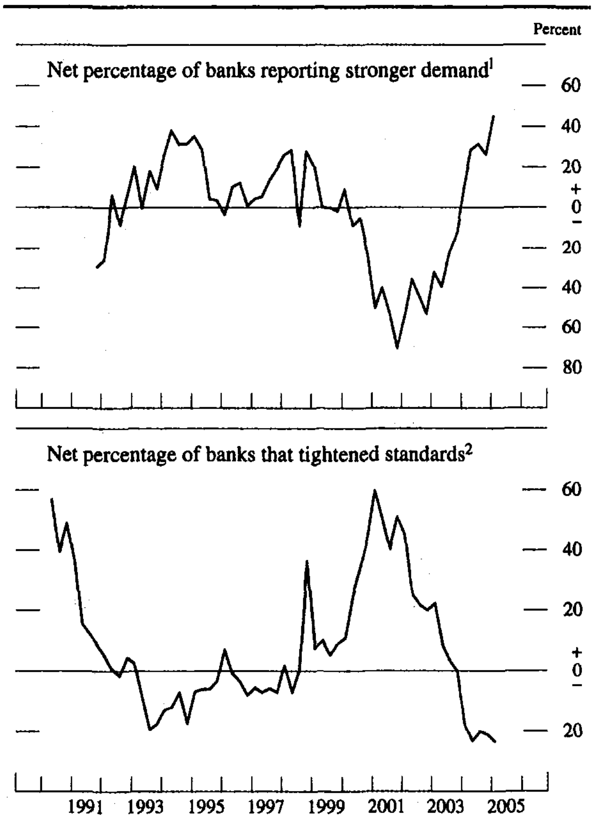
Loans to Businesses

The net financing gap—the difference between capital expenditures and internally generated funds of the U.S. nonfinancial sector—increased last year from the low point it had reached in the third quarter of 2003 (chart 4).[3] In addition, net bond issuance in 2004 was lower than in 2003. Firms relied more on commercial paper and bank loans to meet their funding needs; C&I loans grew 4.4 percent in 2004.

Responses to the Federal Reserve's quarterly Senior Loan Officer Opinion Survey on Bank Lend-

3. The net financing gap rose in the fourth quarter because of a special dividend payment by Microsoft that reduced internal funds by $32 billion. Even after excluding this special payment, however, the financing gap increased over 2004.

5. Demand and supply conditions for C&I loans at selected banks, large and medium-sized borrowers, 1990–2005



Note. The data are drawn from a survey generally conducted four times per year; the last observation is for the January (Q1) 2005 survey. Net percentage is the percentage of banks reporting an increase in demand or a tightening of standards less, in each case, the percentage reporting the opposite. The definition for firm size suggested for, and generally used by, survey respondents is that large and medium-sized firms have sales of $50 million or more.

1. Series begins with the November 1991 survey.

2. Series begins with the May 1990 survey.

Source. Federal Reserve Board, "Senior Loan Officer Opinion Survey on Bank Lending Practices" (www.federalreserve.gov/boarddocs/snloansurvey).

ing Practices (BLPS) suggest that both stronger demand and easier standards and terms contributed to the growth in business loans. The share of respondents reporting stronger demand for C&I loans rose significantly in the 2004 surveys and exceeded 40 percent in the January 2005 survey (chart 5). Reasons cited for increased demand included increases in inventories and accounts receivable, plant and equipment expenditures, and mergers and acquisitions.

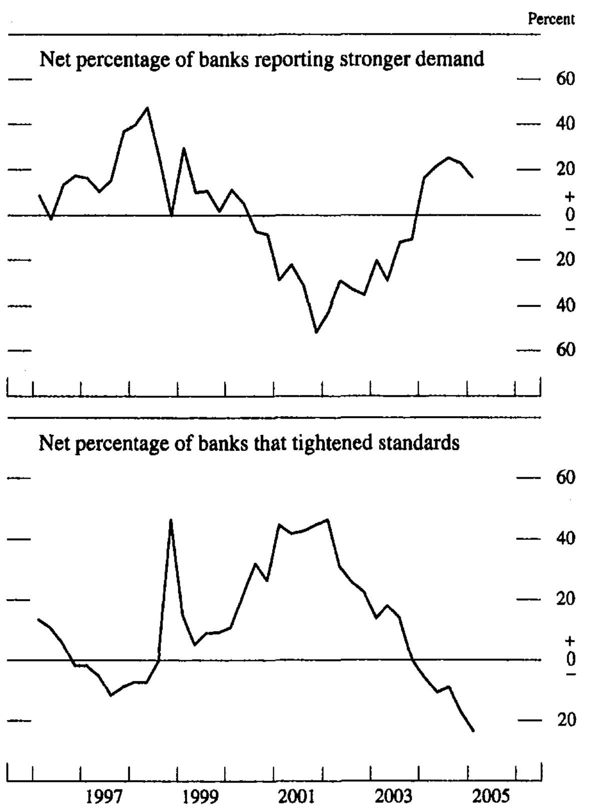
Small and medium-sized banks—which typically lend to smaller businesses—saw substantial increases in C&I loans in 2004 (13.6 percent for small banks and 9.9 percent for medium-sized banks). In contrast, C&I loans at the ten largest banks were essentially flat, but they had previously been in a period of sustained decline. This difference across bank sizes is consistent with data from the June 2004 Call Report, which show that small business loans (original amounts of $1 million or less) grew from mid-2003 to mid-2004, while larger C&I loans contracted. Throughout the year, larger net percentages of BLPS respondents reported increased demand for C&I loans from small borrowers (those with sales of less than $50 million) than from large- and medium-sized borrowers.

Significant fractions of banks responding to the BLPS in 2004 reported also having eased C&I lending standards, in large part because of a firmer economic outlook (chart 5). Moreover, appreciable fractions of respondents reported throughout 2004 and into 2005 that they had eased C&I loan terms—including loan sizes, costs of credit lines, spreads, covenants, and collateralization requirements (data not shown in chart). This easing of loan terms is confirmed by results from the Federal Reserve's quarterly Survey of Terms of Business Lending, which show that banks extended C&I loans of increasing maturity and larger size throughout the year. Another factor influencing C&I lending terms, according to BLPS respondents, was increased competition from other banks and from nonbanks.[4]

Commercial real estate (CRE) loans rose 13.8 percent in 2004. Growth rates of real-estate-secured loans for construction and land development and of loans secured by multifamily properties were particularly strong in the second half of the year as the economy improved. As in previous years, growth rates at medium-sized and small banks were more than twice those posted at larger banks (see box "Commercial Real Estate Loans").

Responses to the BLPS indicated that demand for CRE loans increased throughout the year, although the net percentage of banks reporting increases in demand dipped a bit in early 2005 (chart 6). Respondents also said that they had eased standards and terms on these loans over 2004. The reasons given for easing were similar to those for C&I loans, including more competition from other lenders and an improved economic outlook.

6. Demand and supply conditions for commercial real estate loans at selected banks, 1996–2005



Note. See general note and source note to chart 5.

Loans to Households

Mortgage rates remained low over the course of 2004, and with income and employment advancing, the housing sector expanded strongly again. Against this favorable backdrop, residential mortgage loans grew 15.8 percent in 2004, the fifth consecutive year of gains and an even faster growth rate than in 2003. Residential mortgages, which are loans secured by one- to four-family residential properties and include first-lien mortgages and home equity loans, represent the largest share of bank loans to house-

4. For more details, see the discussion in "Interest Income and Expense" below in the section "Trends in Profitability."

Commercial Real Estate Lending by Smaller Banks

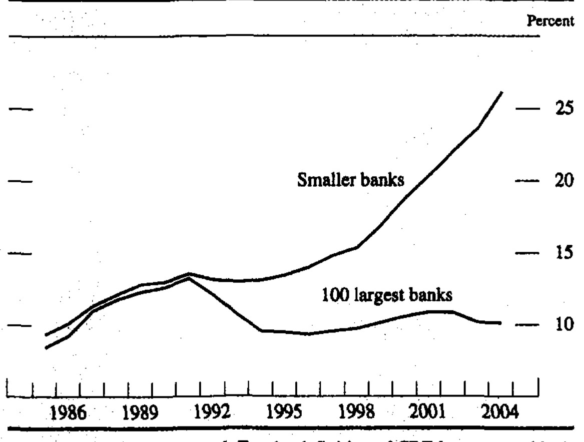
At the 100 largest banks, the share of assets that consists of commercial real estate (CRE) loans has changed little in recent years, while the share at medium-sized and small banks (hereafter, smaller banks) has increased substantially (chart A). This discussion explores some of the possible reasons for, and consequences of, the rapid accumulation of CRE loans at smaller banks. The growth in CRE loans at smaller banks as a group masks considerable variation across banks. We examined the distribution of growth rates of CRE loans at more than 5,000 smaller banks that had at least 1 percent of assets invested in CRE loans at the end of 1996 and remained in existence through the end of 2004. The median quarterly (annualized) growth rate of CRE loans over that period was between 5 percent and 20 percent for more than half of these banks; but about 15 percent of the banks saw runoffs in these loans, while roughly 10 percent of the banks had growth rates exceeding 25 percent (chart B). To facilitate the analysis, we classified each bank as "high growth" or "low growth" depending on whether the median rate of growth of its CRE loans was above or below the distribution's median value of 10.6 percent for all smaller banks in the 1997–2004 period. We then investigated the relative performance of the two groups over that period.

The return on assets at high-growth banks has generally been higher than the return on assets at low-growth banks in recent years (chart C). Similarly, the return on equity (not shown) has been markedly higher at high-growth banks, in part because of their generally greater leverage. This better performance also reflects higher net interest margins at high-growth banks than at low-growth banks over the same period (data not shown). Delinquency rates on CRE loans have been relatively low by historical standards for both groups of banks. The delinquency rate at high-growth banks has been consistently below the rate at low-growth banks (chart D). The better performance of the high-growth banks in this regard may reflect, in part, the very fact of more rapid growth in such loans because new loans are presumably unlikely to default for a time.

A portion of CRE loans consists of C&I loans that are collateralized by real estate—that is, loans the proceeds of

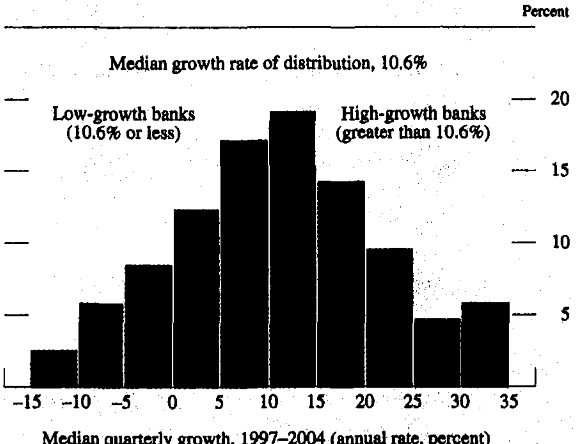
NOTE. Thomas F. Brady, of the Division of Monetary Affairs, prepared this material.

A. Commercial real estate loans as a proportion of assets, by bank size, 1985–2004



NOTE. The data are annual. For the definition of CRE loans, see table 1, note 2. Smaller banks are those smaller than the 100 largest; for more detail on size categories, see general note on the first page of the main text.

B. Distribution of median growth rates of CRE loans at smaller banks, 1997–2004



NOTE. For the definition of CRE loans and smaller banks, see chart A. The growth rates are those of the 5,731 smaller banks that had at least 1 percent of assets invested in CRE loans at the end of 1996 and remained in existence through the end of 2004; these banks corresponded to about 76 percent of the total number of smaller banks and roughly 82 percent of their total assets at the end of 2004. For each bank, we calculated the merger-adjusted growth rate of CRE loans for each quarter and then took the median of its thirty-two quarterly growth rates.

Commercial Real Estate Lending by Smaller Banks—Continued

which were not used to purchase or improve the securing real estate. (Call Report instructions specify that any loan secured by real estate is to be reported as a real estate loan.) In March 2005, Federal Reserve System staff members contacted nine smaller banks that had high concentrations of, and rapid growth in, CRE loans to inquire about their CRE lending. Asked what percentage of their CRE loans were C&I loans secured by real estate, the nine smaller banks gave answers that ranged from about 2 percent to about 30 percent, with most less than 10 percent.[1]

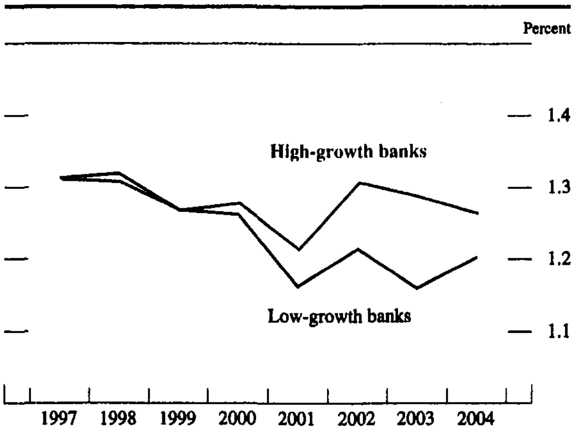
A few of these banks indicated that over the three years ending in the first quarter of 2005, they had tightened CRE lending standards somewhat, on net, but similar fractions noted some tendency to ease loan terms by, for example, raising maximum loan sizes, trimming loan spreads over costs of funds, and boosting loan-to-value ratios. However, these banks had tightened debt-service coverage ratios, on net. They also indicated that their CRE lending over the past three years had been secured by properties located in both urban and suburban areas and to a lesser extent in exurban areas. The types of securing properties most frequently mentioned were warehouses and other industrial structures; also mentioned were office buildings as well as nursing homes and other medical facilities.

The two most frequently mentioned reasons for the rapid growth of CRE lending over the past three years were generally favorable economic conditions and population growth in the banks' lending markets. Banks also mentioned that profitable investment in office buildings sometimes coincided with high vacancy rates because some of the vacant offices were less well suited for the types of businesses expanding in their markets. The banks generally did not attribute much of the growth to an increase in the share of CRE loans that represented real-estate-secured C&I loans. Banks reporting an increase in that share cited two factors: rising values of commercial structures, which increased the capacity of their owners to borrow, and the banks' imposition of stricter collateral requirements on borrowers.

The rapid run-up in CRE loans over the past three years raises questions about its effects on other aspects of banks' balance sheets. The responses of the banks contacted suggest that the growth was accommodated in part by reducing capital-to-asset ratios, although banks also reported raising new capital to meet the rising demand for CRE credit. The banks generally reported that they had not reduced acquisitions of securities or limited the growth of other types of loans to accommodate the additional CRE assets.

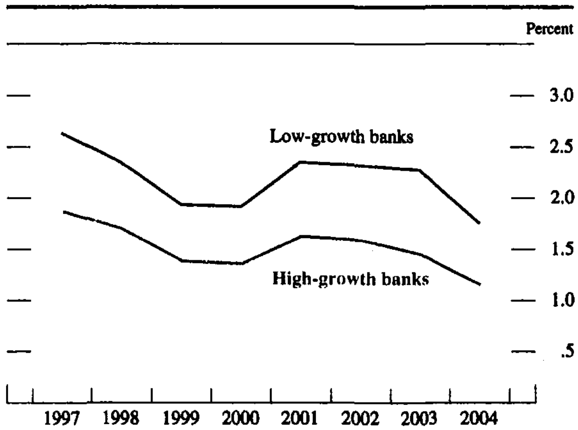
1. A similar question was asked in the Federal Reserve Board's August 2002 Senior Loan Officer Opinion Survey on Bank Lending Practices; the institutions responding to the survey are generally much larger than the smaller banks under discussion here. For the fifty-three banks answering the question, the answer ranged from less than 2 percent to more than 30 percent, with most less than 20 percent. The average for all fifty-three respondents was about 15 percent.

C. Return on assets at smaller banks, 1997–2004



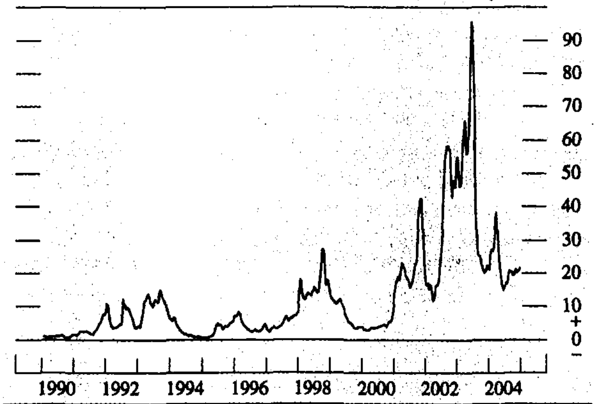
NOTE. For definitions, see charts A and B.

D. Delinquency rates on CRE loans at smaller banks, 1997–2004



NOTE. The data are annual. For the definition of delinquency rates on CRE loans, see the note to chart 22; for other definitions, see charts A and B.

7. Residential mortgage refinancing activity, 1990–2004

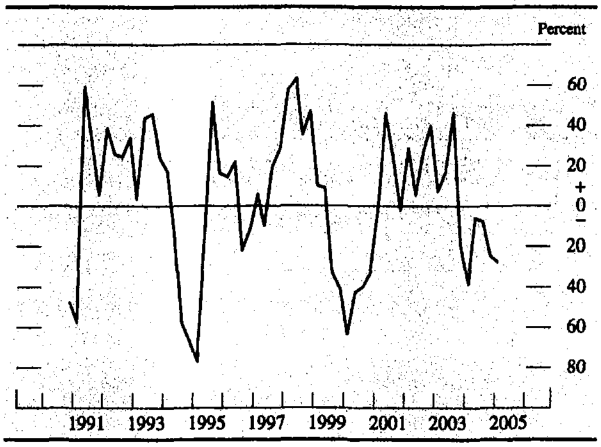


NOTE. The data are four-week moving averages. For definition of residential mortgages, see text.
SOURCE. Mortgage Bankers Association.

holds. Much of the acceleration in residential mortgages resulted from growth in revolving home equity loans, which rose more than 40 percent. Mortgage loans grew especially fast early in the year, when long-term interest rates had declined to a very low level. The low rates generated a renewed flurry of refinancing activity (chart 7) that was accompanied by strong demand for mortgages to finance home purchases. As these rates backed up a bit in anticipation of monetary policy tightening, growth slowed somewhat but remained elevated through the end of the year.

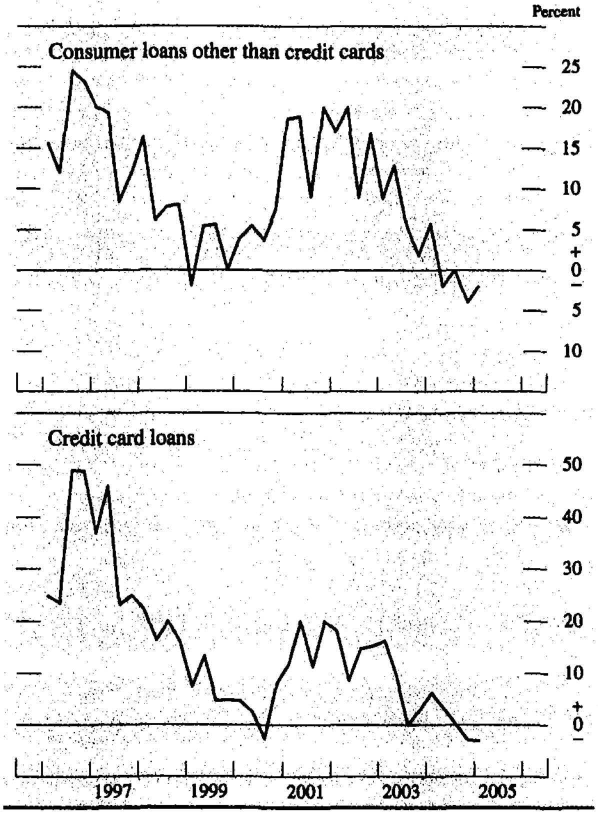
On net, BLPS respondents reported decreased demand for residential mortgages throughout the year (chart 8). Fluctuations over the course of the year in the percentage of banks reporting demand increases seemed to reflect changes in the trend of refinancing

8. Net percentage of selected banks reporting stronger demand for residential mortgages, 1990–2005



NOTE. Series begins with the October 1990 survey. For definition of residential mortgages, see text. See also general note and source note to chart 5.

9. Net percentage of selected banks tightening standards for consumer lending, 1996–2005



NOTE. See general note and source note to chart 5.

activity.[5] In the first half of 2004, the net percentage of banks reporting increased demand rose somewhat, but it dropped back a bit over the latter half of the year.

Residential mortgages have expanded at a double-digit rate since 2002. Responses to special questions on the January 2005 BLPS indicate that several factors contributed to banks' increased holdings of residential mortgages over the previous three years. First, according to 75 percent of the respondents, many mortgages originated over this period had adjustable rates, making them relatively attractive to hold as assets. Second, sustained demand for mortgages had supported their returns. Finally, many banks noted that a widening of spreads between mortgages and mortgage-backed securities made the underlying loans more attractive to hold.

Consumer loans at banks grew 10.1 percent last year. However, after adjustment for the effect of a

5. BLPS respondents are instructed to consider only new loans for home purchase, not refinancings of existing mortgages. In many cases, however, the refinanced mortgage may not be held by the originating bank, making it difficult for the respondents to make this distinction easily.

large merger in the third quarter, the growth rate of consumer loans was a more moderate 5.8 percent.[6]

Banks' standards and terms for consumer loans changed little on net last year according to the BLPS: Approximately the same proportion of banks tightened standards for credit card loans and other consumer loans as eased them (chart 9). Changes in terms reflected a similar trend, with a slight net percentage of domestic respondents having tightened credit card terms and a similarly slight net percentage having done so for other consumer loans (not shown in chart). Overall, demand for consumer loans reportedly moderated.

Other Loans and Leases

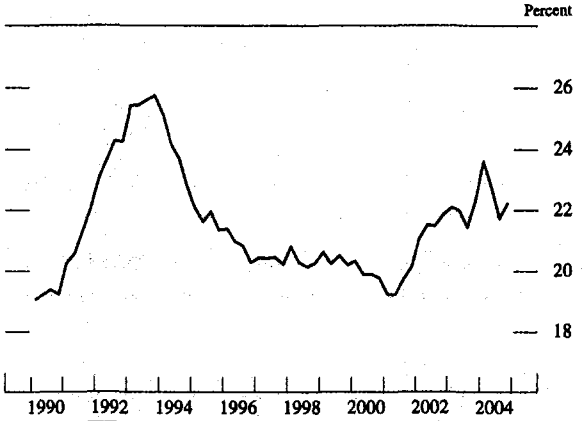
Banks' holdings of other loans and leases grew 3.6 percent in 2004. Although the rate marks a slowdown from 2003, growth in that year was heavily influenced by an accounting change that shifted into this category an estimated $42 billion in assets that were previously off-balance-sheet items.[7] A 5 percent rise in farm loans reversed a downward trend seen since 2001. Improved overall economic conditions strengthened the fiscal situation of many state and local governments and contributed to a slowing in the growth of loans to this sector from 16.8 percent in 2003 to a still-rapid 13.9 percent in 2004.

Securities

Banks expanded their securities holdings considerably again in 2004. Last year's 10.6 percent advance was more than 1 percentage point faster than the 2003 pace and about in line with total asset growth. Much of the growth reflected a substantial rise in securities held in trading accounts, which jumped 36.8 percent on the year; securities held in investment accounts advanced 6.2 percent. As a share of average net consolidated assets, securities holdings in 2004 increased for the third year in a row, to 22.6 percent (chart 10).

Mortgage-backed securities in investment accounts, which grew 13 percent over the year, rose to a 10.4 percent share of bank assets at the end of the

10. Bank holdings of securities as a proportion of total bank assets, 1990–2004



NOTE. The data are quarterly.

fourth quarter. As with mortgage loans, banks' holdings of mortgage-backed securities followed the swings of long-term interest rates. Banks accumulated mortgage-backed securities at a rapid clip in the first quarter; as longer-term interest rates rose in anticipation of the policy tightening, such holdings shrank in the second quarter, and they fell further in the third quarter. Growth returned strongly in the fourth quarter after rates declined.

From a longer-term perspective, bank involvement in residential mortgage products has increased dramatically over the past twenty years. In 1985, residential mortgages accounted for 7.3 percent of average net consolidated assets, while agency pass-throughs—one type of mortgage-backed security available to investors at the time—were less than 1 percent. By the end of 1995, the share of residential mortgage products on banks' books had risen to 22.2 percent—14.4 percent in mortgages and 7.8 percent in securities. By the end of 2004, banks' asset share of these products had risen to more than 28 percent.

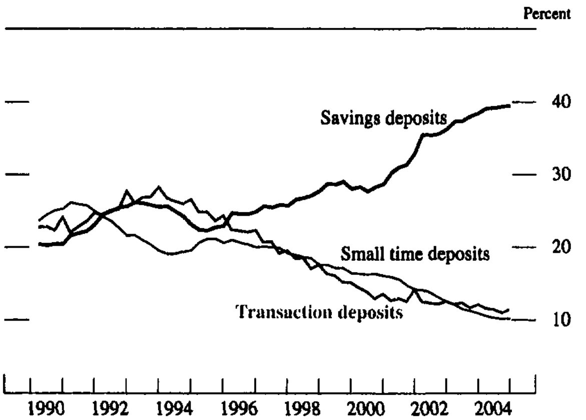
Liabilities

Commercial bank liabilities grew 9.5 percent last year, with all classes of liabilities posting increases. The 8.2 percent growth in core deposits outpaced the previous year's strong advance by about 1 percentage point, but it lagged the expansion in total assets. Some of the run-up in core deposits in the first half of the year was attributable to the decline in mortgage rates in the first quarter (chart 2). The drop in rates led to an increase in refinancing. When securitized mortgages are refinanced, the proceeds are held tem-

6. The merger was of two large bank holding companies and caused a reclassification of certain securitized credit card receivables as credit card loans; credit card outstandings jumped 46.2 percent in the third quarter as a result.

7. For details, see Mark Carlson and Roberto Perli (2004), "Profits and Balance Sheet Developments at U.S. Commercial Banks in 2003," *Federal Reserve Bulletin*, vol. 90 (Spring), p. 168.

11. Selected domestic liabilities at banks as a proportion of their total domestic liabilities, 1990–2004



NOTE. The data are quarterly. Savings deposits include money market deposit accounts.

porarily in a liquid deposit account before disbursement to the securities holders, thereby boosting deposits for a time; the slower pace of refinancing in the second half of the year diminished this effect to some extent. As a share of total liabilities, savings deposits grew during the four quarters of 2004, while the shares of transaction and small-denomination time deposits fell a bit (chart 11).

With the growth of assets outstripping that of core deposits, banks relied more heavily on managed liabilities—defined as the sum of demand notes issued to the U.S. Treasury and other borrowed money, federal funds purchased and securities sold under repurchase agreements, subordinated notes and debentures, large time deposits, and deposits booked in foreign offices. This sum grew 12.1 percent last year, and its share of total liabilities rose to 39.2 percent. For all banks, large time deposits posted the fastest gain, 21.8 percent; at the ten largest banks, such deposits grew even more rapidly, 30.6 percent.

Banks again expanded their use of Federal Home Loan Bank (FHLB) advances in 2004.[8] These loans grew approximately 3.7 percent last year, about the same rate as in 2003, but well below the growth rate of 17.2 percent in 2002. On average last year, FHLB advances equaled 8.6 percent of total managed liabilities at domestic banks—but the proportion was much higher at medium-sized banks (23.9 percent) and at small banks (22.1 percent).

Capital

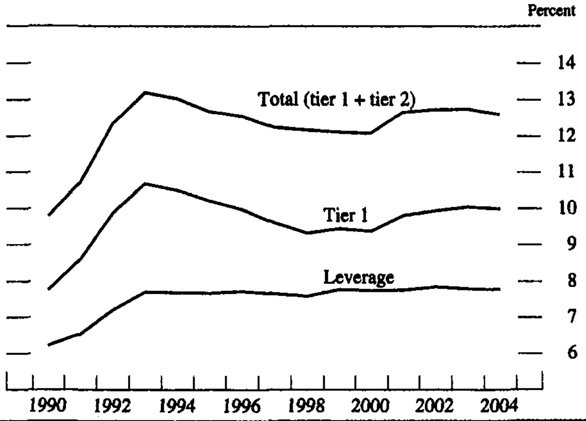
Given the slower growth of liabilities relative to assets, equity capital at banks surged more than 23 percent in 2004. However, much of this increase reflected the effects of accounting for several large mergers, which boosted the value of goodwill.[9] Risk-weighted assets grew 10.5 percent; tier 1 capital (which excludes goodwill) grew 10.0 percent, and tier 2 capital advanced 6.7 percent. As a result, the tier 1 ratio was basically unchanged at about 10 percent, and the total ratio (tier 1 plus tier 2) ticked down slightly; the leverage ratio remained about constant (chart 12).[10] Thus, overall, the share of industry assets

8. The FHLBs were established in 1932 as government-sponsored enterprises chartered to provide a low-cost source of funds, primarily for mortgage lending. They are cooperatively owned by their member financial institutions, a group that originally was limited to savings and loans associations, savings banks, and insurance companies. Commercial banks were first able to join FHLBs in 1989, and since then FHLB advances have become a significant source of funding for them, particularly for medium-sized and small banks.

9. The Financial Accounting Standards Board defines goodwill as an intangible asset equal to the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed—in other words, the premium paid by the acquirer of a firm. For details on how this affected banks' accounting, see Mark Carlson and Roberto Perli (2003), "Profits and Balance Sheet Developments at U.S. Commercial Banks in 2002," *Federal Reserve Bulletin*, vol. 89 (June), p. 255.

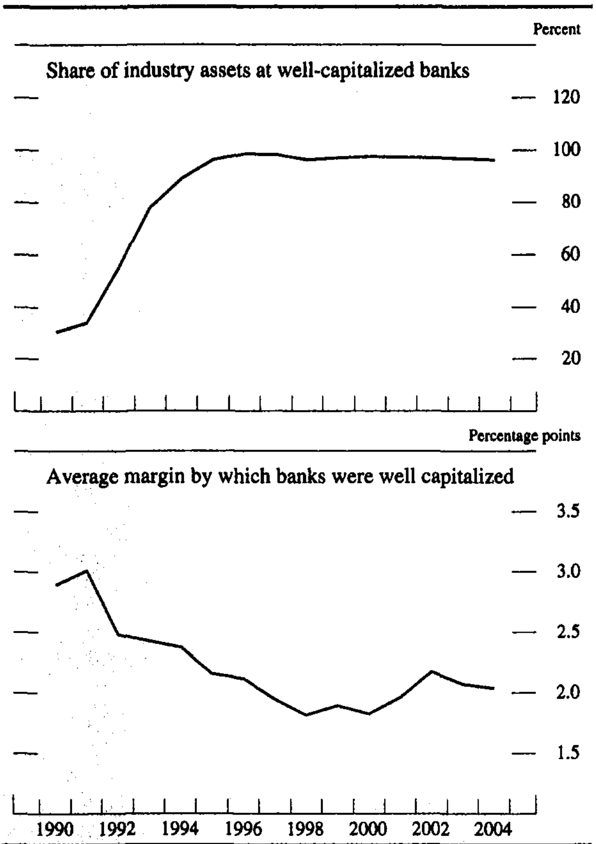
10. Tier 1 and tier 2 capital are regulatory measures. Tier 1 capital consists primarily of common equity (excluding intangible assets such as goodwill and excluding net unrealized gains on investment account securities classified as available for sale) and certain perpetual preferred stock. Tier 2 capital consists primarily of subordinated debt, preferred stock not included in tier 1 capital, and loan-loss reserves. Risk-weighted assets are calculated by multiplying the amount of assets and the credit-equivalent amount of off-balance-sheet items (an estimate of the potential credit exposure posed by the item) by the risk weight for each category. The risk weights rise from 0 to 1 as the credit risk of the assets increases.

12. Regulatory capital ratios, 1990–2004



NOTE. The data are as of year-end. For the components of the ratios, see text note 10.

13. Assets and regulatory capital at well-capitalized banks, 1990–2004



NOTE. The data are annual. For the definitions of "well capitalized" and of the margin by which banks remain well capitalized, see text notes 11 and 12.

held by banks that were considered well capitalized for regulatory purposes remained largely unchanged from the very high level of 2003 at about 96 percent (chart 13).[11] The estimated average margin by which banks exceeded the well-capitalized standard declined slightly in 2004 (chart 13).[12]

Derivatives

The market for innovative financial products has continued to expand. Banks have increased their off-balance-sheet derivatives positions over the past decade, and this trend continued last year. At the end of 2004, the notional value of all derivatives contracts held by banks was more than $88 trillion, up about $19 trillion from the end of 2003. The ten largest banks held the lion's share of these contracts, which increased to 98 percent in 2004. The largest proportion of notional value for these contracts continues to be in interest rate derivatives. Investors use these contracts, in part, to hedge interest rate risk. The continued growth in holdings of mortgages and mortgage-backed securities—instruments whose prices are particularly sensitive to interest rates—likely contributed to an increase in hedging activity by banks' customers in interest rate derivatives markets. As intermediaries in such instruments, banks would therefore see their holdings rise.

Credit derivatives are agreements in which default risks associated with a given borrower are transferred from a beneficiary to a protection provider. The market for credit derivatives continues to develop, and banks' holdings of credit derivatives surged in 2004, increasing at a rate not seen since the beginnings of the market for them, around 1998. Notional holdings still remain small, however, relative to those of some other types of derivatives (see box "Credit Derivatives").

The notional value of banks' holdings of foreign exchange contracts, equity derivatives, and commodity and other contracts—which constitute the remainder of banks' derivatives portfolios—advanced strongly in 2004. Foreign exchange contracts increased 21.0 percent, and equity and commodity contracts combined moved up 33.9 percent.

The notional value of derivatives contracts is one measure of overall market activity; another measure, the fair value of these contracts—which measures the value of all contracts if settled at the reporting date—is substantially smaller. Moreover, banks' derivatives positions tend to be offsetting because of their activity as dealers. At the end of 2004, the gross positive fair value of banks' derivatives contracts totaled about $1.33 trillion and exceeded the negative fair value by $26 billion, up from $23 billion in 2003. Banks have had a positive net fair value in these contracts for the past five years.

The tier 1 ratio is the ratio of tier 1 capital to risk-weighted assets; the total ratio is the ratio of tier 1 plus tier 2 capital to risk-weighted assets. The leverage ratio is the ratio of tier 1 capital to tangible assets.Tangible assets are equal to total assets less assets excluded from common equity in the calculation of tier 1 capital.

11. Well-capitalized banks are those with a total capital ratio greater than 10 percent, a tier 1 ratio greater than 6 percent, a leverage ratio greater than 5 percent, and a composite CAMELS rating of 1 or 2. Each letter in CAMELS stands for a key element of bank financial condition—Capital adequacy, Asset quality, Management, Earnings, Liquidity, and Sensitivity to market risks.

12. The estimated average margin by which banks exceeded standards for being well capitalized was computed as follows: Among the leverage, tier 1, and total capital ratios of each well-capitalized bank, the institution's "tightest" capital ratio is defined as the one closest to the regulatory standard for being well capitalized. The bank's margin is then defined as the percentage point difference between its tightest capital ratio and the corresponding regulatory standard. The average margin among all well-capitalized banks is the weighted average of all the individual margins, and the weights are each bank's share of the total assets of well-capitalized banks.

Credit Derivatives

Credit derivatives are over-the-counter agreements in which the risk of credit loss of a reference entity is transferred from one party (the beneficiary) to another (the protection provider). The Bank for International Settlements estimates that the total notional amount of credit derivatives outstanding worldwide was about $4.6 trillion in June 2004.[1] According to surveys of market participants conducted last year by the British Bankers' Association and Fitch Ratings, banks held the largest share of credit derivatives at the end of 2003. Securities firms, insurance companies, and hedge funds were also active participants in the market. Banks and securities firms were active on both sides of the market, while insurance companies were mostly sellers of protection. Hedge funds have been active as protection buyers for some time, but recently they became major players as protection sellers, too.[2]

The Fitch survey reveals that about two-thirds of all credit derivatives held at the end of 2003 by U.S. and Canadian banks and broker–dealers were credit default swaps (CDS) referenced to an individual entity. Those contracts generally allow the beneficiary to deliver to the protection provider an obligation of the reference entity upon default of the latter and receive its par value in exchange. Portfolio CDS products, such as traded indexes of CDS, baskets of CDS, and synthetic collateralized debt obligations (CDOs) accounted for a further 25 percent of all credit derivatives.[3] Some portfolio products are popular because they allow investors to trade credit risk on a potentially large number of reference entities in just one transaction; others are popular because their value is sensitive to default correlation risk and thus can be used as a hedge against the tendency of different reference entities to default at the same time.

In recent years the total notional amount of credit derivatives held by U.S. commercial banks has expanded very rapidly. According to regulatory reports, it exceeded $2.3 trillion at the end of 2004—more than double the total at the end of 2003—and more than 99 percent of the 2004 total was held at the ten largest institutions. Banks were beneficiaries on more than $1.2 trillion of the 2004 notional amount, and they were protection providers on about $1.1 trillion (chart A). On net, therefore, banks were recipients of credit protection, as they typically have been in the past, and only a handful of banks were net protection providers. As the credit quality of U.S. firms improved and credit spreads declined in 2004, the market value of credit derivatives contracts for which banks were the protection provider more than doubled, to about $15.5 billion. Conversely, the market value of contracts for which banks were the beneficiary declined a similar amount, and those positions showed a loss of about $15 billion at year-end (chart B). The aggregate net fair value of all credit deriva-

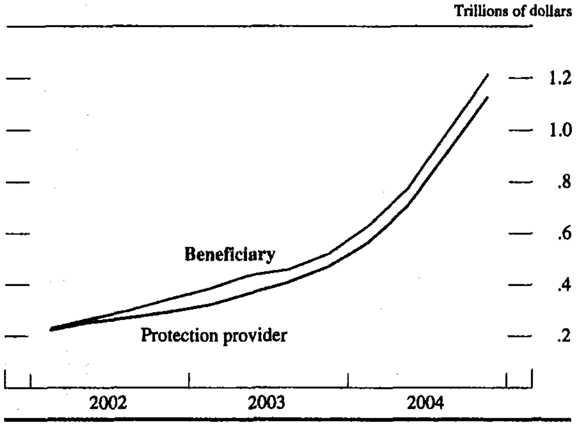
NOTE. Roberto Perli, of the Division of Monetary Affairs, prepared this material.

1. See Bank for International Settlements, "Triennial Central Bank Survey: Foreign Exchange and Derivatives Market Activity in 2004, available at www.bis.org.

2. See the British Bankers' Association, "Credit Derivatives Report 2003/2004," available at www.bba.org.uk; and Fitch Ratings, "Global Credit Derivatives Survey," Special Report, September 7, 2004, available at www.fitchratings.com.

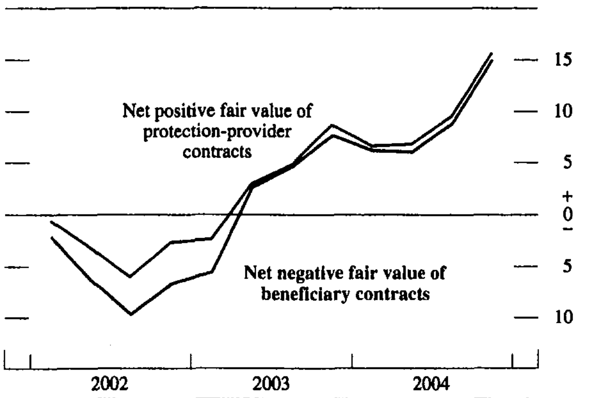
3. A CDS basket is a contract that is referenced to more than one entity. Typically, the buyer of protection has the right to deliver a defaulted bond and receive par in exchange upon the default of any of the entities referenced in the basket. Such contracts are called "first-to-default baskets." Investors can also trade "nth-to-default baskets," whereby they can deliver a bond for par upon the nth default among the reference entities. Synthetic CDOs are contracts that transfer credit risk on portfolios of CDS on a large number of reference entities.

A. Notional amounts of credit derivatives for which banks were beneficiaries or protection providers, 2002–04



NOTE. The data are quarterly.

B. Net fair value of credit derivatives contracts in which banks were beneficiaries or protection providers, 2002–04



NOTE. The data are quarterly. The net positive fair value on protection-provider contracts is computed as the difference between the gross fair value of such contracts with positive fair values and the gross fair value of such contracts with negative fair values. The net negative fair value of beneficiary contracts is computed similarly.

Credit Derivatives—Continued

tives contracts on banks' books was thus only about $500 million, down from a little more than $900 million a year earlier.

As with most other types of derivatives contracts, banks enter into credit derivatives both in their role as dealers and for their own account. The large notional amount of credit derivatives held on banks' books, combined with the small net market value of those contracts, is consistent with banks having a substantial dealer role. Indeed, banks that are engaged in that type of activity would generally aim at keeping a balanced book by entering into at least partially offsetting contracts with a variety of counterparties.

Banks may choose to enter into credit derivative contracts for their own account for a number of reasons. First, banks that wish to reduce their exposure to credit risk may find it less costly to buy protection in the CDS market than to reduce the size of their loan or bond portfolios. Buying such protection, unlike securitizing or selling loans in the secondary market, has the added advantage of enabling banks to retain and service the loans and thus avoid compromising their relationships with clients.[4] About three-fourths of the global banks that responded to the Fitch survey stated that they use credit derivatives to some extent for credit risk management purposes, although less than one-fifth mentioned it as a dominant reason for their involvement in the market.

Second, credit derivatives can be viewed as an alternative asset class, and banks seeking to gain exposure to corporate credit risk or further diversify their existing credit portfolios can sell protection in the single-name or portfolio CDS market as an alternative to buying corporate bonds or extending C&I loans. About 70 percent of global banks do so, according to Fitch, but again only a minority of those said this was their main reason for participating in the market.

A third important reason that banks may want to enter into credit derivatives contracts, mentioned by about half the global banks surveyed by Fitch, is regulatory capital management. Under the 1988 Basel Capital Accord, which determines the amount of regulatory capital that banks are required to hold against their credit exposures, loans to corporations carry a risk-based capital charge of 8 percent, which is largely independent of the credit quality of the borrower. For loans to highly rated corporations, this capital charge likely exceeds the amount of economic capital that a prudent bank would choose to hold against the credit exposure. Although credit derivatives are not covered by the 1988 accord, national bank regulators have treated them in a way that is consistent with the spirit of the accord. If a bank holds a loan on which it has purchased protection in the credit derivatives market from another bank, its only exposure, from a regulatory as well as an economic perspective, is to the counterparty bank. Since, under the 1988 accord, exposures to OECD banks (that is, banks regulated by a member country of the Organization for Economic Co-operation and Development) carry only a 1.6 percent capital charge, credit protection purchased from those banks allows banks to reduce considerably the capital they are required to hold against corporate loans and at the same time retain those loans on their balance sheets. The return earned on such loans, however, net of the cost paid for protection, is far below the loan rate. When implemented, the New Basel Capital Accord, or Basel II, will likely reduce the incentive to use credit derivatives for regulatory capital management of this sort because it provides for risk-based capital charges that are more closely matched with true economic risk.

4. In their responses to a special question in the Federal Reserve Board's January 2003 Senior Loan Officer Opinion Survey on Bank Lending Practices, most banks indicated that purchasing a CDS is superior to selling a loan because it preserves the bank's relationship with the borrower.

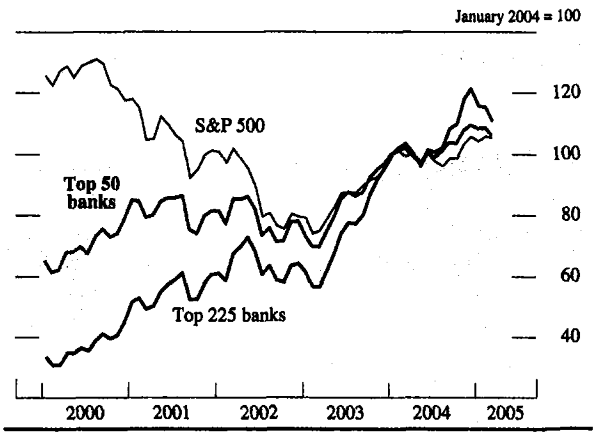
Trends in Profitability

The banking industry continued to be very profitable in 2004.[13] Although return on assets (ROA) and return on equity (ROE) were both slightly below the previous year's levels, they remained well within the high range prevailing since the mid-1990s. ROA, at 1.34 percent, was only 5 basis points below the previous year's record. ROE, which was damped by merger-related increases in reported equity, declined more than 1 percentage point but was still a healthy 14.23 percent. The fraction of banks with negative net income shrank for the third consecutive year, to 5.8 percent, and accounted for less than 1 percent of industry assets.

The slight weakening in profitability occurred mainly at the 100 largest banks. The net interest margin declined a bit further at these banks, likely in part because of additional flattening of the yield curve; a possible further contributor was an intensification of competitive pressure in the C&I loan market. Gains in non-interest income were outpaced by a rise in non-interest expense. Income from fiduciary and securitization activities rose, but income from investment banking was essentially flat, gains from sales of loans fell, and trading revenue contracted sharply. An increase in nonrecurring charges—

13. The adjustments to the data to take account of mergers and the effects of push-down accounting were relatively large for 2004.

14. Bank stock prices, by market value of bank, and the S&P 500, 2000–05

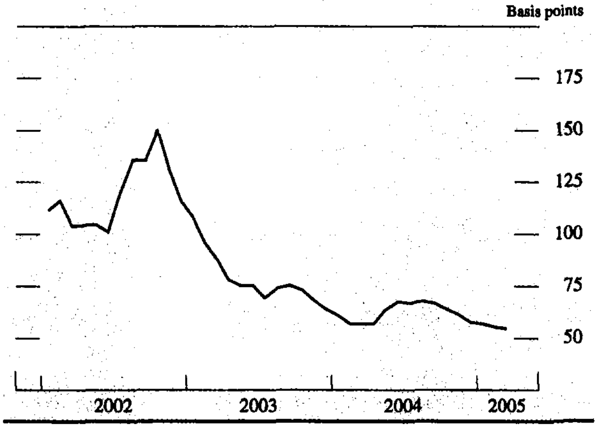


NOTE. The data are monthly and extend through March 2005. Stock prices are weighted by market value.
SOURCE. Standard & Poor's and *American Banker.*

including merger-related expenses and litigation provisions at a few of the largest banks—contributed to the rise in non-interest expense.

Partially compensating for these developments was the continued improvement in overall credit quality. This trend, which has been driven by the strengthening of household and business balance sheets and the ongoing economic expansion, has allowed banks to further reduce their provisions for loan and lease losses. Realized gains on investment account securities, even though not as strong as in 2003, continued to boost income. Unrealized gains on available-for-sale securities declined somewhat; in part, the drop probably reflected adjustments to securities portfolios resulting from the repositioning of interest rate risk, changes in market interest rates, and the realization of past gains through the sale of securities.

15. Average spread of rates on subordinated debt at selected bank holding companies, 2002–05



NOTE. The data are monthly and extend through March 2005. Spreads are over comparable-maturity Treasury securities.
SOURCE. Merrill Lynch bond data.

Despite substantial earnings, banks—particularly the top ten—trimmed the share of profits paid out as dividends. As a result, retained earnings almost doubled as a share of net income and boosted equity capital. Industry equity was also augmented considerably by the revaluation of assets and liabilities that resulted from some large merger transactions, which in turn were accompanied by sizable increases in goodwill. Supported by solid profitability, bank holding company stocks again outperformed the S&P 500 during 2004 (chart 14). The spread of rates on subordinated debt over rates on comparable-maturity Treasury securities remained at very low levels in 2004 (chart 15).

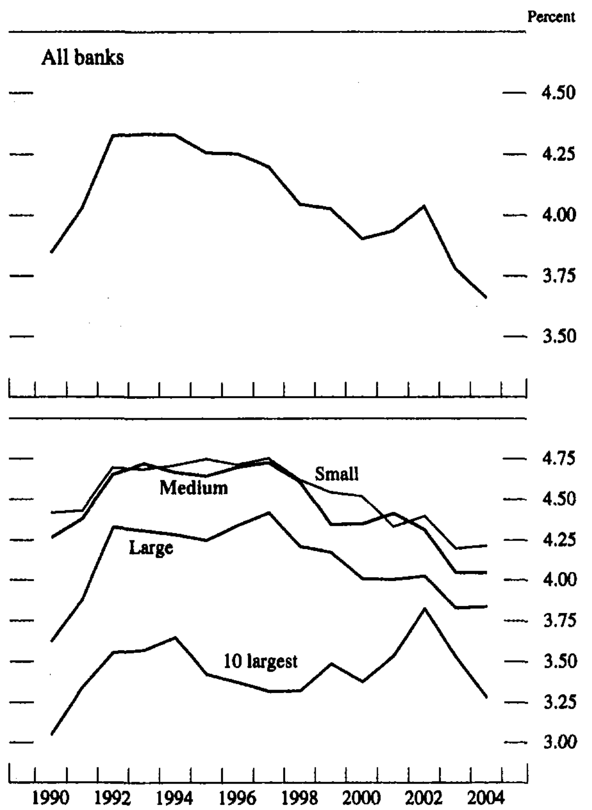
Interest Income and Expense

Despite an increase in short-term market interest rates following the onset of monetary policy tightening in June of last year, the average rate paid on banks' liabilities and earned on banks' assets for 2004 as a whole moved lower. As the average rate earned declined more than the average rate paid, the industry's net interest margin narrowed for the second consecutive year, falling 12 basis points, to 3.66 percent (chart 16). Much of the narrowing came in the first half of 2004, however, and the net interest margin changed little over the second half of the year despite a considerable flattening of the yield curve.[14]

The further narrowing of the net interest margin is also consistent with a reported increase of competitive pressure in the C&I loan market, which appears to have led some banks to trim spreads of loan rates over reference rates despite a pickup in loan demand (chart 17). In the October 2004 BLPS, banks were asked about the increase in competition in the C&I loan market. Respondents that had experienced greater competition during the year reported that the largest increase came from other U.S. commercial banks and that the second-largest increase, especially for the largest commercial banks, came from investment banks. About half of the respondents felt that the persistence of this shift in competition was not well established, but the majority of banks expressing an opinion indicated that the increase reflected a permanent change in the structure of the C&I loan market. In the January 2005 BLPS, banks

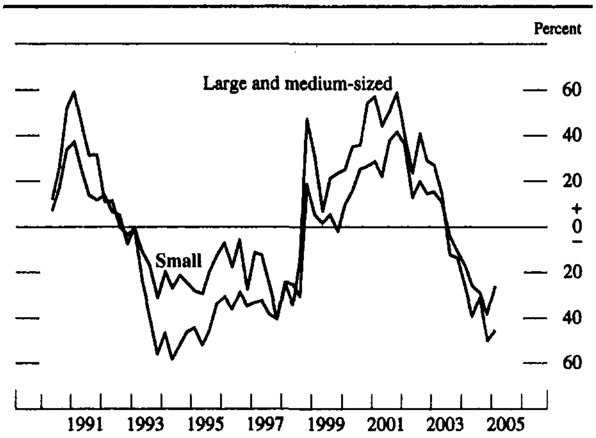
14. For a discussion of the effects of market interest rates on the net interest margin, see Carlson and Perli (2004), "Profits and Balance Sheet Developments," p. 173.

16. Net interest margin, by size of bank, 1990–2004



NOTE. The data are annual. Net interest margin is net interest income divided by average interest-earning assets. For definition of bank size, see the general note on the first page of the main text.

17. Net percentage of selected domestic banks increasing spread of rates on C&I loans over cost of funds, by size of borrower, 1990–2005



NOTE. See general note and source note to chart 5.

were asked why nonbank lenders had become more aggressive competitors. Respondents pointed to the senior status of loans in bankruptcy and restructuring proceedings, increased liquidity in the secondary market, and a trend toward market-based pricing.

The fall in the banking sector's net interest margin was driven by a decline of 25 basis points at the ten largest banks. These institutions rely on managed liabilities for their funding more than other banks do.[15] Because rates paid on these liabilities are more sensitive to changes in market interest rates than are rates paid on core deposits, the net interest margin at the ten largest banks was more adversely affected than that at other banks by the increase in short-term interest rates during 2004. The net interest margin at the ten largest banks was also eroded by continued runoffs of their C&I loans: Despite a pickup in business lending in the second half of the year, the share of interest-earning assets attributable to such loans fell from 15.9 percent to 12.6 percent over the year at the ten largest banks. The large drop was only partially offset by a shift toward higher-yielding loans, such as credit card loans. The ten largest banks also increased their share of interest-earning assets that consisted of investment-account securities (including mortgage-backed securities); because rates of return on securities are generally lower than those on loans (in particular, C&I loans), this shift contributed to the narrowing of the net interest margin.

At large banks, the average rate earned on assets was essentially unchanged, and the average rate paid on liabilities ticked down relative to 2003. As a result, the net interest margin for such banks was little changed. Large banks did not experience runoffs of C&I loans, and they benefited from an increase in the share of credit card loans, the yields on which are higher than those on other loans and were higher in 2004 than in 2003. In addition, these institutions boosted the share of interest-earning assets that consisted of relatively high-yielding real estate loans by 1.7 percentage points, to 36.5 percent; the increase was equally distributed between residential and commercial real estate loans.

As with large banks, the net interest margin was little changed at medium-sized and small banks; the decline in the average rate paid on liabilities was about in line with the fall in the average rate earned on assets. Relative to larger banks, medium-sized and small banks benefited from their greater reliance on core deposits, whose rates adjust slowly to changes in market rates. In addition, these banks further increased the share of commercial real estate loans in their portfolios. Investing in these assets, which appear to have relatively higher yields than residen-

15. At the ten largest banks, the share of interest-bearing liabilities that consisted of managed liabilities was about 58 percent in 2004, compared with a share of 53 percent at large banks, 36 percent at medium-sized banks, and 26 percent at small banks.

tial real estate loans, allowed them to limit the decline in the overall rate of return on their assets.[16]

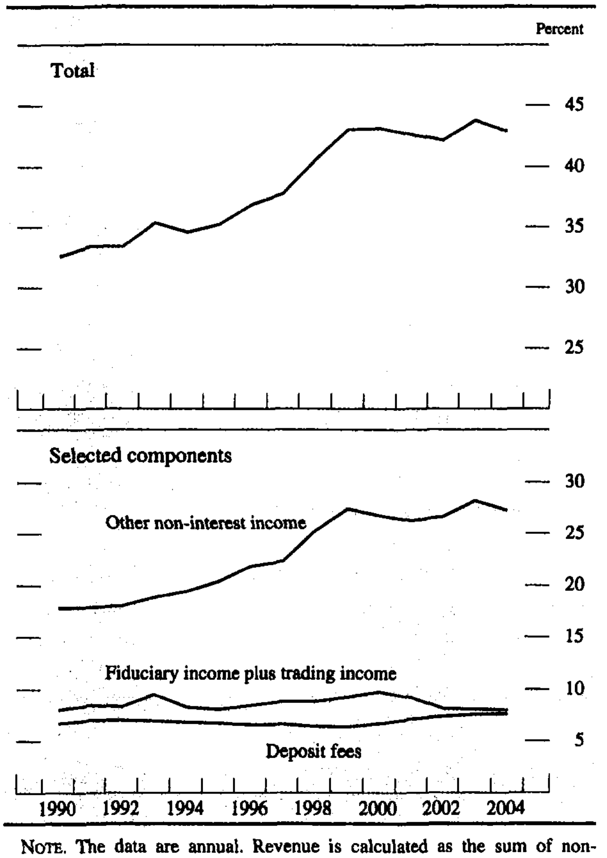
Non-interest Income and Expense

Non-interest income grew 2.6 percent in 2004, a notable slowing from the previous year's 8.9 percent rise. An 11 percent increase at the ten largest banks was partially offset by an almost 4 percent contraction at large banks and by smaller declines at medium-sized and small banks. As a share of total revenue (chart 18, top panel), non-interest income edged down but remained within the range maintained over the past few years following the strong uptrend of the 1980s (not shown) and 1990s. Deposit fees continued to grow about in line with total revenue (chart 18, bottom panel), although the ratio of fees to deposits moved down for the second consecutive year (chart 19). A 12 percent rise in fiduciary income was likely attributable, in part, to gains in equity prices, which pushed up the value of assets held in bank trusts. Trading revenue contracted 13 percent, however, as income from interest rate exposures dropped sharply at the 100 largest banks. Growth in the "other" component of non-interest income declined more than 9 percentage points, to 1.6 percent. Revenue from investment banking activities was almost flat, and gains from sales of loans fell sharply across the industry, probably in part because of reduced mortgage originations. Positive contributions included an 11.5 percent rise in loan servicing fees as well as an increase in securitization income. The remaining component of other non-interest income—which includes, among other things, safe deposit box rent, rent and other income from other real estate owned, and income and fees from automated teller machines—increased about 4 percent.

The rate of growth of non-interest expense increased almost 3 percentage points, to 8.3 percent, in 2004, lifting the ratio of non-interest expense to total revenue roughly 2 percentage points, to 60 percent (chart 20). The cost of premises and fixed assets as a share of revenue was essentially unchanged, and the number of branches continued to grow at a modest pace. Salary and benefit expenses grew 6.3 percent, a slightly slower rate than in 2003, and their ratio to total revenue edged up only a few basis points. The number of bank employees expanded roughly 3 percent, a touch higher than in 2003, but

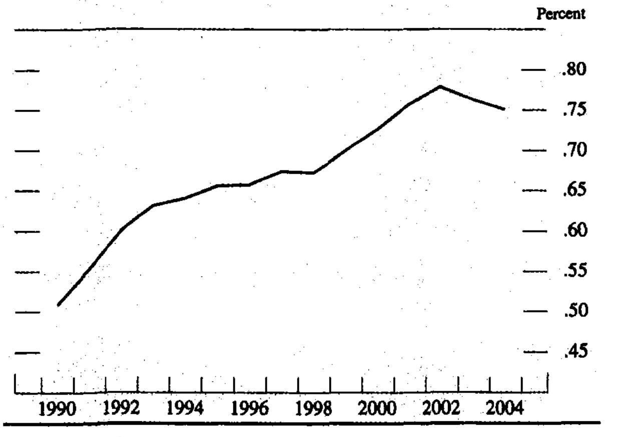
16. Yields on residential and commercial real estate loans are not available separately from the Call Report; only income data for the broader "real estate loan" category are available. To investigate the relationship between the concentration of commercial real estate loans in banks' real estate portfolios and the yield on real estate loans, we ran a cross-sectional regression of the latter on the share of real estate loans that are backed by commercial real estate. We found that the coefficient is both positive and statistically significant for small and medium-sized banks.

18. Non-interest income and selected components as a proportion of revenue, 1990–2004



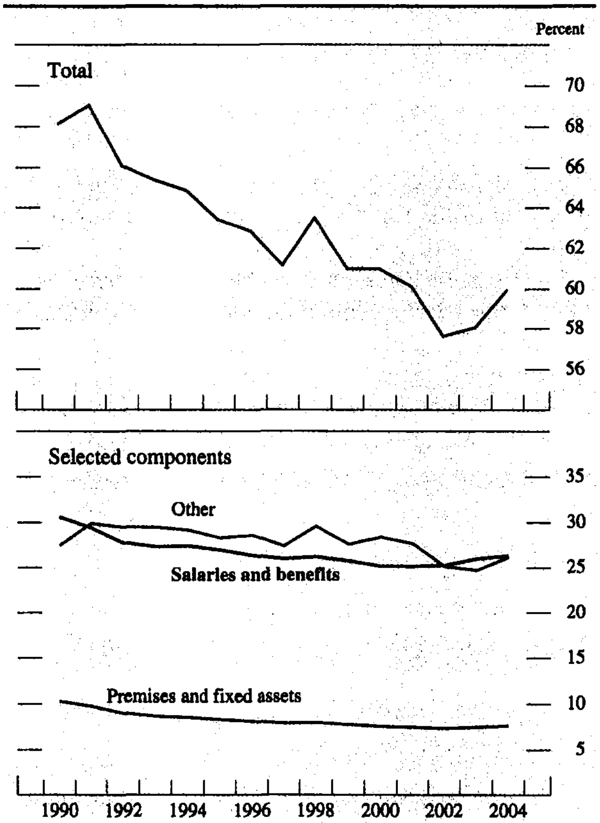
NOTE. The data are annual. Revenue is calculated as the sum of non-interest income and net interest income.

19. Deposit fee income as a proportion of total domestic deposits, 1990–2004



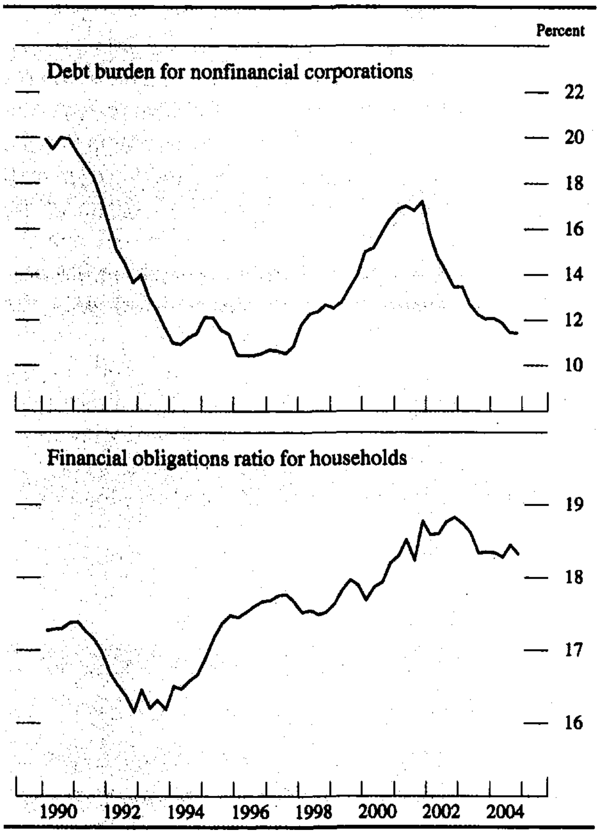
NOTE. The data are annual.

20. Non-interest expense and selected components as a proportion of revenue, 1990–2004



NOTE. The data are annual.

21. Debt burden for businesses and financial obligations ratio for households, 1990–2004



NOTE. The data are quarterly. The debt burden is calculated as interest payments as a percentage of cash flow. The financial obligations ratio is an estimate of debt payments and recurring obligations as a percentage of disposable personal income; debt payments and recurring obligations consist of required payments on outstanding mortgage and consumer debt, as well as rent, auto leases, and property taxes.

SOURCE. For debt burden, national income and product accounts and the Federal Reserve Board; for financial obligations ratio, Federal Reserve Board (www.federalreserve.gov/releases/housedebt).

the growth of salaries and benefits per employee, which was about 6 percent in 2003, decelerated to 3.3 percent last year, and was about flat at the ten largest banks.

The moderation in the growth of salaries and benefits was more than offset by a brisk rise in other non-interest expense, which increased about 1.5 percentage points as a share of total revenue, to 26.2 percent. An increase in nonrecurring charges—including merger-related expenses and litigation provisions related to settlements of alleged failures of corporate governance and conflicts of interest—contributed to the rise in other non-interest expense. Non-interest expense also was reportedly boosted somewhat by increased costs for regulatory compliance as banks responded to the Bank Secrecy Act, the USA Patriot Act, and the Sarbanes–Oxley Act.

Loan Performance and Loss Provisioning

The ongoing economic expansion and a further strengthening of household and business balance sheets contributed to the continued improvement of credit quality in 2004 and allowed banks to reduce their provisions for loan and lease losses. The debt-service burden of businesses continued to decline, while the financial obligations ratio of households, although still high, was below the peak reached at the end of 2002 (chart 21). Presumably reflecting these developments, delinquency rates for all major loan categories moved down, with that for C&I loans posting the largest decline. Delinquency rates on both residential and commercial real estate loans moved down further. Net charge-off rates for nearly all types of loans fell, and those for real estate loans dropped to historically low levels. Nonetheless, total net charge-offs surpassed provisioning, and so total reserves for loan and lease losses fell last year. But with asset quality improving, the ratio of reserves to net charge-offs and to delinquent loans both rose.

C&I Loans

The delinquency rate on C&I loans continued to decline during 2004; by the end of the year, it had fallen 1 percentage point, to 1.9 percent, the lowest level since the first quarter of 1999 (chart 22). The decline was driven primarily by developments at the 100 largest banks, as the substantial increase in such delinquencies at those entities in the aftermath of the 2001 economic slowdown receded. The net charge-off rate on these loans fell sharply, reaching 0.3 percent in the fourth quarter, the lowest level since the first quarter of 1998. As with delinquency rates, the improvement occurred mostly at the 100 largest banks.

Banks were asked in the October 2004 BLPS about their outlook for C&I loan quality over the next year. The majority of respondents indicated that loan quality was likely to stabilize around current levels if economic activity progressed in line with consensus forecasts, while the remaining banks, on net, expected credit quality to continue to improve.

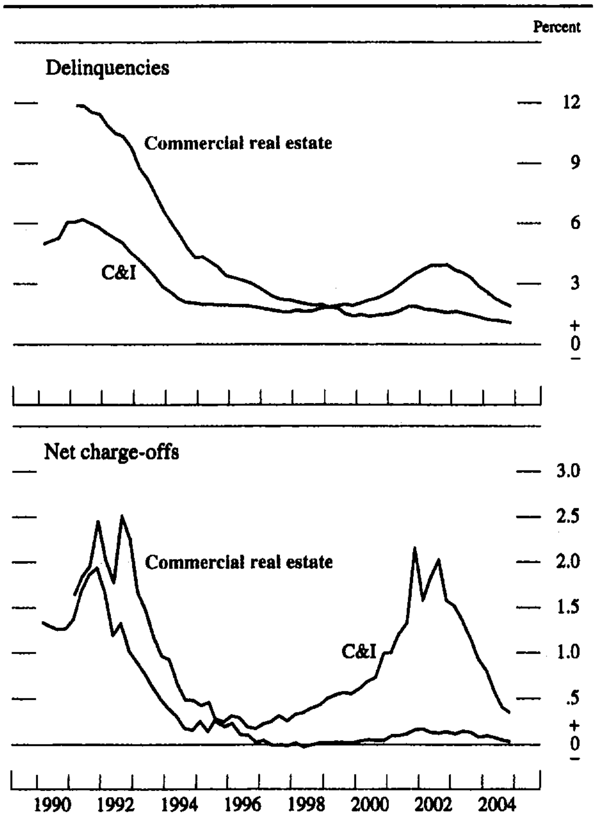
Commercial Real Estate Loans

The credit quality of commercial real estate loans improved further in 2004, even though rents on office buildings continued to contract (albeit at a slower pace). Vacancy rates in the office sector declined in 2004, although they remained elevated, and vacancy rates on retail properties remained relatively low. The delinquency rate on these loans fell 29 basis points, to 1.1 percent last year (chart 22). The net charge-off rate on such loans moved down during 2004 and, by year-end, was near zero across the banking industry.

Loans to Households

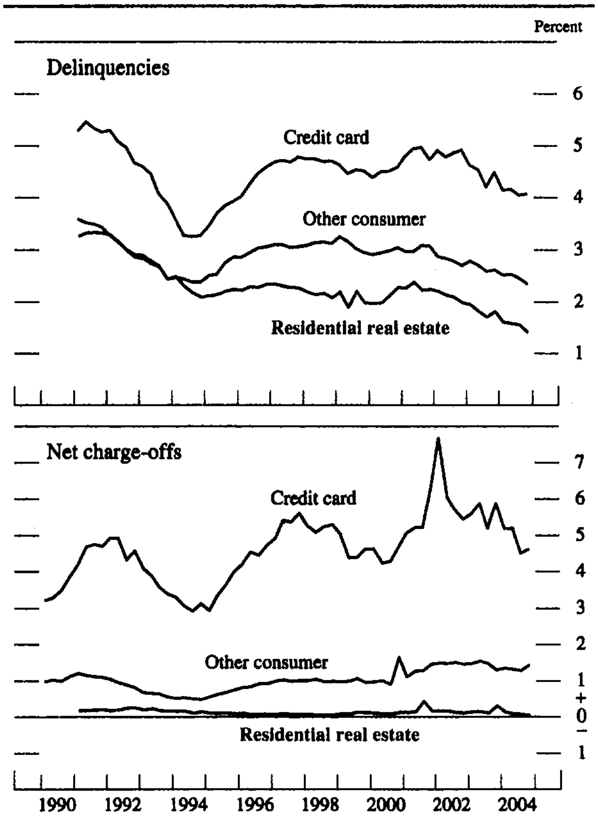
The credit quality of loans to households continued to improve last year. The delinquency rate on residen-

22. Delinquency and charge-off rates for loans to businesses, by type of loan, 1990–2004



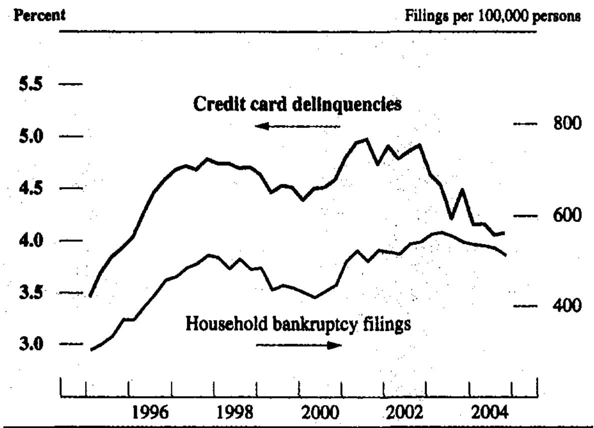
NOTE. The data are quarterly and seasonally adjusted; the data for commercial real estate begin in 1991. Delinquent loans are loans that are not accruing interest and those that are accruing interest but are more than thirty days past due. The delinquency rate is the end-of-period level of delinquent loans divided by the end-of-period level of outstanding loans. The net charge-off rate is the annualized amount of charge-offs over the period, net of recoveries, divided by the average level of outstanding loans over the period. For the computation of these rates, commercial real estate loans exclude loans not secured by real estate (see table 1, note 2).

23. Delinquency and charge-off rates for loans to households, by type of loan, 1990–2004



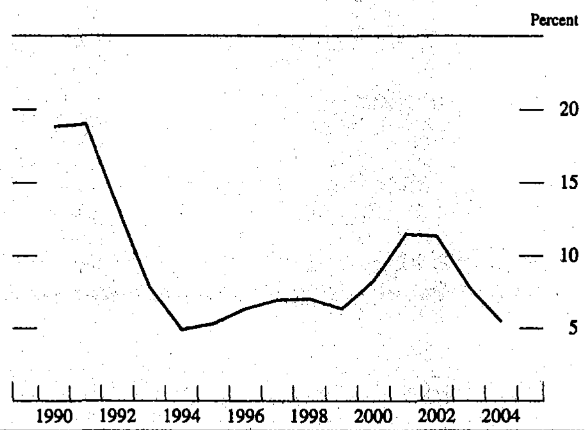
NOTE. Data for delinquencies and for net charge-offs of residential real estate loans begin in 1991. For definitions of delinquencies and net charge-offs, see note to chart 22.

24. Credit card delinquency rate and household bankruptcy filings, 1995–2004



NOTE. The data are quarterly and seasonally adjusted. For definition of delinquencies, see note to chart 22.
SOURCE. Call Report and Visa Bankruptcy Notification Service.

25. Provisions for loan and lease losses as a proportion of total revenue, 1990–2004



NOTE. The data are annual.

tial real estate loans fell 39 basis points, to 1.4 percent, the lowest level since the beginning of the 1990s (chart 23). The improvement was presumably aided in part by the lower loan costs afforded by continued, although slowing, mortgage refinancing. Net charge-off rates on residential real estate loans averaged 10 basis points for the year, and remained in the range that had prevailed over the past several years. Losses were probably restrained in part by rising house prices, which boosted borrowers' equity stakes in their homes and made foreclosures less costly for banks.

Tracking a decline in the household bankruptcy rate, the delinquency rate on credit card loans fell about 40 basis points, to 4.1 percent, in the fourth quarter of last year, the lowest level since the first quarter of 1996 (charts 23 and 24). The delinquency rate on other consumer loans fell as well, to 2.3 percent, in the fourth quarter (chart 23). On average in 2004, charge-off rates on credit card loans were down 75 basis points, to almost 5 percent, while charge-off rates on other consumer loans were essentially unchanged.

Securitized Loans

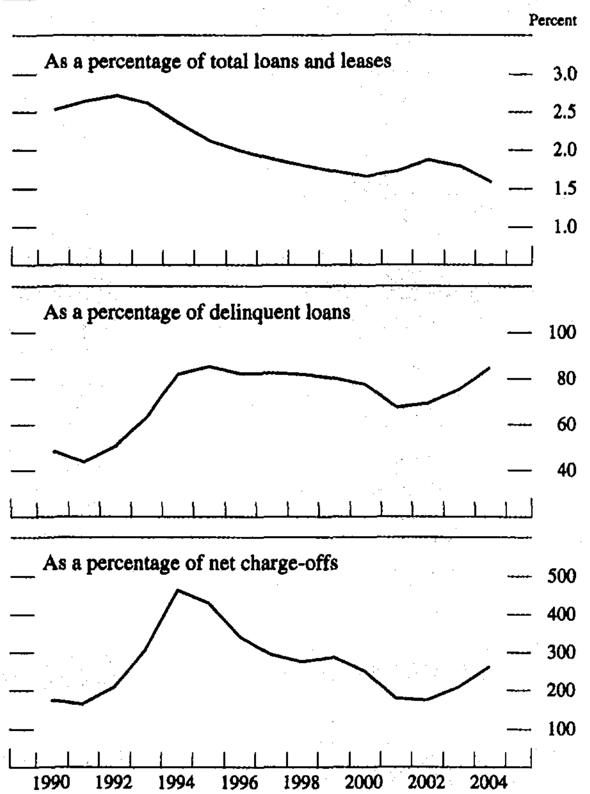
A decline in the delinquency rates on securitized loans on which banks retained servicing rights or provided credit enhancements—a large majority of these loans are to households—also pointed to an improvement in credit quality. The delinquency rate on securitized credit card receivables was 3.9 percent in the fourth quarter of 2004, down more than 70 basis points from the previous year and below the delinquency rate on loans held on banks' books. Despite an uptick in the fourth quarter, the delinquency rate on securitized residential real estate loans averaged 4 percent in 2004, about 50 basis points less than in 2003. The delinquency rate on securitized auto loans averaged 1 percent, about 40 basis points below the average rate in 2003.

Loss Provisioning

With the further improvement in overall credit quality in 2004, banks in all size classes continued to reduce provisions for loan and lease losses. The biggest reduction was at the ten largest banks, and a few of those institutions posted negative provisions for one or more quarters in 2004. The ratio of provisions for loan and lease losses to total revenue fell to the lowest level since the mid-1990s (chart 25), and the ratio of provisions to loans moved down for the third consecutive year.

Net charge-offs exceeded provisioning in 2004, so reserves for loan and lease losses declined roughly 4 percent, and the ratio of such reserves to loans fell to 1.6 percent, the lowest level since the beginning of the 1990s (chart 26). Nonetheless, with the continued improvement in credit quality, the ratio of reserves to delinquent loans moved up about 10 percentage points, to 85 percent, the top end of its recent range. Reserves rose noticeably as a share of net charge-offs as well, surpassing the level that prevailed before the economic slowdown.

26. Reserves for loan and lease losses, 1990–2004



NOTE. The data are annual. For definitions of delinquencies and net charge-offs, see note to chart 22.

INTERNATIONAL OPERATIONS OF U.S. COMMERCIAL BANKS

The share of bank assets booked in foreign offices increased about 40 basis points, to 11.4 percent, in 2004. The dollar volume of exposure to selected East Asian countries about doubled, mostly because of the acquisition of a Korean bank by a large U.S. commercial bank (table 2, memo item). Exposure to eastern Europe expanded briskly, while exposure to India grew a bit less than in the previous year. A rise in exposure to Latin American countries after two years of contraction was mostly attributable to rising exposure to Brazil. As a share of tier 1 capital, exposure to selected East Asian countries surged, while exposure to Latin America fell a bit.

The share of net income due to foreign operations rose almost 1 percentage point, to 7.9 percent (data not shown in table), but it continued to be well below the levels reached in the mid-1990s. As was the case domestically, lower provisioning for loan and lease losses was an important contributor to the gain in earnings from foreign operations.

RECENT DEVELOPMENTS

In the first few months of 2005, output grew at a moderate pace, and labor market conditions continued to improve gradually. Although oil prices and overall inflation pressures picked up during the first quarter, longer-term inflationary expectations remained well contained. Against this backdrop, the Federal Open Market Committee decided to raise its target for the federal funds rate 25 basis points at each of its first two meetings in 2005. Longer-term interest rates rose appreciably—the ten-year Treasury rate rose 24 basis points in the first quarter, and the rate on thirty-year fixed-rate mortgages rose 16 basis points.

Data from the Federal Reserve's H.8 statistical release indicate that the growth of bank credit accelerated to a double-digit pace in the first three months of 2005 and that C&I lending and revolving home equity loans were particularly strong. Securities holdings also expanded rapidly, as domestically chartered banks continued to accumulate mortgage-backed securities in investment accounts.

Core deposits were about flat, on balance, in early 2005. As a consequence, banks continued to ramp up large time deposits and other liabilities at a brisk rate.

Profitability at large bank holding companies generally remained robust in the first quarter of 2005. Profits were boosted by hefty revenues from trading and mortgage servicing, while additional gains in asset quality allowed these institutions to reduce further their loan loss reserves. On the other hand, many institutions reported tighter net interest margins, and increased competition in the credit card market further squeezed profits for some issuers. Nonrecurring expenses also damped profitability in some cases.

Despite banks' strong balance sheets and robust profitability in recent quarters, bank stock prices declined in the first quarter of 2005; the *American Banker* stock index of the 225 banks with the highest market value underperformed the S&P 500 stock index by almost 11 percent. In large part, the weakness in bank stocks likely reflected investor concerns about future profitability because of rising interest rates and a consequent slowing in the pace of the expansion. In contrast to 2004, merger activity was relatively quiet in the first part of 2005.

2. Exposure of banks to selected economies at year-end relative to tier 1 capital, by bank size, 1998–2004

Percent

Bank and year	Selected Asian countries[1]	India	Eastern Europe and Russia		Latin America				Total
			All	Russia	All	Mexico	Argentina	Brazil	
All									
1998	15.49	2.35	3.49	.43	42.93	9.88	9.66	11.27	64.26
1999	14.37	2.39	2.85	.37	39.00	9.50	9.40	10.49	58.61
2000	13.17	2.63	4.35	.49	37.88	9.08	8.41	11.15	58.03
2001	12.09	2.55	4.29	.60	54.06	25.97	6.61	2.99	72.99
2002	11.44	2.74	5.53	1.06	38.90	20.80	2.44	8.36	58.61
2003	11.15	3.86	5.44	1.48	32.85	17.95	1.73	6.77	53.30
2004	20.33	4.16	6.09	1.54	31.78	16.65	1.47	6.51	62.36
Money center and other large banks									
1998	24.02	4.19	5.61	.68	64.20	14.10	15.19	17.04	98.02
1999	20.73	3.56	4.25	.55	53.90	12.62	13.63	14.53	82.44
2000	19.98	4.14	6.83	.77	54.98	12.69	12.68	16.40	85.93
2001	17.88	3.86	6.47	.91	79.08	34.54	9.79	18.74	107.29
2002	16.96	4.18	8.17	1.63	57.32	31.14	3.65	12.38	86.63
2003	16.98	5.93	8.41	2.29	49.19	27.13	2.64	10.02	80.51
2004	30.95	6.31	9.34	2.36	46.96	24.99	2.22	9.59	93.56
Other banks									
1998	2.08	.05	.16	.00	9.51	3.24	.97	.00	11.80
1999	1.75	.07	.08	.01	9.41	3.31	1.01	2.47	11.31
2000	1.41	.03	.08	.00	8.35	2.84	1.04	2.08	9.87
2001	1.07	.06	.14	.00	6.45	2.04	.57	2.05	7.72
2002	1.03	.08	.65	.00	5.00	1.86	.02	.96	6.76
2003	.90	.24	.21	.06	4.20	1.53	.13	1.05	5.55
2004	.90	.21	.14	.04	4.00	1.39	.09	.85	5.25
MEMO									
Total exposure (billions of dollars)									
1998	37.87	5.43	8.53	1.05	104.69	24.15	23.62	27.55	156.52
1999	37.45	6.23	7.43	.95	101.63	24.77	24.51	27.34	152.74
2000	37.30	7.46	12.33	1.39	107.31	25.71	23.82	31.59	164.40
2001	36.32	7.66	12.88	1.80	162.39	78.00	19.87	39.01	219.25
2002	36.32	8.70	17.55	3.37	123.53	66.15	7.75	26.55	186.10
2003	39.12	13.55	19.07	5.20	115.23	62.98	6.07	23.74	186.97
2004	79.57	16.27	23.85	6.02	124.39	65.17	5.75	25.46	244.07

NOTE. For the definition of tier 1 capital, see text note 10. Exposures consist of lending and derivatives exposures for cross-border and local-office operations. Respondents may file information on one bank or on the bank holding company as a whole.

The year-end 2004 data cover seventy banks with a total of $391.4 billion in tier 1 capital; of these institutions, five were money center banks, with $195.9 billion in tier 1 capital, and four were other large banks, with $57.2 billion in tier 1 capital; the remaining sixty-one ("other") banks had $138.3 billion in tier 1 capital. The average "other" bank at year-end 2004 had $29 billion in assets.

1. Indonesia, Korea, Malaysia, Philippines, and Thailand.

SOURCE. Federal Financial Institutions Examination Council Statistical Release E.16, "Country Exposure Lending Survey," available at www.ffiec.gov/E16.htm.

Appendix tables start on page 164

A.1. Portfolio composition, interest rates, and income and expense, all U.S. banks, 1995–2004

A. All banks

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Balance sheet items as a percentage of average net consolidated assets									
Interest-earning assets	86.98	87.38	87.15	86.76	87.03	87.13	86.48	86.42	86.08	86.90
Loans and leases, net	58.39	59.91	58.72	58.33	59.34	60.48	58.95	57.83	56.88	56.98
Commercial and industrial	15.20	15.59	15.77	16.36	17.07	17.16	16.08	14.07	12.18	11.06
U.S. addressees	12.87	13.06	13.17	13.61	14.43	14.67	13.69	12.04	10.48	9.52
Foreign addressees	2.33	2.53	2.60	2.75	2.64	2.49	2.39	2.04	1.70	1.54
Consumer	12.12	12.27	11.50	10.41	9.71	9.38	9.23	9.35	9.06	9.18
Credit card	4.73	4.93	4.62	4.02	3.51	3.52	3.63	3.78	3.55	3.87
Installment and other	7.39	7.34	6.88	6.39	6.20	5.87	5.60	5.57	5.51	5.31
Real estate	25.00	25.04	25.00	24.85	25.44	27.04	27.10	28.39	29.91	30.78
In domestic offices	24.36	24.42	24.39	24.28	24.87	26.49	26.60	27.91	29.46	30.25
Construction and land development	1.59	1.63	1.73	1.86	2.18	2.51	2.85	2.98	2.99	3.25
Farmland	.56	.56	.55	.55	.56	.56	.55	.56	.54	.54
One- to four-family residential	14.41	14.42	14.41	14.25	14.10	14.96	14.67	15.40	16.96	17.42
Home equity	1.88	1.85	1.94	1.89	1.76	1.96	2.18	2.80	3.40	4.34
Other	12.54	12.57	12.47	12.37	12.34	13.00	12.49	12.60	13.57	13.09
Multifamily residential	.81	.85	.83	.82	.88	.99	.97	1.02	1.05	1.06
Nonfarm nonresidential	6.97	6.96	6.88	6.80	7.15	7.48	7.56	7.95	7.91	7.97
In foreign offices	.65	.63	.61	.57	.57	.54	.50	.48	.46	.53
To depository institutions and acceptances of other banks	1.92	2.33	1.93	1.91	1.96	1.87	1.83	1.87	1.98	2.11
Foreign governments	.30	.26	.18	.15	.16	.12	.10	.09	.08	.08
Agricultural production	.96	.92	.90	.89	.83	.78	.75	.70	.63	.59
Other loans	3.11	3.32	2.80	2.78	2.75	2.58	2.34	2.06	2.00	2.35
Lease-financing receivables	1.19	1.51	1.87	2.13	2.52	2.63	2.58	2.44	2.11	1.79
LESS: Unearned income on loans	–.14	–.12	–.09	–.07	–.06	–.05	–.04	–.05	–.04	–.04
LESS: Loss reserves[1]	–1.27	–1.21	–1.13	–1.07	–1.04	–1.02	–1.04	–1.11	–1.04	–.91
Securities	21.94	21.00	20.40	20.37	20.40	20.01	19.53	21.27	21.89	22.57
Investment account	19.38	18.19	17.23	17.48	18.33	17.59	16.82	18.30	18.97	18.99
Debt	18.97	17.74	16.74	16.93	17.73	16.93	16.48	17.99	18.72	18.79
U.S. Treasury	5.25	4.19	3.38	2.71	2.14	1.66	.85	.78	.90	.89
U.S. government agency and corporation obligations	9.81	9.74	9.73	10.28	10.85	10.31	10.08	11.46	12.26	12.37
Government-backed mortgage pools	4.46	4.80	4.93	5.16	5.24	4.75	5.13	6.09	6.75	7.13
Collateralized mortgage obligations	2.67	2.11	1.93	2.12	2.15	1.92	1.95	2.35	2.34	2.01
Other	2.68	2.83	2.86	2.99	3.46	3.63	2.99	3.02	3.17	3.22
State and local government	1.80	1.68	1.59	1.57	1.62	1.52	1.49	1.49	1.48	1.41
Private mortgage-backed securities	.62	.61	.50	.67	.88	.95	1.09	1.25	1.30	1.41
Other	1.49	1.51	1.54	1.70	2.24	2.48	2.98	3.01	2.78	2.72
Equity	.41	.45	.50	.55	.61	.66	.34	.31	.25	.20
Trading account	2.55	2.81	3.16	2.90	2.06	2.43	2.72	2.97	2.93	3.59
Gross federal funds sold and reverse RPs	3.93	3.81	5.18	5.37	4.61	4.12	5.11	4.81	4.85	4.58
Interest-bearing balances at depositories	2.73	2.66	2.86	2.69	2.68	2.52	2.89	2.51	2.45	2.76
Non-interest-earning assets	13.02	12.62	12.85	13.24	12.97	12.87	13.52	13.58	13.92	13.10
Revaluation gains held in trading accounts	2.90	2.24	2.59	2.95	2.57	2.28	2.37	2.42	2.70	2.19
Other	10.12	10.37	10.26	10.29	10.40	10.58	11.15	11.16	11.22	10.91
Liabilities	91.99	91.73	91.57	91.51	91.52	91.58	91.25	90.85	90.96	90.57
Interest-bearing liabilities	71.87	71.63	71.37	71.33	72.52	73.30	72.47	71.20	70.48	71.58
Deposits	56.28	55.83	54.96	54.62	54.78	54.66	54.59	53.87	53.34	54.14
In foreign offices	10.27	10.01	10.01	10.14	10.46	10.92	10.18	8.92	8.90	9.72
In domestic offices	46.01	45.83	44.95	44.48	44.32	43.74	44.42	44.95	44.44	44.42
Other checkable deposits	6.63	4.75	3.61	3.11	2.81	2.46	2.36	2.39	2.47	2.53
Savings (including MMDAs)	17.47	18.70	19.11	19.89	21.00	20.64	22.28	24.92	26.12	27.14
Small-denomination time deposits	16.14	15.96	15.16	14.14	13.10	12.49	11.59	10.13	8.65	7.63
Large-denomination time deposits	5.77	6.41	7.07	7.33	7.42	8.16	8.18	7.51	7.19	7.13
Gross federal funds purchased and RPs	7.70	7.18	8.13	7.98	7.97	7.83	7.95	7.77	7.75	7.24
Other	7.88	8.62	8.27	8.73	9.76	10.81	9.92	9.56	9.39	10.20
Non-interest-bearing liabilities	20.12	20.10	20.20	20.17	19.00	18.28	18.78	19.66	20.48	18.98
Demand deposits in domestic offices	12.68	12.81	12.15	10.99	9.78	8.61	8.00	7.67	7.27	6.58
Revaluation losses held in trading accounts	2.88	2.14	2.64	2.97	2.52	2.29	2.21	2.09	2.30	1.95
Other	4.57	5.14	5.41	6.21	6.70	7.37	8.57	9.90	10.92	10.45
Capital account	8.01	8.27	8.43	8.49	8.48	8.42	8.75	9.15	9.04	9.43
MEMO										
Commercial real estate loans	9.83	9.91	9.98	10.11	10.87	11.58	12.09	12.57	12.47	12.78
Other real estate owned	.19	.14	.11	.08	.06	.05	.05	.06	.06	.06
Managed liabilities	32.10	32.77	34.13	34.97	36.59	38.83	37.42	35.05	34.61	35.69
Federal Home Loan Bank advances	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	2.89	3.17	3.19	3.07
Average net consolidated assets (billions of dollars)	4,149	4,379	4,737	5,148	5,439	5,906	6,334	6,635	7,249	7,879

A.1.—Continued

A. All banks

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Effective interest rate (percent)[2]									
Rates earned										
Interest-earning assets	8.33	8.16	8.17	8.02	7.71	8.20	7.38	6.11	5.30	5.11
Taxable equivalent	8.41	8.22	8.23	8.07	7.76	8.26	7.43	6.16	5.34	5.15
Loans and leases, gross	9.25	9.01	9.03	8.85	8.47	9.00	8.16	6.90	6.16	5.92
Net of loss provisions	8.93	8.56	8.50	8.30	7.97	8.33	7.15	5.85	5.48	5.48
Securities	6.51	6.46	6.54	6.45	6.27	6.47	6.05	4.96	3.96	3.89
Taxable equivalent	6.73	6.66	6.73	6.63	6.46	6.65	6.23	5.12	4.10	4.02
Investment account	6.35	6.39	6.50	6.38	6.25	6.45	6.05	5.04	4.00	3.96
U.S. Treasury securities and U.S. government agency obligations (excluding MBS)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.76	4.42	3.29	3.11
Mortgage-backed securities	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	6.45	5.44	4.24	4.38
Other	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.60	4.74	4.08	3.76
Trading account	7.73	6.86	6.75	6.85	6.47	6.63	6.08	4.47	3.70	3.51
Gross federal funds sold and reverse RPs	5.63	5.21	5.45	5.29	4.78	5.56	3.86	1.93	1.43	1.43
Interest-bearing balances at depositories	6.84	6.20	6.23	6.32	5.95	6.48	4.01	2.79	2.09	1.98
Rates paid										
Interest-bearing liabilities	4.99	4.82	4.92	4.88	4.47	5.17	4.15	2.54	1.87	1.77
Interest-bearing deposits	4.47	4.34	4.39	4.31	3.87	4.45	3.61	2.12	1.48	1.37
In foreign offices	6.12	5.54	5.44	5.66	4.91	5.61	3.95	2.38	1.64	1.77
In domestic offices	4.11	4.07	4.16	4.01	3.63	4.17	3.54	2.07	1.45	1.29
Other checkable deposits	2.06	2.04	2.25	2.29	2.08	2.34	1.96	1.06	.75	.77
Savings (including MMDAs)	3.19	3.00	2.93	2.79	2.49	2.86	2.19	1.13	.74	.72
Large time deposits[3]	5.47	5.39	5.45	5.22	4.92	5.78	5.04	3.37	2.59	2.35
Other time deposits[3]	5.44	5.40	5.54	5.48	5.09	5.69	5.43	3.73	2.91	2.56
Gross federal funds purchased and RPs	5.65	5.12	5.17	5.19	4.73	5.77	3.84	1.88	1.30	1.55
Other interest-bearing liabilities	7.45	6.92	6.94	6.89	6.48	6.97	5.92	4.32	3.59	3.26
	Income and expense as a percentage of average net consolidated assets									
Gross interest income	7.29	7.16	7.15	6.99	6.73	7.18	6.39	5.28	4.55	4.44
Taxable equivalent	7.35	7.22	7.21	7.04	6.78	7.22	6.43	5.32	4.59	4.48
Loans	5.48	5.48	5.41	5.27	5.12	5.53	4.92	4.07	3.56	3.42
Securities	1.23	1.16	1.11	1.10	1.14	1.15	1.00	.89	.74	.74
Gross federal funds sold and reverse RPs	.23	.21	.29	.29	.23	.23	.20	.09	.07	.07
Other	.35	.32	.35	.32	.24	.27	.27	.22	.18	.21
Gross interest expense	3.57	3.43	3.48	3.46	3.22	3.76	2.98	1.79	1.30	1.26
Deposits	2.54	2.46	2.48	2.43	2.20	2.56	2.09	1.23	.87	.81
Gross federal funds purchased and RPs	.44	.38	.43	.43	.39	.45	.31	.15	.10	.12
Other	.58	.59	.57	.60	.63	.75	.58	.41	.33	.33
Net interest income	3.72	3.73	3.68	3.53	3.51	3.41	3.41	3.48	3.25	3.18
Taxable equivalent	3.79	3.79	3.73	3.57	3.56	3.46	3.45	3.53	3.28	3.22
Loss provisioning[4]	.31	.37	.41	.42	.39	.50	.68	.68	.45	.30
Non-interest income	2.02	2.18	2.23	2.40	2.66	2.59	2.53	2.54	2.53	2.39
Service charges on deposits	.39	.39	.39	.38	.40	.40	.42	.45	.44	.42
Fiduciary activities	.31	.33	.35	.37	.38	.38	.35	.33	.31	.32
Trading revenue	.15	.17	.17	.15	.19	.21	.20	.16	.16	.13
Interest rate exposures	n.a.	.09	.08	.05	.07	.08	.10	.08	.06	.01
Foreign exchange rate exposures	n.a.	.06	.08	.09	.09	.08	.07	.07	.07	.08
Other commodity and equity exposures	n.a.	.02	*	.01	.03	.04	.03	.01	.02	.04
Other	1.17	1.29	1.32	1.49	1.69	1.61	1.56	1.61	1.63	1.52
Non-interest expense	3.64	3.71	3.61	3.77	3.76	3.66	3.57	3.47	3.36	3.34
Salaries, wages, and employee benefits	1.54	1.55	1.53	1.55	1.58	1.51	1.49	1.51	1.50	1.46
Occupancy	.48	.48	.47	.47	.48	.45	.44	.44	.43	.42
Other	1.62	1.69	1.62	1.75	1.70	1.70	1.64	1.52	1.43	1.46
Net non-interest expense	1.62	1.54	1.38	1.36	1.11	1.07	1.04	.93	.82	.95
Gains on investment account securities	.01	.03	.04	.06	*	−.04	.07	.10	.08	.05
Income before taxes and extraordinary items	1.81	1.85	1.92	1.81	2.02	1.81	1.76	1.97	2.05	1.98
Taxes	.63	.65	.68	.62	.72	.63	.59	.65	.67	.63
Extraordinary items, net of income taxes	*	*	*	.01	*	*	−.01	*	.01	*
Net income	1.18	1.20	1.25	1.20	1.31	1.18	1.17	1.32	1.39	1.34
Cash dividends declared	.75	.90	.90	.80	.96	.89	.87	1.01	1.07	.76
Retained income	.43	.30	.35	.40	.35	.29	.30	.30	.31	.59
MEMO: Return on equity	14.69	14.51	14.83	14.08	15.39	13.97	13.34	14.41	15.33	14.23

* In absolute value, less than 0.005 percent.

n.a. Not available. MMDA Money market deposit account. RP Repurchase agreement. CD Certificate of deposit.

1. Includes allocated transfer risk reserves.
2. When possible, based on the average of quarterly balance sheet data reported on schedule RC-K of the quarterly Call Report.
3. Before 1997, large time open accounts included in other time deposits.
4. Includes provisions for allocated transfer risk.

A.1. Portfolio composition, interest rates, and income and expense, all U.S. banks, 1995–2004

B. Ten largest banks by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Balance sheet items as a percentage of average net consolidated assets									
Interest-earning assets	77.12	80.12	81.84	81.25	81.49	82.23	81.74	81.68	81.39	83.54
Loans and leases, net	50.05	53.51	50.91	50.76	53.37	55.22	53.86	53.61	52.20	51.29
Commercial and industrial	16.16	17.17	16.90	18.07	19.20	19.87	18.82	16.16	12.98	10.53
U.S. addressees	8.66	9.59	10.24	11.76	13.14	13.95	13.42	11.69	9.40	7.48
Foreign addressees	7.50	7.59	6.66	6.31	6.06	5.92	5.41	4.47	3.59	3.06
Consumer	6.60	6.22	6.40	6.04	5.94	5.43	6.17	7.82	7.96	8.49
Credit card	1.96	1.23	1.34	1.30	1.36	1.34	1.64	2.90	2.81	3.19
Installment and other	4.65	4.99	5.06	4.74	4.58	4.09	4.53	4.92	5.15	5.30
Real estate	15.82	16.53	17.42	16.51	16.96	19.82	19.23	20.78	22.68	23.21
In domestic offices	13.48	14.44	15.69	15.08	15.55	18.48	18.05	19.70	21.74	22.21
Construction and land development	.58	.51	.68	.77	.90	.98	1.27	1.42	1.36	1.40
Farmland	.06	.06	.09	.09	.10	.11	.11	.12	.10	.10
One- to four-family residential	9.62	10.43	11.02	10.33	10.77	13.37	12.41	13.51	16.03	16.71
Home equity	1.40	1.53	1.70	1.72	1.54	1.61	1.78	2.35	2.96	4.04
Other	8.22	8.90	9.31	8.61	9.22	11.76	10.63	11.17	13.07	12.67
Multifamily residential	.38	.38	.39	.38	.43	.60	.51	.55	.47	.45
Nonfarm nonresidential	2.83	3.05	3.52	3.51	3.35	3.42	3.76	4.09	3.78	3.55
In foreign offices	2.35	2.09	1.73	1.43	1.41	1.34	1.18	1.08	.94	1.00
To depository institutions and acceptances of other banks	5.04	6.14	4.20	4.05	4.34	3.78	3.23	3.20	3.54	4.10
Foreign governments	.90	.69	.45	.35	.38	.28	.20	.20	.17	.16
Agricultural production	.21	.23	.31	.28	.26	.23	.28	.23	.19	.22
Other loans	5.76	6.34	4.15	3.74	3.96	3.75	3.51	2.94	2.87	3.31
Lease-financing receivables	1.14	1.59	2.24	2.81	3.40	3.07	3.43	3.44	2.87	2.10
LESS: Unearned income on loans	–.14	–.11	–.07	–.06	–.05	–.04	–.04	–.08	–.06	–.04
LESS: Loss reserves[1]	–1.45	–1.30	–1.08	–1.01	–1.03	–.97	–.97	–1.12	–1.02	–.80
Securities	19.53	19.83	20.00	19.72	18.34	18.98	17.81	20.54	21.22	22.95
Investment account	10.65	10.60	10.97	12.12	13.08	13.71	12.14	14.36	15.31	15.99
Debt	10.27	10.22	10.55	11.64	12.57	13.03	11.88	14.13	15.11	15.83
U.S. Treasury	2.03	1.93	1.56	1.70	1.98	1.96	.68	.59	.82	.86
U.S. government agency and corporation obligations	4.46	4.59	5.34	6.31	6.35	6.59	6.84	8.69	9.20	9.92
Government-backed mortgage pools	2.89	3.58	4.26	5.13	5.03	4.88	4.99	6.38	7.59	8.64
Collateralized mortgage obligations	1.50	.95	.93	.93	.79	.93	1.11	1.52	.91	.70
Other	.08	.06	.15	.26	.52	.78	.74	.79	.70	.58
State and local government	.49	.39	.51	.47	.45	.51	.55	.59	.59	.57
Private mortgage-backed securities	.32	.30	.32	.60	.57	.51	.58	.92	1.10	.95
Other	2.97	3.01	2.81	2.57	3.22	3.47	3.22	3.34	3.40	3.53
Equity	.38	.38	.42	.47	.51	.68	.26	.22	.20	.16
Trading account	8.88	9.23	9.03	7.60	5.25	5.26	5.67	6.18	5.91	6.96
Gross federal funds sold and reverse RPs	3.20	3.10	7.56	7.81	6.64	5.02	6.38	5.26	5.79	6.37
Interest-bearing balances at depositories	4.34	3.68	3.37	2.96	3.14	3.01	3.69	2.28	2.18	2.93
Non-interest-earning assets	22.88	19.88	18.16	18.75	18.51	17.77	18.26	18.32	18.61	16.46
Revaluation gains held in trading accounts	10.77	7.63	7.36	7.62	6.66	5.66	5.48	5.40	5.79	4.45
Other	12.11	12.25	10.80	11.13	11.85	12.11	12.78	12.93	12.83	12.01
Liabilities	93.59	93.04	92.61	92.58	92.28	92.36	92.14	91.52	91.94	91.64
Interest-bearing liabilities	63.37	64.45	65.83	65.81	66.87	67.81	66.76	65.42	65.55	68.18
Deposits	47.49	47.87	47.36	47.65	48.79	49.27	49.09	48.96	49.11	51.26
In foreign offices	28.36	26.41	22.18	20.17	21.04	21.62	19.22	16.27	15.68	16.20
In domestic offices	19.12	21.46	25.18	27.48	27.76	27.66	29.88	32.70	33.43	35.05
Other checkable deposits	2.30	1.61	1.21	.99	.72	.74	.90	.95	1.02	1.22
Savings (including MMDAs)	10.56	12.31	14.26	15.83	16.84	16.73	19.23	22.81	24.28	26.42
Small-denomination time deposits	4.04	4.68	5.82	6.03	5.66	5.38	5.11	4.71	3.68	3.24
Large-denomination time deposits	2.23	2.86	3.89	4.62	4.54	4.80	4.63	4.22	4.45	4.18
Gross federal funds purchased and RPs	6.17	5.88	10.26	9.78	8.84	8.89	9.04	8.83	8.62	7.79
Other	9.71	10.69	8.20	8.37	9.24	9.65	8.62	7.63	7.82	9.13
Non-interest-bearing liabilities	30.22	28.59	26.78	26.77	25.41	24.56	25.38	26.10	26.40	23.46
Demand deposits in domestic offices	8.88	9.73	8.98	8.46	7.83	7.28	7.50	7.40	6.72	5.43
Revaluation losses held in trading accounts	10.68	7.27	7.53	7.67	6.51	5.69	5.10	4.63	4.88	3.95
Other	10.66	11.59	10.27	10.65	11.06	11.59	12.79	14.07	14.80	14.08
Capital account	6.41	6.96	7.39	7.42	7.72	7.64	7.86	8.48	8.06	8.36
MEMO										
Commercial real estate loans	4.40	4.65	5.45	5.61	5.69	5.87	6.68	6.92	6.31	5.99
Other real estate owned	.27	.18	.13	.09	.06	.04	.04	.03	.03	.03
Managed liabilities	47.94	47.39	46.02	44.42	45.49	46.84	43.41	38.89	38.60	39.33
Federal Home Loan Bank advances	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	.82	.82	.84	.79
Average net consolidated assets (billions of dollars)	1,051	1,189	1,514	1,820	1,935	2,234	2,527	2,785	3,148	3,654

A.1.—Continued

B. Ten largest banks by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Effective interest rate (percent)[2]									
Rates earned										
Interest-earning assets	8.20	7.72	7.57	7.55	7.37	7.76	6.85	5.85	5.01	4.74
Taxable equivalent	8.22	7.74	7.60	7.57	7.39	7.78	6.87	5.87	5.03	4.77
Loans and leases, gross	8.84	8.32	8.25	8.21	7.99	8.46	7.52	6.54	5.78	5.53
Net of loss provisions	8.88	8.31	8.10	7.77	7.65	7.92	6.56	5.32	5.21	5.30
Securities	7.40	6.80	6.78	6.83	6.58	6.48	6.26	5.09	4.15	4.11
Taxable equivalent	7.47	6.85	6.85	6.89	6.65	6.55	6.34	5.16	4.21	4.17
Investment account	7.04	6.70	6.76	6.78	6.59	6.40	6.23	5.30	4.26	4.37
U.S. Treasury securities and U.S. government agency obligations (excluding MBS)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.01	3.74	2.62	2.92
Mortgage-backed securities	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	6.42	5.55	4.51	4.83
Other	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	6.34	5.30	4.28	3.76
Trading account	7.83	6.90	6.81	6.92	6.56	6.70	6.33	4.60	3.87	3.52
Gross federal funds sold and reverse RPs	5.20	4.92	5.45	5.20	4.52	4.93	3.86	2.20	1.66	1.47
Interest-bearing balances at depositories	7.15	6.71	6.91	7.16	7.22	7.43	3.73	3.40	2.49	1.80
Rates paid										
Interest-bearing liabilities	5.88	5.44	5.41	5.29	4.79	5.37	4.09	2.55	1.86	1.80
Interest-bearing deposits	4.99	4.57	4.54	4.40	3.82	4.40	3.27	1.95	1.36	1.30
In foreign offices	6.07	5.62	5.52	5.83	4.99	5.67	4.02	2.59	1.76	1.87
In domestic offices	3.42	3.32	3.69	3.39	3.04	3.51	2.85	1.68	1.20	1.08
Other checkable deposits	1.29	1.32	1.97	1.67	1.44	1.61	1.67	.93	.80	.97
Savings (including MMDAs)	3.11	2.76	2.68	2.45	2.11	2.43	1.92	1.02	.73	.71
Large time deposits[3]	3.73	4.62	5.17	4.53	4.36	5.32	4.40	3.26	2.36	2.14
Other time deposits[3]	5.08	4.58	5.45	5.21	4.95	5.53	5.14	3.55	2.86	2.61
Gross federal funds purchased and RPs	5.22	4.93	5.02	5.18	4.53	5.47	3.81	2.02	1.39	1.71
Other interest-bearing liabilities	9.80	8.86	9.13	8.85	8.61	8.15	7.00	5.39	4.26	3.69
	Income and expense as a percentage of average net consolidated assets									
Gross interest income	6.42	6.26	6.31	6.21	6.01	6.39	5.56	4.78	4.06	3.95
Taxable equivalent	6.43	6.27	6.33	6.22	6.03	6.41	5.58	4.80	4.08	3.97
Loans	4.44	4.48	4.31	4.27	4.35	4.74	4.14	3.58	3.05	2.86
Securities	.75	.71	.73	.81	.85	.88	.72	.73	.63	.69
Gross federal funds sold and reverse RPs	.21	.18	.45	.42	.30	.25	.25	.12	.10	.10
Other	1.00	.88	.82	.70	.51	.51	.44	.35	.28	.30
Gross interest expense	3.74	3.52	3.55	3.48	3.16	3.60	2.69	1.65	1.20	1.22
Deposits	2.43	2.26	2.26	2.20	1.97	2.33	1.74	1.06	.75	.74
Gross federal funds purchased and RPs	.35	.31	.54	.54	.40	.49	.35	.18	.13	.14
Other	.95	.95	.75	.74	.79	.78	.59	.41	.33	.33
Net interest income	2.68	2.73	2.76	2.73	2.84	2.78	2.87	3.13	2.86	2.73
Taxable equivalent	2.70	2.75	2.79	2.75	2.86	2.80	2.89	3.15	2.88	2.75
Loss provisioning[4]	.11	.11	.16	.31	.26	.38	.59	.73	.35	.16
Non-interest income	2.16	2.34	2.12	2.15	2.55	2.54	2.23	2.32	2.31	2.21
Service charges on deposits	.25	.28	.32	.33	.37	.40	.44	.48	.46	.45
Fiduciary activities	.30	.31	.34	.32	.31	.27	.29	.26	.26	.24
Trading revenue	.46	.52	.43	.33	.46	.48	.43	.32	.30	.22
Interest rate exposures	n.a.	.30	.23	.10	.17	.20	.21	.15	.12	.03
Foreign exchange rate exposures	n.a.	.17	.20	.20	.19	.18	.14	.14	.14	.14
Other commodity and equity exposures	n.a.	.05	*	.03	.09	.11	.08	.03	.04	.06
Other	1.15	1.23	1.04	1.17	1.41	1.39	1.06	1.25	1.29	1.30
Non-interest expense	3.32	3.57	3.24	3.47	3.45	3.31	3.13	3.16	3.02	3.11
Salaries, wages, and employee benefits	1.58	1.57	1.45	1.45	1.57	1.46	1.38	1.41	1.39	1.34
Occupancy	.50	.50	.47	.47	.50	.47	.45	.46	.45	.43
Other	1.24	1.50	1.33	1.54	1.38	1.39	1.30	1.28	1.18	1.33
Net non-interest expense	1.16	1.23	1.12	1.32	.90	.77	.90	.84	.71	.90
Gains on investment account securities	.03	.04	.08	.11	.03	−.03	.08	.13	.11	.08
Income before taxes and extraordinary items	1.44	1.44	1.56	1.22	1.71	1.60	1.46	1.69	1.91	1.74
Taxes	.55	.52	.58	.44	.66	.60	.48	.57	.62	.55
Extraordinary items, net of income taxes	*	*	*	*	*	*	−.01	*	*	*
Net income	.88	.92	.98	.78	1.05	1.00	.97	1.12	1.29	1.19
Cash dividends declared	.57	.70	.82	.53	.79	.86	.66	1.05	.99	.65
Retained income	.31	.21	.15	.25	.26	.13	.31	.07	.30	.55
MEMO: Return on equity	13.78	13.21	13.22	10.53	13.58	13.04	12.34	13.24	16.01	14.28

* In absolute value, less than 0.005 percent.

n.a. Not available. MMDA Money market deposit account. RP Repurchase agreement. CD Certificate of deposit.

1. Includes allocated transfer risk reserves.
2. When possible, based on the average of quarterly balance sheet data reported on schedule RC-K of the quarterly Call Report.
3. Before 1997, large time open accounts included in other time deposits.
4. Includes provisions for allocated transfer risk.

A.1. Portfolio composition, interest rates, and income and expense, all U.S. banks, 1995–2004

C. Banks ranked 11 through 100 by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Balance sheet items as a percentage of average net consolidated assets									
Interest-earning assets	88.71	88.26	87.50	87.87	88.41	88.67	88.08	88.34	88.10	88.19
Loans and leases, net	62.68	64.24	63.89	64.38	64.23	64.88	62.14	60.00	59.48	60.63
Commercial and industrial	19.26	18.95	19.01	18.92	19.40	18.19	15.84	13.27	11.96	11.91
U.S. addressees	18.10	17.71	17.78	17.59	18.18	17.64	15.36	12.94	11.66	11.65
Foreign addressees	1.16	1.24	1.22	1.33	1.22	.55	.48	.33	.30	.26
Consumer	14.23	15.67	15.62	14.52	13.57	13.79	13.20	12.79	12.57	12.73
Credit card	7.34	8.26	8.50	7.67	6.78	6.97	6.97	6.56	6.35	6.90
Installment and other	6.89	7.40	7.12	6.86	6.79	6.82	6.23	6.22	6.21	5.83
Real estate	23.25	23.26	22.99	24.59	24.80	26.21	27.29	28.94	30.67	32.16
In domestic offices	23.10	23.10	22.85	24.42	24.62	26.12	27.21	28.88	30.54	31.96
Construction and land development	1.50	1.55	1.69	2.03	2.43	3.00	3.31	3.36	3.22	3.51
Farmland	.13	.13	.14	.17	.19	.22	.23	.22	.20	.19
One- to four-family residential	14.16	14.15	13.88	14.86	14.15	14.51	15.51	17.05	18.79	19.52
Home equity	2.19	2.08	2.22	2.17	2.08	2.49	2.90	3.92	4.74	5.90
Other	11.97	12.07	11.65	12.69	12.07	12.02	12.60	13.13	14.05	13.62
Multifamily residential	.77	.89	.93	1.00	1.02	1.11	1.16	1.20	1.32	1.34
Nonfarm nonresidential	6.54	6.37	6.21	6.36	6.82	7.28	6.99	7.05	7.00	7.41
In foreign offices	.15	.16	.15	.18	.19	.09	.09	.06	.13	.20
To depository institutions and acceptances of other banks	1.61	1.53	1.30	1.09	.93	1.05	1.40	1.44	1.21	.54
Foreign governments	.20	.20	.09	.06	.06	.03	.03	.02	.02	.01
Agricultural production	.26	.28	.29	.33	.33	.37	.32	.27	.23	.19
Other loans	3.29	3.27	3.18	3.35	2.99	2.57	2.03	1.80	1.59	1.88
Lease-financing receivables	1.96	2.41	2.70	2.72	3.29	3.82	3.18	2.65	2.35	2.28
LESS: Unearned income on loans	−.07	−.06	−.05	−.04	−.04	−.03	−.02	−.02	−.02	−.02
LESS: Loss reserves[1]	−1.32	−1.27	−1.24	−1.16	−1.11	−1.12	−1.13	−1.17	−1.10	−1.06
Securities	18.64	16.87	15.80	16.66	17.79	17.32	19.00	20.30	21.16	21.28
Investment account	17.88	16.06	15.07	16.13	17.28	16.10	17.71	19.17	20.09	20.12
Debt	17.51	15.62	14.58	15.58	16.64	15.50	17.32	18.82	19.88	19.96
U.S. Treasury	4.82	3.34	2.81	2.25	1.70	1.12	.67	.74	.95	.89
U.S. government agency and corporation obligations	9.40	9.12	8.98	9.93	10.57	9.70	10.09	11.45	12.99	12.80
Government-backed mortgage pools	5.06	5.42	5.17	4.98	5.12	4.31	5.19	6.00	6.08	5.74
Collateralized mortgage obligations	2.82	2.16	2.13	2.83	2.89	2.55	2.42	2.79	3.72	3.42
Other	1.51	1.54	1.68	2.12	2.56	2.84	2.48	2.65	3.19	3.64
State and local government	1.11	.99	.88	.92	.99	.96	.99	.97	.95	.96
Private mortgage-backed securities	1.02	.96	.73	.96	1.35	1.66	2.01	2.13	2.14	2.65
Other	1.16	1.21	1.18	1.53	2.02	2.06	3.56	3.53	2.85	2.66
Equity	.37	.44	.49	.55	.65	.60	.39	.34	.21	.16
Trading account	.76	.80	.73	.54	.51	1.22	1.29	1.13	1.07	1.16
Gross federal funds sold and reverse RPs	4.52	4.26	4.38	3.57	3.34	3.76	4.06	4.71	4.20	2.98
Interest-bearing balances at depositories	2.87	2.89	3.43	3.24	3.06	2.71	2.88	3.33	3.26	3.29
Non-interest-earning assets	11.29	11.74	12.50	12.13	11.59	11.33	11.92	11.66	11.90	11.81
Revaluation gains held in trading accounts	.50	.51	.69	.75	.56	.40	.55	.47	.60	.42
Other	10.78	11.23	11.81	11.38	11.03	10.92	11.37	11.19	11.30	11.39
Liabilities	92.23	92.02	91.85	91.63	91.66	91.57	91.15	90.79	90.65	89.87
Interest-bearing liabilities	74.05	73.14	72.60	73.40	74.97	76.46	75.98	74.69	73.18	74.10
Deposits	52.32	51.81	51.45	51.50	51.50	51.57	51.94	50.48	49.81	50.78
In foreign offices	8.12	7.52	7.85	8.15	7.96	7.34	6.86	6.09	6.33	6.99
In domestic offices	44.20	44.30	43.60	43.35	43.53	44.23	45.08	44.38	43.48	43.79
Other checkable deposits	5.62	3.06	1.95	1.75	1.60	1.32	1.20	1.17	1.33	1.41
Savings (including MMDAs)	18.78	20.76	21.08	21.40	22.46	22.34	24.36	26.45	27.52	27.63
Small-denomination time deposits	14.24	14.09	13.43	12.84	11.85	11.80	10.66	8.78	7.47	6.94
Large-denomination time deposits	5.55	6.39	7.15	7.36	7.62	8.77	8.86	7.98	7.16	7.81
Gross federal funds purchased and RPs	11.37	10.00	9.36	9.48	9.77	9.28	9.71	9.66	9.69	8.96
Other	10.36	11.32	11.79	12.43	13.70	15.61	14.32	14.55	13.68	14.36
Non-interest-bearing liabilities	18.18	18.89	19.24	18.23	16.70	15.12	15.17	16.10	17.47	15.77
Demand deposits in domestic offices	14.26	14.47	14.17	12.39	10.52	8.61	7.17	6.32	5.97	5.63
Revaluation losses held in trading accounts	.49	.49	.68	.76	.58	.41	.52	.44	.56	.40
Other	3.43	3.93	4.39	5.07	5.59	6.09	7.49	9.34	10.95	9.74
Capital account	7.77	7.98	8.15	8.37	8.34	8.43	8.85	9.21	9.35	10.13
MEMO										
Commercial real estate loans	9.42	9.38	9.44	10.11	11.00	12.06	12.06	12.24	12.10	12.85
Other real estate owned	.13	.08	.06	.04	.03	.03	.04	.05	.06	.05
Managed liabilities	35.68	35.60	36.60	38.11	39.83	41.98	40.81	39.48	38.12	39.29
Federal Home Loan Bank advances	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	4.07	4.85	4.75	4.65
Average net consolidated assets (billions of dollars)	1,338	1,450	1,604	1,745	1,881	2,031	2,130	2,124	2,287	2,376

A.1.—Continued

C. Banks ranked 11 through 100 by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Effective interest rate (percent)[2]									
Rates earned										
Interest-earning assets	8.31	8.18	8.33	8.13	7.84	8.44	7.54	6.04	5.30	5.26
Taxable equivalent	8.37	8.23	8.36	8.17	7.88	8.48	7.58	6.07	5.33	5.29
Loans and leases, gross	9.10	8.88	9.03	8.82	8.50	9.14	8.26	6.80	6.11	5.98
Net of loss provisions	8.67	8.21	8.27	8.15	7.80	8.25	6.96	5.59	5.11	5.19
Securities	6.38	6.49	6.55	6.31	6.32	6.64	5.96	4.79	3.80	3.63
Taxable equivalent	6.56	6.66	6.70	6.46	6.46	6.77	6.08	4.91	3.91	3.73
Investment account	6.35	6.49	6.57	6.33	6.34	6.66	6.04	4.86	3.87	3.64
U.S. Treasury securities and U.S. government agency obligations (excluding MBS)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.83	4.28	3.17	2.94
Mortgage-backed securities	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	6.60	5.34	4.20	4.02
Other	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.13	4.22	3.61	3.29
Trading account	7.27	6.53	6.05	5.86	5.58	6.25	4.83	3.59	2.62	3.43
Gross federal funds sold and reverse RPs	5.91	5.31	5.45	5.46	5.12	6.06	3.86	1.68	1.14	1.25
Interest-bearing balances at depositories	6.78	5.82	5.76	5.67	4.81	5.49	4.38	2.46	1.93	2.27
Rates paid										
Interest-bearing liabilities	4.94	4.70	4.79	4.77	4.38	5.22	4.16	2.41	1.79	1.71
Interest-bearing deposits	4.35	4.15	4.22	4.15	3.76	4.42	3.60	1.96	1.35	1.29
In foreign offices	6.30	5.29	5.23	5.22	4.70	5.38	3.67	1.70	1.23	1.42
In domestic offices	4.01	3.96	4.04	3.96	3.60	4.26	3.60	1.99	1.36	1.27
Other checkable deposits	1.89	1.78	2.01	2.41	2.03	2.57	2.32	.94	.64	.72
Savings (including MMDAs)	3.10	2.91	2.84	2.76	2.49	2.94	2.30	1.08	.66	.65
Large time deposits[3]	5.70	5.50	5.47	5.32	4.96	5.88	5.11	3.36	2.70	2.48
Other time deposits[3]	5.35	5.26	5.43	5.35	5.03	5.73	5.42	3.68	2.95	2.58
Gross federal funds purchased and RPs	5.86	5.19	5.29	5.22	4.87	6.02	3.86	1.73	1.20	1.37
Other interest-bearing liabilities	6.43	5.95	5.85	5.81	5.41	6.36	5.30	3.54	3.02	2.76
	Income and expense as a percentage of average net consolidated assets									
Gross interest income	7.40	7.24	7.26	7.16	6.98	7.54	6.70	5.31	4.67	4.67
Taxable equivalent	7.45	7.28	7.30	7.19	7.02	7.57	6.73	5.34	4.70	4.70
Loans	5.79	5.80	5.87	5.79	5.56	6.05	5.28	4.15	3.72	3.72
Securities	1.13	1.03	.98	1.00	1.10	1.09	1.06	.90	.75	.73
Gross federal funds sold and reverse RPs	.27	.23	.22	.19	.18	.22	.15	.08	.04	.03
Other	.21	.18	.19	.18	.14	.18	.21	.18	.15	.19
Gross interest expense	3.62	3.39	3.41	3.45	3.26	3.96	3.14	1.77	1.30	1.26
Deposits	2.29	2.18	2.23	2.23	2.02	2.41	2.01	1.09	.77	.74
Gross federal funds purchased and RPs	.67	.55	.51	.51	.51	.56	.38	.17	.12	.13
Other	.66	.66	.68	.71	.74	.99	.75	.51	.41	.40
Net interest income	3.78	3.84	3.85	3.71	3.72	3.58	3.56	3.54	3.37	3.41
Taxable equivalent	3.84	3.89	3.89	3.74	3.75	3.61	3.59	3.57	3.40	3.44
Loss provisioning[4]	.39	.54	.60	.54	.55	.68	.91	.80	.67	.55
Non-interest income	2.38	2.61	2.76	3.07	3.36	3.18	3.36	3.30	3.29	3.05
Service charges on deposits	.44	.44	.44	.42	.41	.42	.42	.42	.42	.40
Fiduciary activities	.40	.43	.44	.49	.48	.52	.42	.42	.37	.42
Trading revenue	.09	.08	.08	.09	.08	.07	.08	.08	.09	.07
Interest rate exposures	n.a.	.03	.02	.03	.02	.02	.04	.04	.04	−.01
Foreign exchange rate exposures	n.a.	.04	.05	.06	.05	.04	.03	.04	.04	.05
Other commodity and equity exposures	n.a.	.01	*	*	*	*	*	*	.01	.03
Other	1.45	1.67	1.79	2.07	2.39	2.18	2.44	2.37	2.41	2.16
Non-interest expense	3.79	3.85	3.85	4.03	4.12	4.00	3.95	3.73	3.64	3.55
Salaries, wages, and employee benefits	1.47	1.51	1.51	1.53	1.53	1.44	1.47	1.49	1.47	1.45
Occupancy	.47	.48	.46	.46	.45	.43	.42	.40	.41	.39
Other	1.85	1.86	1.88	2.04	2.14	2.14	2.07	1.84	1.76	1.70
Net non-interest expense	1.41	1.24	1.10	.96	.76	.82	.59	.43	.35	.50
Gains on investment account securities	.02	.02	.02	.03	−.01	−.05	.09	.10	.06	.03
Income before taxes and extraordinary items	2.01	2.09	2.18	2.24	2.40	2.02	2.15	2.41	2.41	2.39
Taxes	.70	.75	.77	.78	.86	.70	.74	.82	.82	.82
Extraordinary items, net of income taxes	*	*	*	*	*	*	*	*	*	*
Net income	1.31	1.34	1.42	1.45	1.54	1.32	1.40	1.59	1.59	1.58
Cash dividends declared	.85	1.07	.93	.96	1.16	.94	.96	.99	1.05	.95
Retained income	.46	.26	.48	.50	.38	.38	.44	.60	.54	.63
MEMO: Return on equity	16.84	16.78	17.36	17.38	18.46	15.72	15.79	17.26	17.01	15.56

* In absolute value, less than 0.005 percent.

n.a. Not available. MMDA Money market deposit account. RP Repurchase agreement. CD Certificate of deposit.

1. Includes allocated transfer risk reserves.
2. When possible, based on the average of quarterly balance sheet data reported on schedule RC-K of the quarterly Call Report.
3. Before 1997, large time open accounts included in other time deposits.
4. Includes provisions for allocated transfer risk.

A.1. Portfolio composition, interest rates, and income and expense, all U.S. banks, 1995–2004

D. Banks ranked 101 through 1,000 by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Balance sheet items as a percentage of average net consolidated assets									
Interest-earning assets	90.98	91.11	91.34	91.38	91.68	91.50	91.16	91.36	91.34	91.58
Loans and leases, net	62.24	62.72	62.34	61.23	61.48	62.15	62.46	61.46	61.32	63.34
Commercial and industrial	12.68	12.76	12.38	12.45	12.64	12.95	13.03	12.38	11.51	11.52
U.S. addressees	12.52	12.58	12.14	12.12	12.32	12.60	12.65	12.06	11.20	11.21
Foreign addressees	.16	.18	.23	.32	.32	.36	.38	.31	.31	.31
Consumer	16.39	16.11	14.36	12.56	10.79	10.19	9.76	8.13	6.80	6.34
Credit card	6.45	6.92	5.87	4.78	3.37	3.27	3.61	2.64	1.82	1.92
Installment and other	9.94	9.19	8.49	7.78	7.41	6.92	6.15	5.50	4.97	4.42
Real estate	30.77	31.28	33.10	33.83	35.90	36.93	37.64	38.92	40.96	43.38
In domestic offices	30.75	31.26	33.08	33.81	35.87	36.91	37.62	38.90	40.91	43.32
Construction and land development	2.21	2.38	2.68	2.87	3.48	4.15	4.90	5.40	5.89	6.98
Farmland	.40	.46	.52	.56	.58	.65	.66	.73	.80	.91
One- to four-family residential	17.47	17.29	18.08	18.14	18.26	17.17	16.18	15.39	15.71	15.37
Home equity	2.36	2.30	2.29	2.14	1.99	2.10	2.21	2.51	2.92	3.46
Other	15.11	14.99	15.78	16.00	16.26	15.06	13.97	12.88	12.79	11.90
Multifamily residential	1.21	1.28	1.28	1.25	1.44	1.58	1.69	1.83	2.00	2.24
Nonfarm nonresidential	9.46	9.85	10.52	10.99	12.12	13.36	14.18	15.55	16.51	17.82
In foreign offices	.02	.02	.02	.02	.02	.02	.02	.03	.05	.06
To depository institutions and acceptances of other banks	.36	.50	.59	.52	.46	.37	.38	.37	.37	.25
Foreign governments	.02	.02	.02	.03	.03	.03	.03	.02	.02	.01
Agricultural production	.69	.70	.73	.80	.78	.82	.85	.86	.83	.82
Other loans	1.78	1.67	1.47	1.30	1.25	1.22	1.22	1.18	1.25	1.32
Lease-financing receivables	.90	1.00	.99	.99	.78	.75	.74	.75	.67	.75
LESS: Unearned income on loans	–.12	–.10	–.10	–.09	–.08	–.08	–.07	–.06	–.06	–.06
LESS: Loss reserves[1]	–1.23	–1.23	–1.19	–1.15	–1.06	–1.04	–1.12	–1.10	–1.03	–.98
Securities	23.04	22.61	23.37	24.18	25.17	24.34	22.81	23.86	24.36	23.59
Investment account	22.84	22.49	23.26	24.08	25.09	24.25	22.70	23.80	24.23	23.54
Debt	22.38	21.97	22.65	23.39	24.33	23.46	22.28	23.30	23.79	23.18
U.S. Treasury	6.47	5.59	4.94	3.91	2.53	1.81	1.32	1.22	1.00	1.02
U.S. government agency and corporation obligations	12.21	12.62	13.91	15.08	16.29	15.56	14.70	15.85	16.96	16.70
Government-backed mortgage pools	5.42	5.67	6.20	6.45	6.72	6.22	6.27	6.55	7.03	6.80
Collateralized mortgage obligations	3.55	3.11	3.00	3.21	3.52	3.04	3.08	3.69	3.69	3.41
Other	3.25	3.84	4.71	5.42	6.05	6.30	5.35	5.60	6.24	6.49
State and local government	2.13	2.23	2.43	2.69	2.91	2.91	2.90	2.89	2.95	2.92
Private mortgage-backed securities	.68	.76	.59	.65	1.00	.99	.94	.99	.87	1.08
Other	.89	.76	.78	1.06	1.60	2.19	2.42	2.34	2.01	1.46
Equity	.47	.52	.61	.69	.77	.79	.43	.50	.43	.36
Trading account	.20	.12	.10	.11	.08	.09	.11	.06	.14	.05
Gross federal funds sold and reverse RPs	3.91	3.86	3.59	4.16	3.35	3.40	4.20	4.15	3.85	2.95
Interest-bearing balances at depositories	1.78	1.93	2.05	1.80	1.68	1.60	1.68	1.89	1.81	1.69
Non-interest-earning assets	9.02	8.89	8.66	8.62	8.32	8.50	8.84	8.64	8.66	8.42
Revaluation gains held in trading accounts	.05	.02	*	*	.01	.02	.01	.01	*	*
Other	8.98	8.86	8.66	8.62	8.31	8.49	8.84	8.64	8.65	8.42
Liabilities	91.36	91.06	90.78	90.55	90.90	90.95	90.32	89.93	89.69	89.19
Interest-bearing liabilities	75.02	75.09	75.23	75.45	76.76	77.43	77.01	76.35	75.76	75.00
Deposits	59.59	59.82	61.24	62.20	61.93	62.67	63.10	62.83	61.93	60.79
In foreign offices	1.71	1.33	1.22	1.31	1.20	1.28	1.24	.88	.64	.65
In domestic offices	57.88	58.49	60.02	60.89	60.73	61.40	61.86	61.95	61.29	60.14
Other checkable deposits	8.53	6.19	4.94	4.22	3.75	3.32	3.25	3.32	3.55	3.65
Savings (including MMDAs)	20.72	22.43	23.51	25.57	27.35	27.03	27.67	30.17	31.42	31.65
Small-denomination time deposits	21.08	21.55	21.95	21.15	19.60	19.44	18.79	16.83	15.03	13.45
Large-denomination time deposits	7.55	8.32	9.62	9.96	10.03	11.61	12.14	11.63	11.29	11.39
Gross federal funds purchased and RPs	8.29	8.17	7.06	6.15	6.90	6.30	5.77	5.27	5.35	5.53
Other	7.14	7.10	6.92	7.10	7.92	8.45	8.15	8.25	8.48	8.69
Non-interest-bearing liabilities	16.34	15.96	15.55	15.10	14.15	13.52	13.31	13.58	13.93	14.20
Demand deposits in domestic offices	14.05	13.80	13.11	11.87	10.19	8.97	8.23	8.05	7.97	8.13
Revaluation losses held in trading accounts	.05	.02	.01	.01	.01	*	.01	.01	*	*
Other	2.24	2.14	2.44	3.22	3.95	4.55	5.08	5.52	5.95	6.06
Capital account	8.64	8.94	9.22	9.45	9.10	9.05	9.68	10.07	10.31	10.81
MEMO										
Commercial real estate loans	13.17	13.80	14.72	15.33	17.28	19.32	21.03	23.05	24.62	27.25
Other real estate owned	.17	.13	.11	.09	.08	.07	.08	.10	.11	.10
Managed liabilities	24.71	24.96	24.89	24.65	26.33	28.01	27.75	26.57	26.40	26.98
Federal Home Loan Bank advances	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.27	5.71	6.29	6.46
Average net consolidated assets (billions of dollars)	1,094	1,078	971	938	972	986	1,002	1,022	1,072	1,080

A.1.—Continued

D. Banks ranked 101 through 1,000 by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Effective interest rate (percent)[2]									
Rates earned										
Interest-earning assets	8.44	8.44	8.54	8.38	7.83	8.48	7.86	6.43	5.60	5.46
Taxable equivalent	8.53	8.52	8.63	8.47	7.92	8.56	7.94	6.51	5.68	5.53
Loans and leases, gross	9.45	9.41	9.53	9.42	8.74	9.42	8.76	7.33	6.58	6.26
Net of loss provisions	8.94	8.77	8.79	8.79	8.26	8.75	7.88	6.57	6.02	5.86
Securities	6.24	6.34	6.43	6.31	6.03	6.45	5.97	4.93	3.80	3.77
Taxable equivalent	6.50	6.60	6.69	6.57	6.29	6.71	6.25	5.19	4.05	4.02
Investment account	6.24	6.34	6.43	6.30	6.03	6.45	5.96	4.93	3.82	3.77
U.S. Treasury securities and U.S. government agency obligations (excluding MBS)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.85	4.54	3.42	3.15
Mortgage-backed securities	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	6.33	5.38	3.95	4.01
Other	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.40	4.51	4.07	4.21
Trading account	5.50	5.94	6.37	6.84	7.33	9.30	6.60	3.82	1.67	3.63
Gross federal funds sold and reverse RPs	5.45	5.29	5.42	5.31	4.98	6.15	3.91	1.73	1.27	1.57
Interest-bearing balances at depositories	6.07	5.69	5.44	5.77	5.07	5.76	3.94	1.79	1.26	1.47
Rates paid										
Interest-bearing liabilities	4.64	4.58	4.67	4.60	4.19	4.93	4.11	2.54	1.88	1.73
Interest-bearing deposits	4.26	4.27	4.34	4.28	3.84	4.46	3.82	2.28	1.61	1.44
In foreign offices	5.94	5.72	5.42	5.55	5.07	6.13	4.45	2.14	1.43	1.43
In domestic offices	4.21	4.23	4.32	4.25	3.82	4.43	3.81	2.28	1.61	1.44
Other checkable deposits	2.02	1.96	2.17	2.15	1.99	2.27	1.81	1.06	.74	.72
Savings (including MMDAs)	3.24	3.11	3.08	2.96	2.65	3.07	2.22	1.17	.76	.74
Large time deposits[3]	5.62	5.48	5.56	5.51	5.17	6.00	5.27	3.34	2.58	2.33
Other time deposits[3]	5.53	5.57	5.57	5.64	5.11	5.74	5.51	3.77	2.86	2.51
Gross federal funds purchased and RPs	5.61	5.16	5.20	5.14	4.82	5.95	3.83	1.83	1.29	1.45
Other interest-bearing liabilities	6.28	5.90	6.08	5.99	5.36	6.45	5.41	4.17	3.60	3.37
	Income and expense as a percentage of average net consolidated assets									
Gross interest income	7.70	7.70	7.79	7.66	7.19	7.79	7.16	5.85	5.08	4.99
Taxable equivalent	7.78	7.78	7.87	7.74	7.27	7.86	7.24	5.93	5.16	5.06
Loans	6.00	6.01	6.05	5.89	5.47	5.96	5.59	4.58	4.08	4.02
Securities	1.42	1.42	1.49	1.50	1.51	1.58	1.33	1.15	.91	.88
Gross federal funds sold and reverse RPs	.21	.20	.19	.22	.17	.21	.16	.07	.05	.05
Other	.07	.06	.06	.06	.04	.04	.08	.05	.05	.04
Gross interest expense	3.46	3.41	3.47	3.45	3.20	3.79	3.14	1.92	1.41	1.29
Deposits	2.55	2.57	2.69	2.70	2.44	2.87	2.48	1.49	1.04	.92
Gross federal funds purchased and RPs	.46	.43	.37	.32	.34	.38	.22	.09	.07	.08
Other	.45	.42	.42	.42	.42	.54	.44	.34	.30	.29
Net interest income	4.24	4.29	4.32	4.22	3.99	4.00	4.02	3.93	3.68	3.70
Taxable equivalent	4.32	4.37	4.39	4.29	4.07	4.07	4.10	4.00	3.75	3.77
Loss provisioning[4]	.43	.52	.58	.49	.39	.52	.65	.55	.41	.31
Non-interest income	1.84	1.88	2.07	2.26	2.31	2.35	2.37	2.37	2.31	2.27
Service charges on deposits	.42	.41	.40	.39	.38	.36	.39	.41	.41	.39
Fiduciary activities	.27	.29	.32	.37	.38	.44	.40	.35	.34	.37
Trading revenue	.03	.02	.01	.02	.02	.01	*	*	.01	.01
Interest rate exposures	n.a.	.01	.01	.01	.01	.01	−.01	*	.01	.01
Foreign exchange rate exposures	n.a.	.01	*	*	*	*	*	*	*	*
Other commodity and equity exposures	n.a.	*	*	*	*	*	*	*	*	*
Other	1.12	1.16	1.34	1.49	1.53	1.55	1.58	1.61	1.55	1.50
Non-interest expense	3.68	3.69	3.73	3.86	3.70	3.84	3.88	3.73	3.60	3.54
Salaries, wages, and employee benefits	1.44	1.44	1.50	1.56	1.56	1.59	1.61	1.64	1.64	1.64
Occupancy	.45	.45	.46	.47	.47	.47	.46	.45	.43	.43
Other	1.79	1.80	1.77	1.83	1.68	1.78	1.81	1.64	1.53	1.48
Net non-interest expense	1.84	1.81	1.66	1.60	1.39	1.48	1.52	1.36	1.29	1.28
Gains on investment account securities	−.01	.02	.02	.04	−.01	−.04	.05	.04	.05	.02
Income before taxes and extraordinary items	1.96	1.98	2.10	2.16	2.20	1.96	1.90	2.06	2.03	2.13
Taxes	.68	.69	.73	.74	.74	.67	.66	.67	.66	.69
Extraordinary items, net of income taxes	*	*	*	.06	.01	*	.01	*	.03	*
Net income	1.28	1.29	1.37	1.47	1.47	1.29	1.25	1.39	1.40	1.45
Cash dividends declared	.87	1.04	1.10	1.01	1.06	.92	1.33	1.19	1.64	.78
Retained income	.41	.25	.28	.46	.40	.37	−.08	.19	−.25	.67
MEMO: Return on equity	14.82	14.42	14.89	15.60	16.11	14.21	12.93	13.75	13.54	13.39

* In absolute value, less than 0.005 percent.

n.a. Not available. MMDA Money market deposit account. RP Repurchase agreement. CD Certificate of deposit.

1. Includes allocated transfer risk reserves.
2. When possible, based on the average of quarterly balance sheet data reported on schedule RC-K of the quarterly Call Report.
3. Before 1997, large time open accounts included in other time deposits.
4. Includes provisions for allocated transfer risk.

A.1. Portfolio composition, interest rates, and income and expense, all U.S. banks, 1995–2004

E. Banks not ranked among the 1,000 largest by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Balance sheet items as a percentage of average net consolidated assets									
Interest-earning assets	92.48	92.45	92.45	92.64	92.55	92.52	92.26	92.22	92.13	92.34
Loans and leases, net	56.60	57.38	58.76	59.11	59.76	62.31	62.67	62.72	62.33	63.81
Commercial and industrial	9.65	9.98	10.16	10.33	10.64	11.09	11.10	10.71	10.42	10.29
U.S. addressees	9.59	9.91	10.08	10.25	10.55	11.02	11.02	10.64	10.37	10.25
Foreign addressees	*.06*	*.07*	*.08*	*.08*	*.08*	*.07*	*.08*	*.06*	*.05*	*.04*
Consumer	9.54	9.42	8.98	8.46	8.16	7.98	7.42	6.76	6.16	5.45
Credit card	1.01	1.04	.85	.70	.69	.59	.57	.49	.51	.40
Installment and other	8.53	8.39	8.14	7.76	7.47	7.39	6.85	6.28	5.64	5.05
Real estate	33.54	34.10	35.55	36.04	36.84	39.29	40.30	41.52	42.32	44.76
In domestic offices	33.54	34.10	35.55	36.04	36.83	39.29	40.30	41.52	42.31	44.76
Construction and land development	2.38	2.61	2.82	3.02	3.28	3.70	4.23	4.51	4.99	6.00
Farmland	2.48	2.55	2.69	2.83	2.95	3.06	3.04	3.08	3.12	3.22
One- to four-family residential	17.45	17.47	18.16	18.04	17.66	18.43	18.25	17.91	17.10	17.20
Home equity	1.20	1.20	1.24	1.21	1.17	1.28	1.37	1.62	1.80	2.12
Other	16.25	16.28	16.92	16.83	16.49	17.15	16.87	16.29	15.30	15.08
Multifamily residential	.95	.92	.95	.93	.98	1.04	1.06	1.16	1.28	1.41
Nonfarm nonresidential	10.28	10.54	10.93	11.22	11.96	13.06	13.71	14.86	15.82	16.93
In foreign offices	*	*	*	*	*	*	*	*	*	*
To depository institutions and acceptances of other banks	.19	.21	.20	.14	.14	.12	.12	.10	.09	.07
Foreign governments	*	*	*	*	.01	.01	*	*	*	*
Agricultural production	3.95	3.92	4.05	4.27	4.06	3.85	3.76	3.64	3.39	3.26
Other loans	.72	.69	.67	.67	.67	.69	.67	.65	.66	.68
Lease-financing receivables	.22	.23	.25	.24	.26	.27	.27	.31	.26	.25
LESS: Unearned income on loans	−.30	−.27	−.24	−.20	−.15	−.11	−.09	−.07	−.06	−.06
LESS: Loss reserves[1]	−.93	−.90	−.87	−.86	−.87	−.88	−.88	−.90	−.92	−.89
Securities	30.52	29.53	28.24	26.70	26.91	25.40	22.80	23.34	23.46	23.33
Investment account	30.48	29.50	28.21	26.66	26.88	25.38	22.79	23.33	23.43	23.32
Debt	30.03	29.01	27.69	26.12	26.34	24.82	22.49	23.05	23.11	23.06
U.S. Treasury	9.19	7.85	6.70	5.05	3.34	2.12	1.33	1.04	.90	.81
U.S. government agency and corporation obligations	15.13	15.67	15.58	15.43	16.89	16.95	15.27	16.07	16.22	16.56
Government-backed mortgage pools	4.19	4.21	4.01	3.90	3.95	3.47	3.78	4.54	4.84	4.75
Collateralized mortgage obligations	2.76	2.46	2.19	2.02	2.00	1.70	1.94	2.30	2.20	1.96
Other	8.18	9.00	9.38	9.51	10.93	11.78	9.56	9.23	9.18	9.85
State and local government	4.69	4.62	4.60	4.80	4.96	4.64	4.51	4.56	4.73	4.67
Private mortgage-backed securities	.20	.18	.20	.16	.26	.23	.27	.26	.21	.19
Other	.81	.68	.61	.68	.89	.88	1.11	1.12	1.05	.83
Equity	.45	.49	.52	.54	.53	.56	.30	.27	.31	.26
Trading account	.03	.03	.03	.04	.03	.02	.01	.01	.03	.01
Gross federal funds sold and reverse RPs	3.91	4.04	3.95	5.12	4.17	3.22	5.01	4.26	4.26	3.33
Interest-bearing balances at depositories	1.45	1.51	1.49	1.72	1.71	1.59	1.77	1.89	2.08	1.86
Non-interest-earning assets	7.52	7.55	7.55	7.36	7.45	7.48	7.74	7.78	7.87	7.66
Revaluation gains held in trading accounts	*	*	*	*	*	*	*	*	*	*
Other	7.52	7.55	7.55	7.36	7.45	7.48	7.74	7.78	7.87	7.66
Liabilities	90.04	89.82	89.63	89.54	89.75	89.88	89.59	89.72	89.58	89.55
Interest-bearing liabilities	75.74	75.58	75.47	75.35	75.89	76.04	76.00	76.01	75.47	75.22
Deposits	72.69	72.47	72.06	71.77	71.40	70.53	70.93	70.50	69.82	68.87
In foreign offices	.11	.10	.09	.07	.07	.05	.06	.06	.05	.07
In domestic offices	72.58	72.37	71.97	71.70	71.33	70.48	70.88	70.44	69.77	68.80
Other checkable deposits	12.37	11.75	11.39	11.18	11.07	10.57	10.19	10.42	10.60	10.59
Savings (including MMDAs)	20.41	19.58	18.98	19.01	19.69	19.03	19.13	20.99	22.00	22.71
Small-denomination time deposits	30.91	31.28	31.09	30.42	29.07	28.41	28.07	25.90	24.20	22.46
Large-denomination time deposits	8.89	9.76	10.50	11.10	11.50	12.47	13.48	13.13	12.97	13.04
Gross federal funds purchased and RPs	1.79	1.71	1.67	1.49	1.79	2.06	1.55	1.51	1.52	1.76
Other	1.26	1.41	1.75	2.09	2.71	3.45	3.51	4.00	4.13	4.59
Non-interest-bearing liabilities	14.30	14.23	14.16	14.19	13.86	13.84	13.59	13.71	14.11	14.33
Demand deposits in domestic offices	13.23	13.13	13.09	13.08	12.80	12.64	12.16	12.24	12.58	12.77
Revaluation losses held in trading accounts	*	*	*	*	*	*	*	*	*	*
Other	1.07	1.10	1.06	1.10	1.06	1.20	1.44	1.47	1.53	1.55
Capital account	9.96	10.18	10.37	10.46	10.25	10.12	10.41	10.27	10.42	10.45
MEMO										
Commercial real estate loans	13.72	14.18	14.80	15.27	16.33	17.91	19.15	20.67	22.23	24.50
Other real estate owned	.25	.20	.16	.13	.11	.11	.12	.14	.15	.14
Managed liabilities	12.06	12.99	14.02	14.76	16.09	18.08	18.67	18.79	18.78	19.57
Federal Home Loan Bank advances	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	3.34	3.71	3.87	4.33
Average net consolidated assets (billions of dollars)	666	661	647	644	651	655	675	704	742	769

A.1.—Continued

E. Banks not ranked among the 1,000 largest by assets

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Effective interest rate (percent)[2]									
Rates earned										
Interest-earning assets	8.39	8.37	8.50	8.35	8.05	8.44	7.94	6.79	5.94	5.73
Taxable equivalent	8.53	8.50	8.63	8.48	8.18	8.56	8.05	6.91	6.05	5.84
Loans and leases, gross	9.80	9.75	9.80	9.69	9.28	9.51	9.03	7.84	7.08	6.72
Net of loss provisions	9.54	9.47	9.49	9.34	8.89	9.14	8.59	7.39	6.72	6.45
Securities	6.10	6.14	6.26	6.04	5.88	6.15	5.86	5.02	3.86	3.73
Taxable equivalent	6.49	6.52	6.65	6.46	6.29	6.54	6.28	5.43	4.26	4.11
Investment account	6.10	6.14	6.26	6.04	5.89	6.15	5.86	5.02	3.87	3.73
U.S. Treasury securities and U.S. government agency obligations (excluding MBS)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.97	4.80	3.74	3.39
Mortgage-backed securities	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	6.20	5.47	3.58	3.90
Other	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5.29	4.87	4.43	4.18
Trading account	6.07	6.47	6.33	5.26	3.60	4.01	6.43	4.80	.66	7.23
Gross federal funds sold and reverse RPs	5.95	5.34	5.51	5.36	4.96	6.25	3.83	1.63	1.08	1.32
Interest-bearing balances at depositories	5.88	5.63	5.62	5.67	5.69	6.38	4.56	2.68	1.96	2.03
Rates paid										
Interest-bearing liabilities	4.46	4.49	4.61	4.60	4.28	4.80	4.40	2.92	2.13	1.87
Interest-bearing deposits	4.39	4.44	4.54	4.53	4.22	4.67	4.32	2.78	2.02	1.75
In foreign offices	5.73	5.34	4.77	5.08	4.34	5.13	3.97	1.67	.85	1.04
In domestic offices	4.39	4.44	4.53	4.53	4.22	4.67	4.32	2.79	2.02	1.75
Other checkable deposits	2.50	2.41	2.46	2.44	2.28	2.47	1.97	1.16	.78	.70
Savings (including MMDAs)	3.32	3.26	3.36	3.39	3.21	3.56	2.81	1.72	1.13	1.04
Large time deposits[3]	5.55	5.48	5.53	5.53	5.21	5.89	5.53	3.61	2.78	2.47
Other time deposits[3]	5.51	5.61	5.66	5.63	5.25	5.70	5.60	3.88	2.96	2.55
Gross federal funds purchased and RPs	5.61	5.11	5.22	4.99	4.73	5.69	3.92	1.84	1.31	1.44
Other interest-bearing liabilities	6.45	5.77	6.32	6.45	5.64	6.24	5.74	5.32	4.06	3.67
	Income and expense as a percentage of average net consolidated assets									
Gross interest income	7.78	7.77	7.90	7.75	7.48	7.83	7.35	6.31	5.46	5.32
Taxable equivalent	7.91	7.89	8.02	7.87	7.60	7.95	7.45	6.41	5.56	5.42
Loans	5.63	5.68	5.86	5.80	5.62	5.99	5.75	5.02	4.47	4.35
Securities	1.86	1.80	1.76	1.59	1.58	1.57	1.32	1.16	.89	.87
Gross federal funds sold and reverse RPs	.25	.24	.24	.29	.22	.21	.20	.07	.05	.05
Other	.04	.04	.04	.06	.06	.05	.08	.06	.05	.05
Gross interest expense	3.37	3.39	3.48	3.46	3.26	3.64	3.34	2.22	1.60	1.41
Deposits	3.19	3.22	3.28	3.25	3.02	3.30	3.08	1.98	1.42	1.22
Gross federal funds purchased and RPs	.10	.08	.08	.07	.08	.12	.06	.03	.02	.02
Other	.08	.08	.11	.13	.15	.21	.20	.21	.17	.17
Net interest income	4.41	4.38	4.42	4.28	4.22	4.20	4.01	4.08	3.86	3.91
Taxable equivalent	4.54	4.50	4.54	4.41	4.35	4.31	4.12	4.19	3.96	4.01
Loss provisioning[4]	.24	.25	.27	.29	.31	.32	.36	.35	.29	.23
Non-interest income	1.38	1.42	1.41	1.52	1.44	1.32	1.31	1.39	1.47	1.39
Service charges on deposits	.44	.44	.44	.42	.42	.43	.44	.45	.43	.43
Fiduciary activities	.22	.19	.20	.23	.26	.21	.25	.27	.28	.32
Trading revenue	.01	*	*	*	*	.01	*	*	*	*
Interest rate exposures	n.a.	*	*	*	*	*	*	*	*	*
Foreign exchange rate exposures	n.a.	*	*	*	*	*	*	*	*	*
Other commodity and equity exposures	n.a.	*	*	*	*	*	*	*	*	*
Other	.71	.79	.77	.86	.75	.68	.62	.67	.76	.64
Non-interest expense	3.80	3.70	3.69	3.74	3.73	3.58	3.55	3.57	3.56	3.52
Salaries, wages, and employee benefits	1.79	1.77	1.80	1.82	1.82	1.78	1.79	1.82	1.82	1.81
Occupancy	.50	.49	.49	.49	.49	.47	.47	.46	.45	.45
Other	1.51	1.44	1.40	1.43	1.42	1.32	1.29	1.28	1.28	1.27
Net non-interest expense	2.42	2.28	2.28	2.23	2.29	2.26	2.24	2.18	2.09	2.14
Gains on investment account securities	*	.01	.01	.02	*	−.01	.04	.05	.04	.02
Income before taxes and extraordinary items	1.75	1.85	1.89	1.79	1.62	1.61	1.45	1.60	1.53	1.56
Taxes	.55	.59	.59	.53	.47	.45	.39	.41	.38	.38
Extraordinary items, net of income taxes	*	*	*	*	*	*	*	−.01	*	*
Net income	1.20	1.26	1.30	1.26	1.15	1.17	1.06	1.18	1.14	1.18
Cash dividends declared	.62	.64	.74	.82	.70	.79	.64	.68	.67	.64
Retained income	.58	.62	.56	.44	.45	.38	.42	.50	.47	.54
MEMO: Return on equity	12.05	12.37	12.53	12.02	11.26	11.52	10.16	11.47	10.97	11.29

* In absolute value, less than 0.005 percent.

n.a. Not available. MMDA Money market deposit account. RP Repurchase agreement. CD Certificate of deposit.

1. Includes allocated transfer risk reserves.
2. When possible, based on the average of quarterly balance sheet data reported on schedule RC-K of the quarterly Call Report.
3. Before 1997, large time open accounts included in other time deposits.
4. Includes provisions for allocated transfer risk.

A.2. Report of income, all U.S. banks, 1995–2004

Millions of dollars

Item	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Gross interest income	302,530	313,696	338,865	359,675	366,137	423,839	404,606	350,091	329,770	350,041
Taxable equivalent	305,166	316,156	341,298	362,140	368,764	426,476	407,288	352,838	332,553	353,029
Loans	227,376	239,850	256,141	271,441	278,537	326,800	311,876	269,942	258,158	269,746
Securities	51,029	50,631	52,660	56,598	62,116	67,665	63,086	59,316	53,315	58,583
Gross federal funds sold and reverse repurchase agreements	9,744	9,272	13,658	14,999	12,330	13,546	12,649	6,223	5,122	5,245
Other	14,382	13,944	16,406	16,637	13,155	15,829	16,994	14,610	13,175	16,467
Gross interest expense	148,010	150,249	164,692	178,161	174,946	222,159	188,824	118,915	94,462	99,245
Deposits	105,326	107,512	117,350	125,217	119,665	151,145	132,390	81,894	62,744	63,986
Gross federal funds purchased and repurchase agreements	18,424	16,780	20,439	22,182	21,130	26,860	19,590	9,919	7,590	9,203
Other	24,259	25,956	26,903	30,760	34,149	44,155	36,841	27,101	24,128	26,055
Net interest income	154,520	163,447	174,173	181,514	191,191	201,680	215,782	231,176	235,308	250,796
Taxable equivalent	157,156	165,907	176,606	183,979	193,818	204,317	218,464	233,923	238,091	253,784
Loss provisioning	12,667	16,395	19,402	21,427	21,186	29,386	43,238	45,298	32,790	23,996
Non-interest income	83,850	95,313	105,640	123,668	144,429	153,163	160,298	168,543	183,586	188,391
Service charges on deposits	16,056	17,050	18,558	19,769	21,497	23,719	26,873	29,631	31,693	33,457
Fiduciary activities	12,889	14,296	16,584	19,268	20,502	22,220	21,989	21,637	22,455	25,101
Trading revenue	6,337	7,525	8,018	7,693	10,429	12,235	12,547	10,735	11,446	9,956
Other	48,568	56,444	62,480	76,939	92,001	94,988	98,889	106,541	117,991	119,877
Non-interest expense	151,162	162,581	171,060	193,833	204,632	216,432	226,057	230,315	243,299	263,400
Salaries, wages, and employee benefits	64,017	67,826	72,346	79,538	86,151	89,036	94,239	100,485	108,469	115,305
Occupancy	19,761	20,892	22,080	24,164	25,865	26,765	27,944	29,317	31,319	33,257
Other	67,384	73,865	76,634	90,129	92,616	100,631	103,875	100,514	103,510	114,838
Net non-interest expense	67,312	67,268	65,420	70,165	60,203	63,269	65,759	61,772	59,713	75,009
Gains on investment account securities	481	1,123	1,825	3,090	250	–2,280	4,625	6,415	5,633	3,822
Income before taxes	75,024	80,908	91,177	93,016	110,055	106,744	111,411	130,521	148,438	155,614
Taxes	26,241	28,447	32,001	31,965	39,211	37,250	37,105	42,980	48,450	49,887
Extraordinary items, net of income taxes	28	88	56	506	169	–31	–324	–78	427	63
Net income	48,812	52,550	59,230	61,556	71,012	69,463	73,980	87,464	100,416	105,791
Cash dividends declared	31,106	39,419	42,801	41,205	52,101	52,547	54,844	67,231	77,757	59,585
Retained income	17,706	13,131	16,430	20,351	18,912	16,916	19,137	20,232	22,659	46,206

Background on FOMC Meeting Minutes

Deborah J. Danker and Matthew M. Luecke, of the Board's Division of Monetary Affairs, prepared this article.

On December 14, 2004, the Federal Open Market Committee (FOMC) decided to move up the publication of its minutes to three weeks after the end of each meeting. That action has cut in half the average time between the meeting and publication of the minutes. It has also apparently heightened public attention to the FOMC minutes. To give additional context to the Committee's decision, this article outlines previous changes to the release schedule for the minutes and provides a brief overview of the content of the minutes and the way they are now produced.

From the inception of the FOMC, the Federal Reserve has had an obligation to maintain records of the Committee's policymaking actions and to publish those records in its annual report to the Congress.[1] Accordingly, the Federal Reserve initially published a summary of FOMC proceedings once a year. Over time, however, as views about public access to information changed and as financial markets matured, broadened, and deepened, the FOMC provided more information more promptly, going well beyond the basic information required by the Federal Reserve Act.

This article focuses on the minutes and their production, but the minutes are by no means the sole source of public information about FOMC policymaking. For example, the Committee releases a statement on the same day that policy decisions are made, the Chairman provides semiannual testimony to the Congress, and the Board submits semiannual Monetary Policy Reports, which include a summary of the economic projections of the Board members and Reserve Bank presidents. In addition, the Chairman testifies on the economy and other topics on several occasions during the year; Committee members regularly give public speeches; and a wide range of documents, including FOMC meeting transcripts, is made available after a five-year lag.

HISTORY

The Federal Open Market Committee was created in its modern form by the Banking Act of 1935, and for much of its history, the publicly available reports from its meetings were the "Records of Policy Actions"—also known as the "Policy Record." (See timeline chart of past and present nomenclature.) For its own use, the Committee initially maintained extensive "minutes," which were detailed records of attendance, discussions, and decisions at each meeting. These minutes remained confidential, and the Records of Policy Actions, which were published once a year, were the official statement of FOMC policymaking for decades.[2] At first, the Records of Policy Actions included only a paragraph or two of background or reasoning behind each action. However, these records grew over time and had reached an average of about five pages per meeting by the mid-1960s, when the Committee reviewed its information-disclosure practices.

1967—Release of Record of Policy Actions after Ninety Days

In discussions undertaken in light of the pending effective date of the Freedom of Information Act, the Committee agreed that information about monetary policy decisions should be made available to the public on a timely basis but that caution was needed so that the information released would not impair the Committee's ability to formulate and implement policy. The consensus that emerged was that the time lag on the release of information should be shortened.

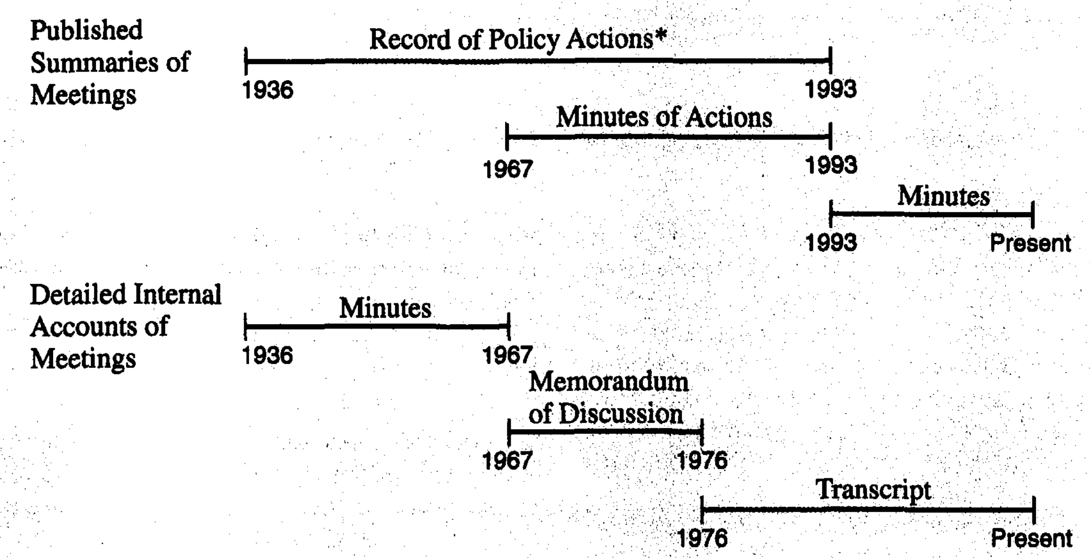
Accordingly, in June 1967, the Committee announced that it would release the Record of Policy Actions about ninety days after each meeting and

NOTE. The authors are grateful for helpful comments received, especially from their former colleagues Normand Bernard and David Lindsey.

1. Section 10, paragraph 10 of the Federal Reserve Act states: "The Board of Governors of the Federal Reserve System shall keep a complete record of the action taken by the Board and by the Federal Open Market Committee upon all questions of policy relating to open-market operations and shall record therein the votes taken in connection with the determination of open-market policies and the reasons underlying the action of the Board and the Committee in each instance. The Board shall . . . include in its annual report to the Congress . . . a copy of the records required to be kept under the provisions of this paragraph."

2. In 1964, the FOMC made the minutes for the years 1936–60 available to the public through the National Archives.

Reports from FOMC Meetings: Past and Present Nomenclature



*Also referred to as "Policy Record."

would also publish it in the *Federal Reserve Bulletin.* The Committee believed that a ninety-day lag would be a relatively safe starting point and that, as experience was gained, it might be possible to reduce the lag between policy action and publication.

The Committee also began to make available on the same schedule a new document—a companion piece to the Record of Policy Actions—that was called "Minutes of Actions." This document included summaries of all actions (both policy actions and nonpolicy actions, such as procedural or organizational votes) as well as a list of attendees. The document did not state the reasoning behind the actions or give any indication of the discussion at the meeting; that information was covered in the Record of Policy Actions. The material previously included in the FOMC's internal minutes was now in effect split into two documents—the Minutes of Actions and the "Memorandum of Discussion," a detailed account of the discussion at each meeting. Subsequently, the Committee began releasing its internal minutes, and later the Memorandum of Discussion, to the public with a lag of about five years.[3]

3. In 1967, the Committee sent the internal minutes for 1961 to the National Archives. In 1970, it transmitted those for 1962–65 and decided on a regular schedule of releasing them after about five years.

1975—Release of Record of Policy Actions after Forty-Five Days

In the years after the passage of the Freedom of Information Act, it became clear that there was a substantial public appetite for further and more-timely information related to the Committee's meetings. Committee discussions about the schedule and content of existing information releases resulted in a decision to cut the lag on the release of the Record of Policy Actions from ninety days to forty-five days. The March 1975 announcement about shortening the release lag time noted that "in the light of experience, the Committee decided that a delay as long as 90 days was no longer necessary to avoid an unacceptable degree of risk that speculators would be able to take unfair advantage of the information or that market reactions would impair the effectiveness of the Committee's functions."

1976—Earlier Release of Lengthened Record of Policy Actions

In May 1976, the Committee announced that an expanded version of the Record of Policy Actions for each meeting would be released a few days after the subsequent meeting.[4] Because the Committee was meeting monthly at that point, the lag shortened to an average of just over thirty days.[5] The expanded document, which was approximately doubled in length, included a fuller discussion of economic and financial developments and more information on members' views on current and longer-run policy issues. At the same time, the Committee decided that continued production of the Memorandum of Discussion was no longer merited.

1993—Combination of the Record of Policy Actions and Minutes of Actions

Congressional interest in FOMC information disclosure picked up substantially in the early 1990s. To dispel some confusion that arose in the midst of discussions with the Congress about information release and to simplify its procedures, the Committee decided to combine the content of the Record of Policy Actions and that of the Minutes of Action into a single document called the "Minutes of the FOMC Meeting." Also, the Committee agreed to construct lightly edited transcripts of its previous meetings from unedited transcripts dating back to 1976, which would be released to the public with a lag of about five years.[6] In early 1995, the Committee decided to follow the same publication practice for future transcripts as well.

2004—Release of the Minutes after Three Weeks

In December 2004, the Committee announced that it would expedite the release of the minutes of its meetings to three weeks after each meeting, a reduction of between two and five weeks in the lag (the previous release schedule had depended on the timing of the subsequent meeting, which could vary by several weeks). In support of this decision, participants at that FOMC meeting noted that the minutes contained a more complete and more nuanced explanation of the reasons for the Committee's decisions and views of the risks to the outlook than was possible to include in the post-meeting announcement. They also noted that the earlier release would help markets interpret economic developments and predict the course of interest rates and that the minutes would provide a more up-to-date context for public remarks by individual policymakers. Some concern was expressed, however, that the financial markets could misinterpret the minutes and that the specter of early release could either impair the discussion at FOMC meetings or lead to less-comprehensive, and therefore less-useful, minutes over time. On balance, the Committee viewed the pluses as outweighing the minuses and decided unanimously to expedite the release of the minutes.

CONTENT

The FOMC expressed its views on the content of the minutes years ago when it said that the document "contains a full and accurate report of all matters of policy discussed and views presented, clearly sets forth all policy actions taken by the FOMC and the reasons therefor, and includes the votes by individual members on each policy action."[7] In practice, this means that the minutes cover all policy-related topics that receive a significant amount of attention at the meeting and they record the policy decisions and the reasoning supporting those decisions. All policy votes are recorded. If there is a dissent, the reason for the dissent as expressed at the meeting is included in the minutes. All attendees at the meeting are named and identified by title and affiliation. Because the objective of the minutes is to provide a fair, accurate, and complete record of the FOMC meeting, only information that was available at the time of the meeting is reflected in the content of the minutes, and only opinions that were expressed at the meeting are included. Subsequent information—such as a market reaction to the post-meeting statement, new economic data, or any notation votes or unscheduled FOMC meetings that might occur before the publication date of the minutes—would not be included in the minutes for that meeting; it would be reflected in the minutes of the next regularly scheduled meeting.

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4. In practice, this decision meant that the minutes were released on the Friday after the next meeting. They continued to be released on that schedule until early 1997, when the release was shifted to the Thursday after the next meeting.

5. In 1981, when the FOMC cut its meeting schedule back to eight regularly scheduled meetings each year, the lag on releasing the policy record lengthened concomitantly: "A few days after the subsequent meeting" came to mean a publication date that was once again about forty-five days, on average, after the meeting.

6. To date, transcripts for 1979–99 have been released; 1976–78 are pending.

7. From the March 10, 1977, FOMC—Statements of Policy, which is available in the *Federal Reserve Regulatory Service*, vol. 4, loc. no. 8–830. That statement referred specifically to the Record of Policy Actions, which at the time was the functional equivalent of the current minutes.

Conventions of Language

The minutes try to convey clearly the content of the meeting through commonly used language. At times, the minutes use specific terms in the interest of precision. For example, the minutes distinguish among the terms "members," "meeting participants," and "staff." "Members" refers only to the twelve members of the FOMC—namely, the individuals eligible to vote at that meeting—whereas "meeting participants" includes both the members and the seven nonvoting Reserve Bank presidents (or those attending in their stead). The views of all meeting participants are included in the discussion of current economic conditions and the outlook. When it comes to the description of the policy discussion (usually the final few paragraphs of the minutes), however, the views of the twelve members are the focus. This focus reflects the intention of this section, which is to provide the specific reasons underlying the policy action decided upon by those voting at the meeting. Comments by other meeting participants may be mentioned by way of background in this section when it is felt that they provide important context for the policy discussion, but such comments would not be attributed to members.

To give an indication of how widely expressed a particular view is at a meeting, the minutes use common quantitative wording: "all," "most," "many," "several," "few," or "one," in descending order. Often, other similar words are used for stylistic purposes, and care should be used by readers to avoid over-interpreting specific wording. Moreover, tracking expressions of support for particular viewpoints in the give-and-take of a meeting tends to be an imprecise science. For example, a meeting participant speaking relatively late in a meeting may choose not to repeat views expressed earlier by others, or speakers may alter or amend their views in the course of the meeting. Therefore, these quantitative words should be read as indicative rather than definitive.

Document Structure

The minutes follow a structure that is fairly consistent from one meeting to the next. The initial section includes a list of attendees and any noteworthy organizational or procedural items. For the FOMC's annual organizational meeting, this initial section is appreciably longer because it also includes the election of Committee officers and the approval of various Committee documents.

The second section of the minutes follows a more-or-less standard format in presenting an overview of the economic and financial information provided to the Committee. This section ends with a summary of the staff forecast at the time of the meeting. In the case of the two-day meetings, during which the Committee discusses a special topic, the opening paragraphs of this section typically summarize the staff presentation and the Committee discussion of the special topic.

The third section covers meeting participants' perspectives on current economic developments and the outlook. The structure of this section is less standard because it depends upon the focus of the discussion. Nevertheless, the section typically includes paragraphs on such topics as business investment, consumer spending, the labor market, the external sector, and inflation. For the two-day meetings, the third section tends to be longer, in part because the minutes cover participants' projections for the economy.

The fourth section of the minutes focuses directly on the policy decision. It includes a few paragraphs covering members' views on policy and any discussion of the post-meeting statement. It also records the vote, including the language that the Committee voted on and the vote of each member by name. The minutes then conclude with confirmation of the date for the FOMC's next scheduled meeting.

A record of any notation votes that occurred during the period between regularly scheduled meetings would be included at the end of the minutes of the later meeting, as would the minutes of any unscheduled FOMC meetings, such as conference calls, that occurred during that period.

PROCESS

The minutes of each FOMC meeting are now prepared on an accelerated timetable in order for the document to be approved by the Committee and published on time, twenty-one days after the end of the meeting. An internal experiment covering most of the 2004 FOMC meetings preceded the decision to expedite the release, and that experiment was an essential element in providing the Committee with the necessary confidence that the shortened schedule could be met reliably.

Staff Draft

The minutes are drafted by staff members of the Board of Governors who attend the FOMC meeting. But the process of producing the minutes begins even before the meeting, as the standard staff summaries of the economic and financial situation (for example, the Greenbook and the Bluebook) prepared for each meeting become available a few days ahead of the meeting. A Board staff member uses those summaries, along with the staff presentations prepared for the FOMC meeting and other input, to draft the section of the minutes that reviews the information provided to the Committee. Shortly after the meeting, a draft of this section is completed, and several senior staff members review it for accuracy and pass it on to be incorporated with the other sections.

The writing of the third and fourth sections of the minutes, which cover the discussion of the economic outlook and the policy decision, begins as soon as the meeting ends. Several senior staff members gather and discuss major themes from the meeting and the way they will be covered in the minutes. The author of these sections, an officer from the Board's Division of Monetary Affairs serving on a rotating basis, begins a draft based initially on notes taken at the meeting. By the day after the meeting, however, a rough transcript of the meeting has been prepared, and the author typically relies on the transcript to complete the draft. By the end of the week of the meeting, a draft that includes all sections of the minutes is circulated among the officers in the Division of Monetary Affairs for review.

Policymaker Review

A series of several rounds of policymaker review of the draft minutes begins during the week after the meeting. After the minutes have been reviewed by the Chairman, the Secretary of the FOMC sends the draft to the meeting participants for comments late in the week after the FOMC meeting (typically on Thursday of that week, or nine days after a Tuesday meeting). Early in the subsequent week, the Secretary sends out a revised draft that incorporates input received from meeting participants. By the end of the second week after the meeting, a final version is produced and provided to the Committee for approval by a notation vote. The notation voting period lasts about four calendar days and closes at noon on the day before publication. After the processes of preparation and coordination for the release of the minutes are completed, the approved minutes are published at 2:00 p.m., twenty-one days after the policy decision was made.

This shortened schedule for release has required the Federal Reserve to devote additional resources to produce the minutes. A wider circle of drafters is engaged to ensure that the deadline is met, and logistics are closely coordinated to ensure that policymakers are available for timely review and approval of the minutes. The Committee believed that the costs and risks associated with the new schedule were outweighed by the benefits of additional policy transparency and openness. As such, the earlier release of the minutes was viewed as consistent with the evolution of the FOMC's communication strategy over the years. □

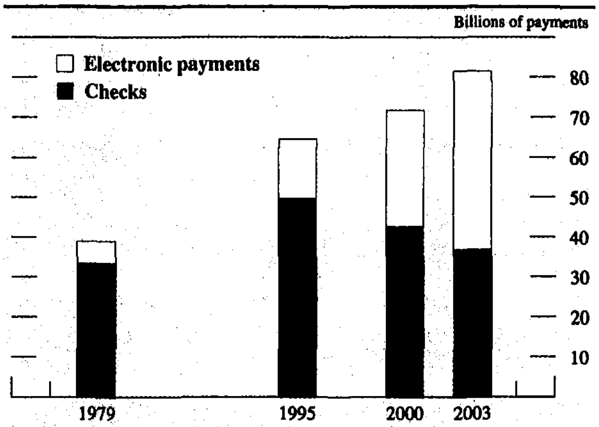
Trends in the Use of Payment Instruments in the United States

Geoffrey R. Gerdes and Jack K. Walton II, of the Board's Division of Reserve Bank Operations and Payment Systems, and May X. Liu and Darrel W. Parke, of the Board's Division of Research and Statistics, prepared this article. Namirembe Mukasa, of the Board's Division of Reserve Bank Operations and Payment Systems, provided research assistance.

An efficient payments system is important for the smooth functioning of the large and complex U.S. economy. As the availability and use of technology evolves, the payments system adapts to the changing needs and expectations of individuals, businesses, and governments. In the United States, many payments traditionally made with paper instruments—checks and cash—are now being made electronically—with debit or credit cards or via the automated clearinghouse (ACH).

Until recently, paper checks accounted for the majority of noncash payments.[1] A Board of Governors study published in 2002 concluded that the number of checks paid annually in the United States likely began to decline during the mid-1990s (chart 1).[2] A more recent study conducted by the Federal Reserve System, which estimated and compared the number of checks paid in 2000 with the number paid in 2003, showed that the decline in the number of checks paid may have accelerated over the past few years.[3] The average annual rate of decline in the number of checks paid is estimated to have been 3.3 percent between 1995 and 2000 and 4.3 percent between 2000 and 2003.[4] Although growth rates for electronic payments have been high for decades, the cumulative effect of this growth has only recently become large enough to substantially affect the number of checks paid. By 2003, led by rapid growth in debit card payments, the number of electronic payments exceeded the number of check payments for the first time in U.S. history (chart 1, table 1).

1. Annual number of noncash payments in the United States, selected years



SOURCE. Federal Reserve Board.

The large number of electronic payments generally indicates growing efficiency of the payments system. The processing of paper payments typically requires extensive physical handling. Automation has created opportunities for depository institutions and other payments processors not only to introduce new payment instruments, but also to reduce their costs in processing paper and electronic payments. Future innovations are expected to continue to help decrease costs and add value and functionality. (See box "Changes in the Processing of Payments.")

This article analyzes the results of two payments surveys conducted in 2004, one of depository institutions (the 2004 depository institution survey) and

1. Because some checks are converted to electronic payments at the point of sale or during the process of collection, the number of checks paid differs from the number of checks written. This point is discussed in the box "Changes in the Processing of Payments." Unless otherwise noted, statements in this article about the number of checks refer to the number of paid checks.

2. Geoffrey R. Gerdes and Jack K. Walton II (2002), "The Use of Checks and Other Noncash Payment Instruments in the United States," *Federal Reserve Bulletin*, vol. 88 (August), pp. 360–74, www.federalreserve.gov/pubs/bulletin/2002/0802_2nd.pdf.

3. Federal Reserve System (2004), *The 2004 Federal Reserve Payments Study: Analysis of Noncash Payments Trends in the United States: 2000–2003*, Federal Reserve System Study, December 15, www.frbservices.org/Retail/pdf/2004PaymentResearchReport.pdf. Some figures reported in this article are revised from that earlier study because of improvements to the statistical imputation procedure, described in the appendix.

4. Rates of change (for example, rates of decline and rates of growth) reported in this article are computed as the average compounded annual rate of change, that is, the constant rate that if compounded annually would yield the observed change for the indicated time period.

1. Number and value of noncash payments, 2000 and 2003

Type of payment	Number		Value		
	Billions of payments	Percent of total	Trillions of dollars	Percent of total	Average, in dollars
2000					
Check[1]	41.9	57.8	39.8	66.7	951
Electronic	30.5	42.2	19.9	33.3	651
Debit card	8.3	11.4	.3	.6	42
Signature	5.3	7.3	.2	.4	40
PIN	3.0	4.2	.1	.2	46
Credit card	15.6	21.6	1.3	2.1	82
General-purpose[2]	12.3	17.0	1.1	1.8	87
Private-label[2]	3.3	4.6	.2	.3	62
ACH[4]	6.1	8.4	18.2	30.6	2,984
CCD	1.0	1.4	13.1	22.0	12,585
Retail	5.1	7.0	5.1	8.5	1,005
EBT[5]	.5	.7	.0	.0	26
Total noncash payments	**72.4**	**100.0**	**59.7**	**100.0**	**824**
2003					
Check[1]	36.6	45.3	39.0	59.1	1,065
Electronic	44.3	54.7	27.0	40.9	609
Debit card	15.6	19.3	.6	1.0	40
Signature	10.3	12.7	.4	.6	42
PIN	5.3	6.6	.2	.3	38
Credit card	19.0	23.4	1.7	2.6	89
General-purpose[2]	15.2	18.8	1.4	2.1	93
Private-label[3]	3.8	4.6	.3	.4	76
ACH[4]	8.9	11.0	24.6	37.3	2,766
CCD	1.4	1.8	16.4	24.8	11,424
Retail	7.5	9.2	8.3	12.6	1,108
EBT[5]	.8	1.0	.0	.0	26
Total noncash payments	**80.9**	**100.0**	**66.0**	**100.0**	**815**
	Number		Value		
	Change over period (billions of payments)	Annual rate of change (percent)[6]	Change over period (trillions of dollars)	Annual rate of change (percent)[6]	
Change, 2000–2003					
Check	–5.2	–4.3	–.8	–.7	
Electronic	13.8	13.2	7.1	10.7	
Debit card	7.3	23.5	0.3	21.9	
Signature	5.0	24.9	.2	26.7	
PIN	2.3	21.0	.1	13.9	
Credit card	3.4	6.7	.4	9.9	
General-purpose	2.9	7.3	.3	9.5	
Private-label	.5	4.4	.1	11.5	
ACH	2.8	13.4	6.4	10.5	
CCD	.4	11.1	3.2	7.5	
Retail	2.4	13.8	3.2	17.6	
EBT	.3	15.4	.0	16.2	
Total noncash payments	**8.6**	**3.8**	**6.3**	**3.4**	

NOTE. The number and value of checks and ACH payments for 2000 are revised downward from figures reported in Gerdes and Walton, "The Use of Checks," because of revisions to data and improvements in estimation. The number and value of checks and ACH payments for 2003 are revised from figures reported in Federal Reserve System, *2004 Federal Reserve Payments Study* because of improvements to the imputation procedure. See the appendix for details.

1. Includes checks paid by depository institutions, U.S. Treasury checks, and postal money orders.
2. Includes the four widely accepted general-purpose credit and charge cards.
3. Includes private-label credit cards issued by oil companies and many large retailers and specialized charge cards for travel and entertainment.
4. CCDs are cash concentration or disbursement transactions, about half of which are internal corporate transfers. Retail includes all other payments.
5. Electronic benefit transfer.
6. Compound annual growth rate.

one of electronic payments networks, processors, and credit card issuers (the 2004 electronic payment survey). It also draws on the results of two similar surveys conducted in 2001. The primary purposes of the 2004 surveys were to estimate the number and value of payments made by means of several types of noncash payment instruments in 2003 and to estimate rates of change from 2000 to 2003. (See the appendix for details on the surveys.)

The 2004 depository institution survey allowed for comparisons among different types and sizes. It also made possible an analysis of regional differences in the number and value of check, ACH, and debit card payments and automated teller machine (ATM) withdrawals. The 2004 electronic payment survey provided additional information on the use of ACH, cash back from debit cards, and different types of credit cards.

The surveys have focused on the amount of and trends in noncash payments. Indirect evidence discussed later, however, suggests that the use of cash has declined as a share of all payments in recent decades.[5] Whether the total number of cash transactions has begun to decline, as has the number of checks, is less clear.

Trends in Payment Instrument Use

Checks

The total number of checks paid annually in the United States is estimated to have declined from 41.9 billion in 2000 to 36.6 billion in 2003 (table 1).[6] As noted earlier, the annual rate of decline was 4.3 percent, compared with an estimated 3.3 percent between 1995 and 2000.[7] Although the use of checks declined, checks remained the most commonly used type of noncash payment in 2003.

Checks also continued to be the largest noncash payment type by value.[8] In fact, the value of checks exceeded the combined value of all the other noncash

5. Although the 2004 depository institution survey collected data on the number and value of ATM withdrawals, the surveys generally did not collect data that could be used to estimate the number or value of cash payments.

6. The number and value of checks for 2000 are revised downward from figures reported in Gerdes and Walton, "The Use of Checks," based on revisions to earlier data by several large commercial banks.

7. The estimated number of checks paid in 1995 was 49.5 billion.

8. The value of payments made via large-value funds transfer systems was $763 trillion in 2003, much greater than the value of payments made by other types of instruments, but those payments are outside the scope of this article. The overall number of these transfers, however, was 188 million in 2003, negligible compared with the number of payments described in this study. The check collection system is no longer used extensively for large-value funds transfers

Changes in the Processing of Payments

Automation of ACH, Credit Card, and Check Processing

Twenty-five years ago, all the major payment instruments in use today—cash, checks, credit cards, automated clearinghouse (ACH), and debit cards—were being used in commercial activity for some segments of the U.S. economy. Improvements in the processing of payments by cash, check, credit cards, and ACH over the past several decades have decreased the amount of physical processing and increased the amount of electronic processing. Because processing of payments has become more electronic generally, the rise in the share of noncash payments made with so-called electronic instruments understates the extent of the transition of the payments industry from physical to electronic processing.

Debit card networks were originally based on automated electronic systems that linked ATMs together, and the processing of these payments did not include a significant physical processing component. However, the processing of the other two types of electronic payments—ACH and credit cards—which once included considerable physical activity, now is wholly electronic.

The ACH system has evolved from the physical exchange of computer tapes within and among regional associations of depository institutions to an integrated electronic network for clearing and settlement that connects depository institutions around the country. Similarly, credit card processing has evolved from a largely physical activity—one in which accumulated paper transaction slips were deposited into a merchant's bank and then cleared and settled in a process similar to the process for paper checks—to an activity in which the availability of funds is almost always verified in real time over an electronic network and clearing and settlement occur electronically.

Changes that increase automated, electronic processing within the check collection system have come relatively slowly. Over the past twenty-five years, technology has evolved to allow the exchange by mutual agreement of electronic information on checks between depository institutions. Despite this capability, the collection of most checks, in the absence of an agreement between depository institutions, has involved extensive physical processing, transportation, and delivery because state laws require that the original check be presented to the paying depository institution for settlement. However, the Check Clearing for the 21st Century Act, Public Law 108–100 (Check 21), is expected to facilitate use of electronics in the processing of checks, because the original paper check is no longer necessary for settlement. Instead, when a paper check is required, a depository institution may satisfy that requirement by providing a special paper copy of the original check known as a substitute check. A substitute check that meets specified standards is the legal equivalent of the original. Thus, it is possible for depository institutions to truncate checks and collect them electronically, but also to present paper checks when necessary. As this article is written, seven months after the effective date of Check 21, the use of new electronic processing methods provided for in the act is growing only slowly. However, depository institutions are expected to increase their use of electronic check-clearing methods over time to further automate the check collection and settlement process by exchanging check images. These and other efforts will make check processing increasingly similar to the processing of other noncash payments.

Conversion of Checks

Recently, technological innovations have occurred that allow the use of information from a check to initiate an electronic payment. This process, known as check conversion, was typically initiated by merchants at point-of-sale registers and by back-office transaction processors for large billers, into payments that are processed by ACH or the debit card networks and has contributed significantly to the recent acceleration in the growth of electronic payments. The conversion of checks began to take hold in the late 1990s, eventually resulting in changes to ACH network rules and in payments regulations that govern the practice.

payment types. The value of checks was an estimated $39.0 trillion in 2003, compared with $39.8 trillion in 2000, indicating an annual decline of 0.8 percent. In constant (2003) dollars the value of checks declined almost 3 percent annually.[9]

The average value of checks increased slightly, reaching $1,065 in 2003, up from $951 in 2000 ($1,009 in 2003 dollars). This small change in average value suggests that the use of smaller-value checks (for amounts less than $1,000) declined more rapidly than the use of larger-value checks. Indeed, calculations show that at least 87 percent of the decline in checks paid, by number, resulted from a decline in the number of checks for less than $1,000.[10] The greater decline of smaller-value checks

because most such transfers are uniquely suited to the large-value systems.

9. Over the period 2000 to 2003, inflation, as measured broadly by the implicit price deflator for gross domestic product, averaged 2 percent per year.

10. According to a 2001 survey of checks collected, about 87 percent of checks in 2000 were for amounts less than $1,000. See Gerdes and Walton, "The Use of Checks."

suggests that checks involving an individual and a business—checks written by individuals to pay businesses and by businesses to pay individuals—were being replaced by other types of payments in substantially greater numbers than checks written by businesses to pay businesses.[11]

Automated Clearinghouse (ACH) Payments

The number of ACH payments increased from 6.1 billion in 2000 to 8.9 billion in 2003, for an annual growth rate of 13.4 percent.[12] The value of ACH payments grew at a slower pace, increasing from $18.2 trillion to $24.6 trillion, an annual growth rate of 10.5 percent. The average value of an ACH payment declined from $2,984 in 2000 ($3,110 in 2003 dollars) to $2,766 in 2003.

The decline in the average value of ACH payments was due almost entirely to a decline in the value of ACH transactions called cash concentration or disbursement (CCD) transactions. Most CCD transactions are large-value financial transfers conducted by large corporations, and include nonpayment activity, such as internal corporate account balance transfers.[13] They may be made by check, but over time they have increasingly been made over large-value funds transfer systems. The decline in average value may reflect movement of large-value ACH CCD transactions to large-value funds transfer systems or a trend toward the concentration of corporate accounts at fewer depository institutions.

The number of retail ACH payments—ACH payments not classified as CCD payments—increased from 5.1 billion in 2000 to 7.5 billion in 2003, for an annual rate of growth of 13.8 percent.[14] In both years, retail ACH payments constituted more than 80 percent of ACH payments. Such payments are comparable to certain types of recurring payments typically made by check, such as payroll and remittance payments by businesses and remittance payments by consumers (for example mortgage payments, bill payments to credit card accounts, and utility payments).

The average value of retail ACH payments was $1,108 in 2003, up from $1,005 in 2000 ($1,064 in 2003 dollars). The average value increased at a slower rate than that of checks, so that by 2003 the average values of retail ACH payments and checks were roughly the same.

Recently, new uses of the ACH to convert checks to ACH payments and to make nonrecurring payments over the telephone or Internet (typically made by credit or debit card) have contributed significantly to the growth of ACH payments. The number of ACH payments identified as check conversion transactions was more than 300 million in 2003 and rose to at least 1.1 billion in 2004.[15] The number of ACH payments for Internet or telephone purchases accounted for at least 600 million payments in 2003 and at least 900 million in 2004.

Debit Card Payments

Among electronic payments, debit card transactions grew the most in terms of number, from 8.3 billion in 2000 to 15.6 billion in 2003. The growth in debit card payments accounted for more than half the growth in electronic payments over the period.

Debit cards are used primarily by consumers for everyday purchases at retail stores. Credit cards and checks are also used for this purpose, but, with an average value in 2003 of $40, debit card payments were used for small-value payments more commonly than other payment instruments except electronic benefits transfers and, perhaps, cash.

Most debit cards can be used not only to make payments, but also to access an ATM network by entering a personal identification number (PIN). Depending on the arrangements made by the depository institution that issues the card, payments by debit card may be routed through one or more networks. Payments authorized with a PIN may flow

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11. Payments by individuals to other individuals are generally made by check or cash. It is possible for individuals to pay other individuals electronically, but the number of such payments was too small in 2003 to have contributed significantly to the decline in the number of small-value checks.

12. The number and value of ACH payments for 2000 are revised from earlier figures reported in Gerdes and Walton, "The Use of Checks."

13. CCD payments are traditionally used by large corporations to move funds between their own accounts for internal business and financial purposes and, as such, are of limited interest to this article. However, results of a survey of members of the Association of Financial Professionals (AFP), conducted by Dove Consulting and the AFP in 2003, suggested that around half of CCDs are payments between two counterparties and not just internal transfers. The portion of the value of CCDs that represent payments between counterparties is unknown.

14. This portion of ACH transactions is considered separately because of the mixing of nonpayment transactions with payments in ACH CCD transactions.

15. National Automated Clearing House Association. Figures include check conversion transactions at the point of sale, in the back offices of billers, and at "lockbox" services provided by depository institutions and others. The figures understate total transactions because they include only those transactions processed on an ACH network and exclude transactions processed internally by only one depository institution (on-us). An unknown—but likely small—number of checks were converted to debit card network payments.

through regional or national debit card networks. Some debit cards may also be used to make signature-based payments (including remote payments that the cardholder authorizes over the Internet or telephone). Almost all such payments are routed through networks operated by VISA or MasterCard. Such cards, therefore, may be used in the same way as credit cards. They have different financial characteristics, however, as they are linked to a transaction (deposit) account rather than a credit account. The number of signature-based debit card payments almost doubled between 2000 and 2003, from 5.3 billion to 10.3 billion for an annual growth rate of almost 25 percent. This growth accounted for most of the increase in debit card payments. The average value of a signature-based debit payment increased from $40 in 2000 to $42 in 2003.

The number of debit card payments authorized by a PIN increased from 3.0 billion in 2000 to 5.3 billion in 2003, an annual growth rate of 21 percent. Although PIN-based debit card payments had a higher growth rate than both ACH and credit card payments, they started from a smaller base. PIN-based payments grew more slowly than signature-based payments, accounting for less than one-third of the growth in debit card payments from 2000 to 2003. The average value of PIN-based debit card payments declined from $46 in 2000 ($49 in 2003 dollars) to $38 in 2003.

When a debit card is used to make a purchase and the card user authorizes payment with a PIN, some merchants may, on request, return part of the payment in cash, sometimes called cash back. In such cases, the value of the payment includes both the value of the purchase and the value of the cash returned. Most debit card networks could not report the value of cash back, nor could they report the number of PIN debit payments that involved the return of cash. The data provided by a few networks suggest that in 2003, about 11 percent of PIN-based debit payments involved the return of some cash to the card user and that about 7 percent of the total value of PIN-based debit payments was returned to card users as cash (a corresponding 93 percent of PIN debit value was used for purchases). For PIN-based debit payments that included some cash back, the value of the cash returned averaged about $30.[16]

From 2000 to 2003, the increase in the average value of signature-based debit card payments was small ($2), indicating little change. The decline in the average value of PIN-based debit card payments was larger ($8), however, indicating an increasing proportion of small-value payments. How much of the decline for PIN-based payments should be attributed to declines in the cash-back or purchase portion of the payments is unclear.

Changes in fees charged to card users and merchants may help to explain the greater use and faster rise in signature-based compared with PIN-based debit card payments. Most depository institutions do not charge account holders for using a debit card—among those that do, fees are much more common for PIN-based purchases than for signature-based purchases. The trend in fees charged to card users is unknown. Fees charged to merchants for accepting signature-based payments declined between 2000 and 2003, while fees for accepting PIN-based payments increased.[17]

Credit Card Payments

The number of credit card payments increased from 15.6 billion in 2000 to 19.0 billion in 2003, an annual growth rate of 6.7 percent. Among electronic payment instruments, payments by credit card grew at the slowest rate over the period. Credit card payments have shown high rates of growth in the past, and credit cards have been an important payment type for decades. Growth rates are no longer influenced by the high rates of adoption that occurred in earlier decades, however, and the overall slowdown in growth is likely a result, in part, of the maturity of the credit card as a payment instrument.

The tapering off of the growth in credit card payments also corresponds to the rapid rise in the use of signature-based debit cards. Just as debit card payments may have replaced many check and cash payments, they may have replaced some credit card payments as well.

Of the 19.0 billion credit card transactions in 2003, 3.8 billion were private-label card transactions, up from 3.3 billion in 2000, for an annual growth rate of 4.4 percent. Private-label credit cards, which were in common use before general-purpose credit cards were introduced, are the most mature type of credit card. During the 1990s, the use of private-label credit cards declined, in part because card users increasingly began to use general-purpose credit cards and debit cards in their place. The recent resurgence of

16. Because cash back was reported as a separate aggregate, it was not possible from the survey data to compare the average value of PIN-based debit card payments that included cash back with the average value of ones that did not.

17. Board of Governors of the Federal Reserve System (2004), *Report to the Congress on the Disclosure of Point-of-Sale Debit Fees* (Washington: Board of Governors, November), www.federalreserve.gov/boarddocs/rptcongress/posdebit2004.pdf.

private-label credit card payments may have been influenced by programs that give discounts or rewards for purchases made with the cards or by relatively liberal credit provided by merchants to otherwise-credit-constrained consumers.

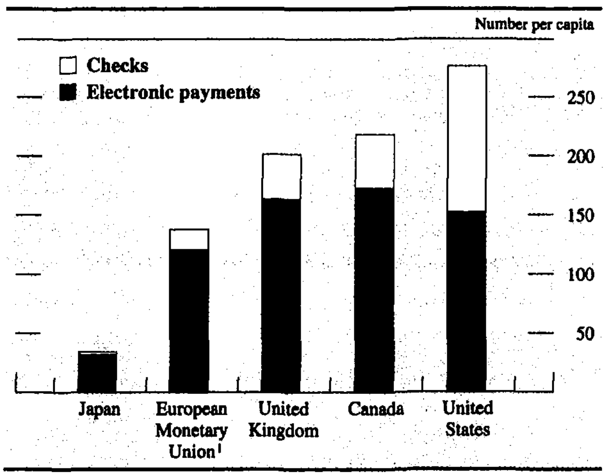
Electronic Benefits Transfers

The average (nominal) value of an electronic benefits transfer (EBT) was $26 in both 2000 and 2003, implying that the average value in 2003 dollars declined. EBTs are used to disburse federal and state government benefits, such as food stamp benefits. The number of EBTs rose from 0.5 billion in 2000 to 0.8 billion in 2003, for an annual growth rate of about 15 percent. Much of the growth was due to replacement of paper food stamps. As most states have completed conversion to EBTs, future growth is not likely to be influenced by high rates of adoption and, barring substantial growth in the food stamp program, is likely to taper off in the future.

Payments in Other Countries

A look at noncash payments in other countries provides some perspective on the use of checks and electronic payments in the United States. Compared with other industrialized economies—Japan, the European Monetary Union (EMU), the United Kingdom, and Canada—the number of checks per capita is considerably higher in the United States (chart 2).

2. Number of noncash payments per capita, selected economies, 2003



1. Includes Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Luxemburg, The Netherlands, Portugal, and Spain.

Sources. European Central Bank, *Payment and Securities Settlement Systems in the European Union, June 2004*; Bank for International Settlement, *Statistics on Payment Systems in the Group of Ten Countries*; and Federal Reserve Board.

The number of electronic payments per capita is higher in the United States than in Japan and the EMU, but lower than in the United Kingdom and Canada. Detailed data (not shown) indicate that the number of electronic payments per capita in some countries of the EMU, such as Finland, Germany, and the Netherlands, is higher than in the United States. Similarly, the use of electronic payments may be higher in some regions of the United States than in others, as is discussed later.

Between 2000 and 2003, the number of electronic payments per capita in all these economies increased, whereas the number of checks per capita declined. Without reliable measures of cash use, however, a comprehensive comparison across countries of the extent to which electronic payments have replaced all forms of paper-based payments (mostly cash and checks) is not possible.

Payments and Withdrawals from Accounts at Depository Institutions

The 2004 depository institution survey provided enough information to estimate the number and value of check payments (including money orders, cashiers, certified, official, travelers, rebate, and credit card checks), ACH payments (credit and debit transactions), debit card payments (signature and PIN), and ATM withdrawals by type and size of depository institution (table 2).[18] In the following discussion, all these means of debiting accounts are referred to collectively as account debits. The survey collected information on account debits for March and April 2004, and the estimates are expressed as annual rates by multiplying the two-month totals by six. The data reported here should be viewed as annualized figures for March and April 2004, and they may not well represent either calendar year 2003 or calendar year 2004, particularly in the case of ACH and debit card payments which had high rates of growth in both years.[19]

Depository institution survey estimates of the total value of ACH payments reported in this section, however, are much greater than estimates reported for

18. ACH payments may be credit transfers originated by a payer or debit transfers originated by a payee. ACH payments that result in account debits at a responding depository institution are credits originated on instructions of an account holder (payee) or debits received, possibly from another depository institution, on instructions of a payee.

19. The average number of checks processed by the Federal Reserve Banks in March and April is roughly equal to the average processed in other months of the year, so the sum of March and April is representative of other months for these checks.

2. Annual number and value of debits to transaction accounts held at depository institutions

Type and size of institution (transaction deposits in millions of dollars)	Number of institutions	Checks paid			ACH payments			Debit card payments		
		Number (billions)	Value (trillions of dollars)	Average value (dollars)	Number (billions)	Value (trillions of dollars)	Average value (dollars)	Number (billions)	Value (trillions of dollars)	Average value (dollars)
Commercial banks	**6,580**	**29.06**	**36.253**	**1,248**	**9.07**	**84.175**	**9,277**	**12.42**	**.497**	**40**
600 and above	99	19.89	29.070	1,461	7.54	79.988	10,607	10.33	.418	40
200–599	173	2.19	2.119	967	.49	2.545	5,149	.79	.030	39
100–199	389	1.83	1.491	816	.38	.590	1,561	.49	.019	38
0–99	5,919	5.15	3.573	694	.66	1.053	1,594	.82	.030	37
Savings institutions	**1,129**	**2.95**	**1.510**	**511**	**.51**	**2.161**	**4,230**	**2.14**	**.087**	**40**
600 and above	15	1.37	.627	457	.21	1.774	8,591	1.49	.061	41
200–599	39	.46	.253	545	.07	.129	1,741	.21	.009	41
100–199	52	.25	.140	570	.04	.060	1,492	.10	.004	41
0–99	1,023	.87	.489	562	.19	.199	1,044	.33	.013	39
Credit unions	**6,411**	**4.17**	**.915**	**219**	**.88**	**.316**	**358**	**3.45**	**.131**	**38**
600 and above	3	.19	.050	256	.05	.021	416	.25	.010	38
200–599	31	.43	.108	253	.10	.040	383	.49	.019	39
100–199	80	.54	.136	252	.13	.049	375	.60	.023	39
0–99	6,297	3.01	.621	207	.60	.206	346	2.11	.079	38
All institutions	**14,120**	**36.18**	**38.677**	**1,069**	**10.47**	**86.653**	**8,279**	**18.01**	**.715**	**40**

Type and size of institution (transaction deposits in millions of dollars)	Number of institutions	ATM withdrawals			Total debits to transaction accounts			Memo		
		Number (billions)	Value (trillions of dollars)	Average value (dollars)	Number (billions)	Value (trillions of dollars)	Average value (dollars)	Transaction deposits (billions of dollars)	Total deposits (billions of dollars)	Total assets (billions of dollars)
Commercial banks	**6,580**	**3.87**	**.345**	**89**	**54.43**	**121.270**	**2,228**	**680**	**4,866**	**8,031**
600 and above	99	3.11	.291	93	40.87	109.766	2,686	409	3,155	5,445
200–599	173	.25	.019	75	3.72	4.713	1,268	55	409	709
100–199	389	.17	.013	73	2.87	2.112	736	53	289	403
0–99	5,919	.34	.023	69	6.97	4.679	671	163	1,013	1,474
Savings institutions	**1,129**	**.71**	**.058**	**81**	**6.32**	**3.815**	**604**	**135**	**800**	**1,332**
600 and above	15	.40	.038	93	3.48	2.499	719	89	325	608
200–599	39	.10	.007	73	.85	.397	469	13	122	207
100–199	52	.06	.004	63	.45	.208	467	7	63	101
0–99	1,023	.15	.010	63	1.55	.711	460	25	289	416
Credit unions	**6,411**	**1.29**	**.094**	**72**	**9.79**	**1.455**	**149**	**69**	**540**	**623**
600 and above	3	.10	.008	79	.60	.089	148	5	32	38
200–599	31	.17	.013	79	1.19	.180	152	9	65	75
100–199	80	.20	.015	78	1.47	.224	152	11	80	93
0–99	6,297	.83	.057	69	6.54	.963	147	45	363	417
All institutions	**14,120**	**5.87**	**.497**	**85**	**70.53**	**126.541**	**1,794**	**885**	**6,205**	**9,985**

NOTE. Annualized figures based on survey data for March 2004 and April 2004. Excludes institutions that had no transaction deposits. The number and value of debits are revised from figures reported in Federal Reserve System, *2004 Federal Reserve Payments Study* because of improvements to the imputation procedure. See the appendix for details.

2003 and much greater than growth rates would imply (table 1). Some of the large commercial banks that responded to the 2004 depository institution survey had difficulty distinguishing ACH payments from other (large-value) funds transfers called offset entries.[20] The 2003 estimates of ACH value are believed to be more accurate because they are based, in large part, on aggregate values reported by the ACH operators.

20. The difficulty in separating offset entries from ACH payments is due to use of a shared platform to process both, a common practice of some of the largest depository institutions. The difficulty, which involves a small number of very large-value entries, did not substantially affect the estimates of the number of ACH payments. See the appendix for more information.

Shares of Account Debits among Depository Institutions, by Type and Size of Institution

Depository institutions are grouped into three types (commercial banks, savings institutions, and credit unions) and, within each type, into four categories according to size: largest, large, medium, and small. The largest depository institutions (those with transaction deposits of $600 million or above) accounted for the majority of account debits (table 3). This group of 117 institutions (99 commercial banks, 15 savings institutions, and 3 credit unions) represents fewer than 1 percent of the 14,120 depository institutions that had transaction deposits during the survey period, yet these institutions held 57 percent of transaction deposits, and accounted for 64 percent of account debits by number and 89 percent by value. Moreover, the largest depository institutions accounted for most of the debits of each type (check, ACH, debit card, or ATM withdrawal), by both number and value. The debit type for which this group had the largest share by number was ACH payments (a little less than 75 percent), and the smallest share by number was checks (almost 60 percent).

The average value of account debits varied with depository institution size. For ACH payments in particular, a substantial amount of value was concentrated at the largest commercial banks (table 2). The greater average value of ACH payments at the largest banks was due, in part, to the exceptionally high values reported by some banks, as noted above, but the average value of checks was also considerably greater at these largest banks. Generally, the increase in the average value of ACH payments and checks with increasing size of commercial banks appears to have been driven by the greater presence of large business customers at larger commercial banks.[21] Larger commercial banks are more likely to have large corporations as customers, and these customers are more likely to make larger-value payments by check or ACH.

Savings institutions appear to have lower proportions of business customers than commercial banks, shown by the lower average values of their check and ACH payments. The average value of ACH payments was substantially greater at the largest savings institutions, compared with the large savings institutions while the average value of checks was smaller.

Credit unions, which generally do not handle transaction accounts for businesses, had the lowest average values of check and ACH payments. They did not show material increases in the average value of check payments with increasing institution size. However, they did show increases in the average value of ACH payments with increasing size.

21. We estimate that in 2000 the average value of checks written by individuals was about $350 and by businesses, $1,700. These are the authors' estimates based on a study in which individual checks that could be classified were sorted by payer. See Federal Reserve System (2002), *Retail Payment Research Project: A Snapshot of the U.S. Retail Payment Landscape*, Federal Reserve System Study, pp. 12–14, www.frbservices.org/Retail/pdf/RetailPaymentsResearchProject.pdf.

3. Distribution of debits to transaction accounts among depository institutions, by number and value

Percent

Type and size of institution (transaction deposits in millions of dollars)	Distribution of institutions, by number	Checks paid		ACH payments		Debit card payments		ATM withdrawals		Total debits to transaction accounts		Memo		
		Number	Value	Number	Value	Number	Value	Number	Value	Number	Value	Transaction deposits	Total deposits	Total assets
Commercial banks	**46.6**	**80.3**	**93.7**	**86.7**	**97.1**	**69.0**	**69.6**	**65.9**	**69.5**	**77.2**	**95.8**	**76.9**	**78.4**	**80.4**
600 and above	.7	55.0	75.2	72.0	92.3	57.3	58.4	53.0	58.5	57.9	86.7	46.2	50.8	54.5
200–599	1.2	6.1	5.5	4.7	2.9	4.4	4.3	4.2	3.7	5.3	3.7	6.2	6.6	7.1
100–199	2.8	5.0	3.9	3.6	.7	2.7	2.6	3.0	2.6	4.1	1.7	6.0	4.7	4.0
0–99	41.9	14.2	9.2	6.3	1.2	4.5	4.2	5.8	4.7	9.9	3.7	18.5	16.3	14.8
Savings institutions	**8.0**	**8.2**	**3.9**	**4.9**	**2.5**	**11.9**	**12.1**	**12.1**	**11.6**	**9.0**	**3.0**	**15.3**	**12.9**	**13.3**
600 and above	.1	3.8	1.6	2.0	2.0	8.3	8.5	6.9	7.6	4.9	2.0	10.1	5.2	6.1
200–599	.3	1.3	.7	.7	.1	1.2	1.2	1.6	1.4	1.2	.3	1.5	2.0	2.1
100–199	.4	.7	.4	.4	.1	.6	.6	1.0	.7	.6	.2	.8	1.0	1.0
0–99	7.2	2.4	1.3	1.8	.2	1.8	1.8	2.6	2.0	2.2	.6	2.8	4.7	4.2
Credit unions	**45.4**	**11.5**	**2.4**	**8.4**	**.4**	**19.1**	**18.3**	**22.0**	**18.8**	**13.9**	**1.2**	**7.8**	**8.7**	**6.2**
600 and above	.0	.5	.1	.5	.0	1.4	1.4	1.7	1.6	.8	.1	.5	.5	.4
200–599	.2	1.2	.3	1.0	.0	2.7	2.6	2.8	2.6	1.7	.1	1.0	1.0	.7
100–199	.6	1.5	.4	1.2	.1	3.3	3.3	3.3	3.1	2.1	.2	1.2	1.3	.9
0–99	44.6	8.3	1.6	5.7	.2	11.7	11.1	14.2	11.6	9.3	.8	5.1	5.9	4.2
All institutions	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

NOTE. See general note to table 2.

Distribution of Depository Institutions' Account Debits, by Type and Size of Institution

Overall, about 51 percent of account debits were made by check, 15 percent were ACH payments, 26 percent were debit card payments, and 8 percent were cash withdrawals from ATMs (table 4).[22] The distribution of account debits, by number, at commercial banks differed markedly from the distributions at savings institutions and credit unions.

The proportion of checks at commercial banks was about 53 percent, compared with 47 percent at savings institutions and 43 percent at credit unions. For commercial banks, the proportion of checks declined noticeably with increasing size. The proportion at small banks (those with less than $100 million in deposits) was about 74 percent, and at the largest banks, 49 percent. The proportion of checks also declined with increasing size at savings institutions and credit unions. The proportion of checks may be smaller at larger depository institutions because they provide (and perhaps encourage) greater use of ACH and debit cards. Larger depository institutions may also serve more sophisticated customers, including large businesses, that may be more willing or able to take advantage of cost savings or other benefits afforded by other types of payment.

For commercial banks, the proportion of ACH payments by number increased with increasing size, the reverse of the relationship for checks, and payments at larger banks were more likely to be made via ACH. The greater proportion of ACH payments at the largest banks may have had much to do with greater use of ACH by large corporate account holders. The proportion of ACH payments, by number, did not increase with increasing size at savings institutions and credit unions; it was generally flat across size categories for credit unions, and it declined with increasing size for savings institutions.

Debit card payments and ATM withdrawals are made primarily by individuals—and as a proportion of debits, are more prevalent at credit unions, because generally these institutions do not have large business customers. About 35 percent of payments at credit unions and 34 percent of payments at savings institutions were made by debit card. In contrast, the proportion of debit card payments for commercial banks, which as a category have more business customers, was smaller, at 23 percent. Similarly, the proportion of ATM withdrawals was greater for savings institutions and credit unions—11 percent and 13 percent, respectively, compared with 7 percent for commercial banks.

Overall, as estimated from the 2004 depository institution survey, signature-based debit card payments, at 11.7 billion, were almost twice as common as PIN-based debit card payments, at 6.3 billion. The ratio of signature-based to PIN-based debit card payments was roughly similar across institutions of different types and sizes, indicating that use of signature and PIN authorization for debit card purchases

22. These figures do not represent percentages in total noncash payments primarily because debits to deposit accounts include ATM withdrawals and do not include credit card payments.

4. Distribution of debits to transaction accounts at depository institutions, by number and value

Percent

Type and size of institution (transaction deposits in millions of dollars)	Checks paid		ACH payments		Debit card payments		ATM withdrawals		Total debits to transaction accounts	
	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value
Commercial banks	**53.4**	**29.9**	**16.7**	**69.4**	**22.8**	**.4**	**7.1**	**.3**	**100.0**	**100.0**
600 and above	48.7	26.5	18.5	72.9	25.3	.4	7.6	.3	100.0	100.0
200–599	58.9	45.0	13.3	54.0	21.1	.6	6.6	.4	100.0	100.0
100–199	63.6	70.6	13.2	27.9	17.1	.9	6.1	.6	100.0	100.0
0–99	73.9	76.4	9.5	22.5	11.8	.6	4.8	.5	100.0	100.0
Savings institutions	**46.8**	**39.6**	**8.1**	**56.6**	**33.9**	**2.3**	**11.2**	**1.5**	**100.0**	**100.0**
600 and above	39.5	25.1	5.9	71.0	42.9	2.4	11.6	1.5	100.0	100.0
200–599	54.9	63.7	8.7	32.4	25.2	2.2	11.2	1.7	100.0	100.0
100–199	55.2	67.4	9.1	28.9	23.2	2.0	12.6	1.7	100.0	100.0
0–99	56.3	68.9	12.3	27.9	21.5	1.8	10.0	1.4	100.0	100.0
Credit unions	**42.6**	**62.8**	**9.0**	**21.7**	**35.2**	**9.0**	**13.2**	**6.4**	**100.0**	**100.0**
600 and above	32.6	56.2	8.6	24.0	42.3	10.9	16.5	8.8	100.0	100.0
200–599	36.0	60.0	8.8	22.3	41.2	10.5	14.0	7.3	100.0	100.0
100–199	36.9	60.9	8.9	21.8	40.9	10.4	13.4	6.9	100.0	100.0
0–99	45.9	64.4	9.1	21.4	32.2	8.2	12.7	6.0	100.0	100.0
All institutions	**51.3**	**30.6**	**14.8**	**68.5**	**25.5**	**.6**	**8.3**	**.4**	**100.0**	**100.0**

NOTE. See general note to table 2.

does not vary with the size or type of institution. Although the ratio of signature to PIN debits did not vary with size or type, there was substantial variation among responding institutions. (Figures referred to in this paragraph are not shown in the tables.)

Variation in the use of signature-based and PIN-based debit card payments from institution to institution reflects card user preferences but can be influenced by incentives to use one or the other authorization method offered by either merchants or depository institutions. Merchants, for example, may or may not accept both authorization methods, or may limit acceptance of cards to certain purchase values or to certain products. Card associations or depository institutions may offer more benefits to users that authorize debit card payments with a signature. In 2003, per-transaction fees charged to merchants generally increased with the value of the payment for signature-based debit card payments but were generally fixed for PIN-based payments. Some depository institutions charge their customers fees for their debit card purchases authorized with a PIN.[23] Depository institutions and card associations also offer benefits to customers who authorize with a signature.

"On Us" Payments

The proportions of account debits that are on-us—that is, those that involve only one depository institution—are interesting because clearing and settlement of such payments occur internally at the depository institution and, therefore many of the costs associated with coordinating payments with other depository institutions are not incurred.[24] For example, when a check needs to be collected from another depository institution, float cost and risk-reduction incentives lead depository institutions to use fast and costly transportation channels to expedite check presentment and collection. Float costs and some risks are absent when a check is on-us, allowing depository institutions to avoid expensive transportation channels.

Commercial banks as a group generally had the highest proportion of on-us account debits, by number and value, while credit unions had the lowest proportion (table 5). Banks with both businesses and consumers as customers are more likely to have on-us payments. About 13 percent of checks collected in 2000 were from one individual to another.[25] Thus, 87 percent involved a business or government. The relatively high proportions of on-us check and ACH payments at commercial banks were influenced by these institutions' larger share of business customers.

Overall, 23 percent of checks paid were on-us, about 4 percentage points lower than the estimate from the 2001 depository institution survey. The on-us proportion declined for all types of institution, but the proportion reported by credit unions declined considerably—from an estimated 6 percent in 2000 to 2 percent in 2003. The decline in the proportion of on-us checks could be one consequence of a possible decline in the cashing of personal checks as a means of obtaining cash at a teller window in an individual's own depository institution (discussed later). However, some evidence suggests that respondents reported more accurate on-us figures in the 2004 survey, implying that estimates of the proportion of on-us payments from the 2001 survey may have been too large.[26]

The proportion of on-us ACH payments in terms of value was notably larger for the largest commercial banks and savings institutions than for their smaller counterparts. The larger proportions appear to have resulted from data reported by some very large depository institutions that apparently generate a significantly larger share of large-value on-us ACH payments than other similarly sized institutions. As noted earlier, some of the reported ACH payments also included large-dollar account entries, called offset entries, conducted for internal account-balancing and settlement purposes. Institutions that had problems distinguishing offset entries appear to have overestimated the value of both on-us and interbank ACH payments.

The largest proportions of on-us account debits, both by number and value, were for ATM withdrawals except by value for large savings institutions. Most of the other types of account debits involve payments to other parties, who choose the depository institution in which to deposit funds. In the case of ATM withdrawals, the account holder plays the role of payee and payer, choosing the depository institu-

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23. Board of Governors of the Federal Reserve System, *Point-of-Sale Debit Fees.*

24. For checks and ACH payments, "on us" means that the payer and the payee use the same depository institution. For ATMs, the term means that the withdrawal occurred at a proprietary ATM (owned by the account holder's depository institution). Data on on-us debit card payments were not collected. On-us account debits plus interbank account debits sum to total account debits.

25. Federal Reserve System, *Retail Payment Research Project.*

26. The survey definition of "on-us" focuses on both the payer and the payee. It appears that some depository institutions interpreted the term to mean *any* check the depository institution is responsible for paying. Respondents may have become more familiar with the survey definition of on-us over time.

5. Proportion of selected debits to transaction accounts at depository institutions that were on-us, by number and value

Percent

Type and size of institution (transaction deposits in millions of dollars)	Checks paid		ACH payments		ATM withdrawals		Total debits to transaction accounts	
	Number	Value	Number	Value	Number	Value	Number	Value
Commercial banks	**26.9**	**32.4**	**21.9**	**42.1**	**67.9**	**69.4**	**29.6**	**39.3**
600 and above	28.7	32.8	24.8	42.9	70.4	71.7	32.0	40.3
200–599	20.7	27.5	13.0	33.9	63.2	60.8	23.0	31.1
100–199	21.5	32.6	5.2	16.8	60.7	62.1	21.8	28.3
0–99	24.5	31.5	5.3	17.4	52.6	51.3	23.9	28.4
Savings institutions	**10.9**	**19.1**	**6.7**	**68.1**	**54.1**	**57.5**	**17.8**	**48.4**
600 and above	11.4	21.8	10.8	79.2	57.4	57.7	20.7	64.4
200–599	9.4	16.0	4.8	22.9	53.7	59.3	15.6	19.1
100–199	11.6	18.8	4.8	19.8	49.9	59.6	17.3	19.8
0–99	10.6	17.4	3.5	12.2	47.2	54.9	14.2	16.4
Credit unions	**2.4**	**4.4**	**1.7**	**4.3**	**37.0**	**38.6**	**9.4**	**6.8**
600 and above	.6	1.6	.3	2.0	52.9	41.7	15.5	5.7
200–599	2.3	3.8	2.3	6.5	46.3	44.0	12.8	7.7
100–199	2.7	4.3	2.8	7.7	44.2	44.7	12.1	8.2
0–99	2.5	4.7	1.6	3.4	31.6	35.4	7.8	6.4
All institutions	**22.8**	**31.2**	**19.5**	**42.7**	**59.5**	**62.2**	**26.2**	**39.2**

NOTE. See general note to table 2.

tion in both cases. Not surprisingly, therefore, these payments are more likely to be on-us. For commercial banks, 68 percent of ATM withdrawals are on-us (69 percent by value), much higher than their on-us shares for other types of account debits. Commercial banks also generally have the largest networks of ATMs. Even credit unions, which own relatively few ATMs and for which the on-us shares for check and ACH payments were negligible, as a group had an on-us share for ATM withdrawals of 37 percent (39 percent by value). The larger on-us shares for ATM withdrawals also appear to reflect account holder avoidance of the fees commonly charged for using an ATM owned by another depository institution or other company (nonproprietary ATM).

Regional Variation

Estimates of the number and value of account debits by region are useful because they may help identify the ways in which differences in regional characteristics may influence the use of payment instruments. The 2004 depository institution survey yielded enough information to estimate the number and value of debits to accounts located in the four geographic divisions of the United States defined by the U.S. Census Bureau: Northeast, South, Midwest, and West (table 6). Estimation of debits from accounts in urban and rural locations was also possible (table 7). The 2004 survey gives a much clearer picture of the ways payment use differs by region than earlier surveys, which collected data sufficient to study regional variation in the use of checks but not in the use of other types of account debits.

Variation by Geographic Division

Estimates of account debits were constructed for each region after allocating depository institution data to regions according to the location of their branches.[27] These regional estimates, along with other regional data, provided the basis for comparing the use of payments in different regions of the country.

The estimate for checks as a proportion of total account debits at depository institutions ranged from a low of 46 percent in the West to a high of 55 percent in the Midwest.[28] By value, the shares of checks

27. As no region-specific data were collected from multiregion depository institutions, it was necessary to make an assumption about the way payments were allocated within responding multiregion depository institutions. For commercial banks and savings institutions, data on the regional distribution of deposits were available, so account debits at these institutions were allocated to regions in proportion to their deposits. For credit unions, account debits were allocated to regions according to the distribution of their branches. See the appendix for a discussion of the method used and assumptions required to allocate the figures for multiregion depository institutions to regions.

28. A preliminary multivariate statistical analysis that controlled for other factors correlated with depository institutions' share of checks in total reported account debits, by number, including depository institution size and type, showed that the greater share of checks for institutions in the Midwest is significantly different (in the statistical sense) from the shares in other regions.

appear to cluster into two groups: The West and Midwest had the lowest proportions, at 20 percent and 25 percent, respectively, and the South and Northeast had the highest proportions, at 41 percent and 40 percent respectively.[29] The average value of checks was lowest in the West ($923) and highest in the Northeast ($1,355). One explanation for the high value of checks in the Northeast may be that use of a special type of corporate checking account—the controlled-disbursement account—is concentrated in this region.

The regions are not equal in population. One way to put them on a comparable basis is to express the figures in terms of number or value per capita.[30] The annual number of account debits per capita ranged from a low of 231 in the South to a high of 262 in the Midwest. The annual number of checks per capita was lowest in the West, at 110, and highest in the Midwest, at 144. The value of checks per capita was also lowest in the West, but it was highest in the Northeast.

The regions also vary by amount of economic output (defined as the sum of gross state output for the states in each region) and can be put on a comparable basis by expressing the figures in terms of number or value of account debits per $1,000 of economic output. The annual number of account debits per $1,000 of regional output ranged from 5.9 in the Northeast to 7.2 in the Midwest. The number of checks per $1,000 of economic output was lowest in the West, at 2.8 and highest in the Midwest, at 3.9. The value of checks per $1,000 of economic output was also lowest in the West, at $2,618, but was highest the Northeast, at $4,042.

Debit card payments accounted for 33 percent of account debits by number in the West, compared with a range of 21 percent to 25 percent in the other regions. The proportion of debit card payments by value in the West was driven down by the extremely high value for ACH payments. The annual number and value of debit card payments per capita in the West, however, highlights the more prevalent use of debit cards in that region. The West had about 79 debit card payments per capita; the South and Midwest were well behind at 59.[31] The Northeast, at 51 debit card payments per capita, showed the lowest use, only 65 percent of the per capita figure in the West. Depository institutions in the West began offering debit card payments earlier than those in other regions, providing one explanation for the high debit card use in the West compared with other regions. Evidence from a different study also suggests that fees charged to cardholders for PIN debit use are least prevalent in the West and most prevalent in the Northeast.[32]

The average value of a debit card payment was $45 in the Northeast, compared with $39 in the other regions. The reason for the difference is unknown, but it could be that there were more cash-back transactions or a larger proportion of higher-value debit payments in the Northeast.

The annual number of ATM withdrawals per capita was highest in the Northeast, at 24, and lowest in the South, at 18. The average value of ATM withdrawals was highest in the Northeast, at $93, and lowest in the Midwest and South, at $78 and $79 respectively. The ATM data suggest that cash is used relatively more frequently in the Northeast, but individuals in other regions may obtain cash through other means, such as by writing checks, making debit card purchases with a PIN for cash back, or obtaining cash directly from a teller at a local depository institution branch.

Although data on ATM withdrawals provide indirect evidence of cash use, data on frequency and value of cash payments would better contribute to our understanding of which payment types are preferred in the different regions. The other important payment type missing from the regional analysis, of course, is credit card payments. Although the data presented here provide the most comprehensive and detailed information to date on the regional distribution of payments, evidence on payment use across regions remains incomplete because of the lack of cash payment and credit card payment data by region.

Urban and Rural Variation

The total number and value of payments were much smaller for rural areas than for urban areas, reflecting

29. One important caveat to the comparison of check shares by value is that the two institutions that reported the highest ACH values, much higher than other institutions of similar size, operated in the West and Midwest and likely contributed substantially to the low share of value for checks. Thus, the comparison of shares by value is sensitive to errors in reporting ACH payments, whereas the share by number and other results reported in this section are not.

30. Note that per capita figures are based on the entire population and include all payments, not just those made by individuals. Thus, figures do not represent averages of adult individuals or heads of household.

31. While estimates for subregions are too unreliable to report in detail, they show that the Pacific region (Alaska, California, Hawaii, Oregon, and Washington) had the highest use of debit cards per capita in the United States and the Middle Atlantic region (New York, New Jersey, and Pennsylvania) had the lowest.

32. Board of Governors, *Point-of-Sale Debit Fees*, p. 16 and p. 17, table 3.

6. Annual number and value of debits to transaction accounts at depository institutions, by geographic region

Item	Northeast			South			Midwest			West		
	Multi-region	Single region	All institutions	Multi-region	Single region	All institutions	Multi-region	Single region	All institutions	Multi-region	Single region	All institutions
Number (billions)	**8.7**	**4.8**	**13.4**	**11.1**	**13.1**	**24.2**	**8.6**	**8.6**	**17.2**	**7.6**	**8.1**	**15.8**
Checks	4.3	2.5	6.8	5.2	7.5	12.7	4.0	5.4	9.4	3.3	3.9	7.3
ACH	1.9	.6	2.5	2.0	1.5	3.5	1.7	.9	2.6	1.2	.7	1.8
Debit card	1.7	1.1	2.8	3.0	3.1	6.1	2.2	1.6	3.9	2.5	2.8	5.3
ATM	.8	.6	1.3	.9	1.0	1.9	.6	.6	1.3	.7	.7	1.4
Value (trillions of dollars)	**18.87**	**4.27**	**23.15**	**21.89**	**10.75**	**32.64**	**31.68**	**5.79**	**37.47**	**25.29**	**7.99**	**33.29**
Checks	7.18	2.07	9.25	7.30	5.94	13.23	6.07	3.40	9.47	3.92	2.8	6.72
ACH	11.54	2.10	13.64	14.39	4.63	19.02	25.48	2.28	27.75	21.21	5.02	26.23
Debit card	.08	.05	.13	.12	.11	.24	.09	.06	.15	.10	.11	.20
ATM	.08	.05	.12	.08	.07	.15	.05	.05	.10	.06	.06	.12
Distribution by number (percent)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Checks	50.0	52.3	50.8	46.8	57.2	52.4	46.8	62.7	54.8	43.8	48.5	46.2
ACH	22.1	12.4	18.6	18.0	11.7	14.6	19.8	10.7	15.3	15.2	8.2	11.6
Debit card	19.1	23.6	20.7	27.5	23.5	25.3	25.9	19.1	22.5	32.3	34.4	33.4
ATM	8.9	11.7	9.9	7.8	7.7	7.7	7.5	7.5	7.5	8.7	9.0	8.9
Distribution by value (percent)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Checks	38.0	48.5	40.0	33.3	55.2	40.5	19.2	58.7	25.3	15.5	35.0	20.2
ACH	61.1	49.3	58.9	65.8	43.1	58.3	80.4	39.4	74.1	83.9	62.8	78.8
Debit card	.4	1.2	.5	.6	1.1	.7	.3	1.1	.4	.4	1.4	.6
ATM	.4	1.1	.5	.4	.6	.5	.2	.8	.3	.2	.8	.4
Number per capita	**159**	**88**	**247**	**106**	**125**	**231**	**131**	**131**	**262**	**115**	**122**	**237**
Checks	80	46	126	50	72	121	61	82	144	50	59	110
ACH	35	11	46	19	15	34	26	14	40	17	10	27
Debit card	30	21	51	29	29	59	34	25	59	37	42	79
ATM	14	10	24	8	10	18	10	10	20	10	11	21
Value per capita (dollars)	**346,779**	**78,487**	**425,266**	**209,466**	**102,828**	**312,294**	**484,242**	**88,438**	**572,681**	**380,660**	**120,306**	**500,965**
Checks	131,933	38,085	170,018	69,831	56,796	126,626	92,752	51,923	144,675	59,018	42,164	101,182
ACH	212,018	38,656	250,675	137,725	44,272	181,997	389,360	34,827	424,187	319,260	75,571	394,830
Debit card	1,382	916	2,298	1,160	1,095	2,256	1,319	961	2,280	1,449	1,634	3,082
ATM	1,445	830	2,275	750	665	1,415	812	727	1,539	933	937	1,870
Average (dollars)	**2,178**	**894**	**1,722**	**1,974**	**821**	**1,349**	**3,693**	**675**	**2,185**	**3,309**	**985**	**2,113**
Checks	1,658	829	1,355	1,407	792	1,044	1,511	632	1,008	1,171	713	923
ACH	6,031	3,565	5,450	7,211	3,028	5,397	14,972	2,486	10,601	18,319	7,578	14,410
Debit card	46	44	45	40	37	39	39	38	39	39	39	39
ATM	102	81	93	91	69	79	83	74	78	93	85	89

the smaller population and lower economic output in rural areas (table 7).[33] The relative use of checks was lower and the relative use of electronic debits was higher in urban areas. The proportion of checks, by number, was 60 percent in rural areas and 49 percent in urban areas. The proportions of ACH and debit card payments and ATM withdrawals, by number, were all higher in urban areas, with debit card payments having the largest difference in share—27 percent in urban areas, compared with 21 percent in rural areas.

Generally, the number and value of payments per capita were higher in urban areas, reflecting the greater amount of wealth and business activity in those areas.

Comparison with Earlier Findings

The annual number of check payments declined in all divisions between the 2001 and 2004 depository institution surveys. The most pronounced changes occurred in the South and West, with declines of 32 and 29 checks per capita, respectively, compared with 25 checks per capita in the Midwest. The decline was by far the smallest in the Northeast, at only 7 checks per capita.

33. Note that rural areas include some areas surrounding cities.

6.—Continued

Item	Northeast			South			Midwest			West		
	Multi-region	Single region	All institutions	Multi-region	Single region	All institutions	Multi-region	Single region	All institutions	Multi-region	Single region	All institutions
Number per $1,000 of output	**3.8**	**2.1**	**5.9**	**3.0**	**3.6**	**6.6**	**3.6**	**3.6**	**7.2**	**3.0**	**3.2**	**6.1**
Checks	1.9	1.1	3.0	1.4	2.0	3.5	1.7	2.2	3.9	1.3	1.5	2.8
ACH	.8	.3	1.1	.5	.4	1.0	.7	.4	1.1	.5	.3	.7
Debit card	.7	.5	1.2	.8	.8	1.7	.9	.7	1.6	1.0	1.1	2.0
ATM	.3	.2	.6	.2	.3	.5	.3	.3	.5	.3	.3	.5
Value per $1,000 of output (dollars)	**8,245**	**1,866**	**10,111**	**5,987**	**2,939**	**8,925**	**13,216**	**2,414**	**15,629**	**9,850**	**3,113**	**12,963**
Checks	3,137	906	4,042	1,996	1,623	3,619	2,531	1,417	3,948	1,527	1,091	2,618
ACH	5,041	919	5,960	3,936	1,265	5,201	10,626	950	11,577	8,261	1,956	10,217
Debit card	33	22	55	33	31	64	36	26	62	37	42	80
ATM	34	20	54	21	19	40	22	20	42	24	24	48
Number-to-deposits ratio[1]	**78.1**	**62.0**	**71.5**	**109.8**	**71.2**	**84.9**	**126.2**	**68.0**	**88.4**	**125.3**	**54.8**	**75.4**
Checks	39.0	32.5	36.3	51.3	40.7	44.5	59.1	42.7	48.4	54.9	26.6	34.8
ACH	17.2	7.7	13.3	19.8	8.3	12.4	25.0	7.3	13.5	19.0	4.5	8.7
Debit card	14.9	14.6	14.8	30.2	16.7	21.5	32.6	13.0	19.9	40.5	18.8	25.2
ATM	6.9	7.3	7.1	8.5	5.5	6.5	9.4	5.1	6.6	10.9	4.9	6.7
Value-to-deposits ratio[2]	**170,035**	**55,477**	**123,115**	**216,762**	**58,409**	**114,527**	**465,933**	**45,924**	**193,144**	**414,622**	**54,009**	**159,260**
Checks	64,690	26,920	49,220	72,263	32,262	46,437	89,245	26,963	48,793	64,283	18,929	32,166
ACH	103,958	27,324	72,571	142,522	25,148	66,744	374,638	18,085	143,062	347,744	33,926	125,519
Debit card	678	647	665	1,201	622	827	1,269	499	769	1,578	733	980
ATM	709	587	659	776	378	519	781	378	519	1,017	421	595
Number of institutions	133	2,096	2,229	248	4,540	4,788	186	5,007	5,193	155	1,960	2,115
Population (millions)	...	...	54.4	...	...	104.5	...	...	65.4	...	...	66.4
Output (billions of dollars)[3]	...	...	2,289	...	...	3,657	...	...	2,397	...	...	2,568
Transaction deposits (billions of dollars)	111	77	188	101	184	285	68	126	194	61	148	209

NOTE. Annualized figures based on survey data for March 2004 and April 2004. Multiregion institutions are those that have deposits in more than one region; single-region institutions have deposits in only one region. The Northeast region includes Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, and Vermont. The South region includes Alabama, Arkansas, Delaware, the District of Columbia, Florida, Georgia, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, Texas, Virginia, and West Virginia. The Midwest region includes Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, and Wisconsin. The West region includes Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, and Wyoming.

1. Annual number of debits per $1,000 of transaction deposits.
2. Annual value of debits per $1,000 of transaction deposits.
3. Output is measured as the sum of the gross state products in the region.

SOURCES. Federal Reserve; and Department of Commerce, Bureau of Economic Analysis and Bureau of the Census.

Recall that in the 2004 survey, the number of debit card payments per capita was considerably lower in the Northeast than in other regions and that ATM withdrawals were higher. These findings suggest that the Northeast has lagged other regions in the replacement of checks (and cash) with debit card payments and that the declines in checks in the other regions were being led by a replacement of checks written by individuals rather than businesses. The number of checks per capita also declined more in rural areas than in urban areas, 34 checks per capita compared with 23, suggesting that the replacement of checks with other payment types happened with greater frequency in rural areas.

Returned Check and ACH Payments

Some checks that are presented for payment are returned unpaid because of insufficient funds, closed accounts, fraud, or other reasons. The same is true for ACH payments.[34]

34. Credit card and debit card payments also may fail because of credit limits or insufficient funds, closed accounts, disputes, or fraud. Because most of these types of payments are approved in real time and are not returned in the same sense as checks and ACH payments, they are outside the scope of this discussion.

7. Annual number and value of debits to transaction accounts at depository institutions, in urban and rural areas

Item	Urban	Rural	Total
Number (billions)	**58.4**	**12.2**	**70.5**
Checks	28.9	7.3	36.2
ACH	9.0	1.5	10.5
Debit card	15.5	2.5	18.0
ATM	5.0	.8	5.9
Value (trillions of dollars)	**111.7**	**14.9**	**126.5**
Checks	33.3	5.4	38.7
ACH	77.3	9.3	86.7
Debit card	.6	.1	.7
ATM	.4	.1	.5
Distribution by number (percent)	**100.0**	**100.0**	**100.0**
Checks	49.4	60.2	51.3
ACH	15.4	12.2	14.8
Debit card	26.5	20.7	25.5
ATM	8.6	6.9	8.3
Distribution by value (percent)	**100.0**	**100.0**	**100.0**
Checks	29.8	36.1	30.6
ACH	69.2	62.9	68.5
Debit card	.6	.6	.6
ATM	.4	.4	.4
Number per capita	**248**	**221**	**243**
Checks	122	133	124
ACH	38	27	36
Debit card	66	46	62
ATM	21	15	20
Value per capita (dollars)	**473,857**	**269,636**	**435,165**
Checks	141,369	97,229	133,006
ACH	328,016	169,547	297,992
Debit card	2,628	1,732	2,458
ATM	1,844	1,128	1,708
Average value (dollars)	**1,913**	**1,221**	**1,794**
Checks	1,155	731	1,069
ACH	8,609	6,287	8,279
Debit card	40	38	40
ATM	86	74	85
Number-to-deposits ratio[1]	**82.1**	**74.2**	**80.6**
Checks	40.6	44.7	41.3
ACH	12.6	9.1	12.0
Debit card	21.8	15.3	20.6
ATM	7.1	5.1	6.7
Value-to-deposits ratio[2]	**157,083**	**203,172**	**144,618**
Checks	46,864	32,663	44,202
ACH	108,737	56,957	99,032
Debit card	871	582	817
ATM	611	379	568
Number of institutions	9,745	6,206	15,951
Population (millions)	235.7	55.1	290.8
Transaction deposits (billions of dollars)	711	164	875

NOTE. Annualized figures based on survey data collected March 2004 and April 2004. Urban areas are those defined as metropolitan statistical areas or New England county metropolitan statistical areas; rural areas are defined as those outside urban areas.

1. See table 6, note 1.

2. See table 6, note 2.

SOURCES. Federal Reserve; and Department of Commerce, Bureau of Economic Analysis and Bureau of the Census.

Returned Checks

Checks were returned an estimated 187 million times in 2003 down from about 240 million times in 2000. Some checks returned for insufficient funds are presented again (re-presented) and returned again if funds are still unavailable. Because some checks are returned more than once, and therefore would have been counted more than once in the depository institution survey, the ratio of the number of times checks are returned to total checks is an upper bound on the probability that a check will be returned. It is estimated that check returns constituted, at most, 0.52 percent of estimated total checks in 2003 (or about 5.2 returns for every 1,000 checks presented), compared with 0.58 percent of estimated total checks in 2000 (or about 5.8 returns for every 1,000 checks presented).[35] Thus, the number of returned checks processed through the check collection system declined faster than the total number of checks presented.

One reason for the decline in the proportion of checks returned through the check collection system is that some checks are now being re-presented through the ACH system. When such ACH payments are returned, they are returned through the ACH network and are no longer identified as check returns. In 2003, just less than 23 million checks were re-presented through the ACH.[36] More than half of these ACH check re-presentments (about 12 million) were returned.[37] Thus, the returned checks processed through the check collection system (187 million) and ACH systems totaled close to 200 million, or 5.5 returns for every 1,000 checks presented. The num-

35. The 2004 depository institution survey also collected data on the portion of returned checks that were on-us. Such checks would be returned directly to the depositing customer rather than another depository institution. An estimated 21 million returned checks, or about 11 percent of all returned checks, were on-us. Data on on-us returned checks were not collected in the 2001 depository institution survey. In Gerdes and Walton, "The Use of Checks," reports discussing returned checks for 2000 assumed that the estimates of returns reported by depository institutions did not include on-us returns, and the proportion of returned checks was computed as a percentage of interbank checks, resulting in a larger percentage than reported here. On the basis of the 2004 survey results and a reexamination of the 2001 survey, we believe that depository institutions did include on-us checks in the returned checks reported.

36. National Automated Clearing House Association.

37. It is not known how many of these returned check re-presentments were themselves re-presented.

ber of checks re-presented (and possibly returned) through the ACH system was negligible in 2000.

Returned ACH Payments

About 1.05 percent of retail ACH payments were returned in 2003 (estimated from the electronic payments survey), or 10.5 returns for every 1,000 payments, about twice the rate that checks were returned. Only about 0.06 percent of ACH CCD transactions were returned, a considerably smaller return rate than for checks or for retail ACH payments. Most ACH returns were debit transactions.[38]

When comparing return rates for check and ACH payments, it is important to recognize that differences in technological and industry practice are partly responsible for any differences in observed return rates. The total number of ACH returns is understated because the number of on-us ACH returns is unknown. But ACH returns include certain returns that have no counterpart in the check collection system.

By industry rule, paying depository institutions and their customers have sixty days to return unauthorized retail ACH debits received (debits to an account on the instruction of the payee) but must return checks by midnight of the next business day following presentment.[39] The extra time for ACH returns may allow for the detection and return of erroneous or fraudulent ACH payments—payments that if made by check would have to be pursued through other means and therefore would not be identified as returned checks. Business associations commonly voice more concern about check fraud than ACH fraud because businesses often use accounts that block ACH debits from being received, avoiding any type of fraud or error. Depository institutions typically do not offer accounts that block all ACH debit receipts to individuals but instead require that a specific payment be identified and block ACH payments only on a case-by-case basis.

In contrast to the decline in the rate of returned checks, the rate of returned retail ACH payments increased from 0.79 percent in 2000 to 1.05 in 2003. The increase appears to have been due primarily to higher return rates for new categories of payments. A number of new rules and technological innovations in the ACH system have begun to provide explicitly for and separately identify one-time, nonrecurring ACH debit transactions originated remotely either over the Internet or by telephone or by converting a check to an ACH payment. Such payments may be more likely than recurring payments (which are typically either payroll or mortgage or other bill payments) to be disputed, or to involve erroneous or fraudulent payments, and therefore to be returned.[40] The rate of returned ACH CCDs, which as noted earlier are either internal transfers or business payments, declined slightly from 2000 to 2003.

Use of Cash

About 5.9 billion ATM withdrawals were made in 2003. About two-thirds of these withdrawals were on-us (that is, made from proprietary ATMs belonging to the account holder's depository institution). Therefore, about one-third were from ATMs owned by another depository institution or other company (nonproprietary) and likely involved a withdrawal fee, charged either by the account holder's depository institution or the owner of the ATM, or both.[41] The overall average ATM withdrawal was $85, and the average on-us withdrawal was about $89.

ATM cash withdrawals provide funding for an unknown number of cash transactions. If the average value of payments by cash were known, the number of cash payments that would be funded by the ATM withdrawals could be estimated. For example, if the average cash payment in 2003 was $85, equal to the

38. Precise allocations of returns by debits and credits were not available.

39. If the account does not contain sufficient funds for payment, ACH debits must be returned the day after the transaction was received.

40. Certain types of recurring check payments, such as payroll or mortgage payments, are also less likely to be returned unpaid. Selected data on checks sent to billers that were converted to ACH payments showed a return rate slightly lower than the estimated return rate for checks in 2003.

41. There are exceptions to the practice of charging fees for nonproprietary ATM withdrawals. Some Internet banks, for example, reimburse a portion of withdrawal fees charged by nonproprietary ATM owners, and some ATM owners may waive fees for withdrawals from accounts at certain classes of institution. A Federal Reserve study showed that fees for on-us ATM withdrawals are negligible. See Board of Governors of the Federal Reserve System (2003), *Annual Report to the Congress on Retail Fees and Services of Depository Institutions* (June), www.federalreserve.gov/boarddocs/rptcongress/2003fees.pdf.

average value of ATM withdrawals, the total number of cash payments supported by ATM withdrawals in 2003 would have been 5.9 billion. If the average value of payments from these ATM withdrawals was equal to the average value of PIN-based debit card payments ($38), then the number of cash payments would have been just over two cash payments for each ATM withdrawal, or more than 12 billion. But cash transactions are commonly used for low-value payments. If the average value of cash transactions supported by ATM withdrawals was around $5—about seventeen payments for each ATM withdrawal—then the resulting cash transactions would have totaled more than 100 billion in 2003, compared with an estimated 81 billion noncash transactions in that year.

As the calculations show, a reasonable guess for the average value of a cash transaction could imply a large number of transactions funded by ATM withdrawals. Without supporting data, however, guesses about the average value and implied number of cash transactions are highly speculative and should be viewed as such.

ATM withdrawals do not fund all cash transactions. But, as shown earlier, only a small amount of cash is obtained via PIN-based debit payments compared with the amount obtained from ATMs. Fewer than 600 million PIN-based debit card payments involved cash returned to the card holder. The cash returned to card holders averaged $30. Besides ATM withdrawals and cash back from debit card purchases, the most common means of obtaining cash appears to be cashing payroll checks or personal checks at depository institutions or merchants. According to one study, the means of obtaining cash used most often by individuals in 1984 was cashing a personal or payroll check (77 percent), followed by ATM withdrawals (11 percent).[42]

Industry data show increases throughout the 1990s and early 2000s in the number of ATMs and ATM transactions (which are made for other purposes besides withdrawals), suggesting that the use of ATMs to obtain cash has likely also increased.[43] The use of ATM withdrawals as a means of obtaining cash relative to other means has likely increased since the early 2000s, although how much it has increased is unknown.

Increases in the number and use of ATMs shown by industry data may be an indication that ATMs are replacing checks as a means of obtaining cash. The cashing of personal checks at the teller window of an individual's depository institution results in an on-us check. Recall that the share of on-us checks declined from 2000 to 2003, especially at credit unions (from 6 percent to 2 percent), as the use of ATMs was growing. Therefore, the increases in the number of ATMs and ATM transactions do not necessarily indicate that the use of cash is increasing.

Summary of Findings

Confirming the results of earlier studies, recent survey data show that the number of checks paid in the United States has been declining, although the number of electronic payments has been increasing. Led by growth in debit card payments, the number of electronic payments exceeded the number of check payments in 2003. However, the value of check payments continued to exceed the combined value of the electronic payment instruments studied—debit and credit cards, ACH, and electronic benefits transfers. Some payments that were made by check in the past are now being made with these electronic instruments. Although the surveys discussed in this article provided no direct evidence on cash use, some cash payments likely have been replaced as well.

The 2004 depository institution survey allowed for more detailed study of payments and withdrawals from transaction accounts. For each type of account debit studied—checks, debit card payments, ACH payments, and ATM withdrawals—most were made from accounts at the largest 1 percent of depository institutions (as ranked by value of transaction deposits). Commercial banks showed decreasing shares of checks paid and increasing shares of electronic payments with increasing size. Other differences existed between depository institutions of different types. For example, credit unions, which are generally used by individuals and not by businesses, had the smallest shares of checks and greater shares of debit card and ATM use than commercial banks and savings institutions.

On-us account debits, for which the payer and payee use the same depository institution, were generally more common at the largest depository institutions. Credit unions had very small shares of on-us

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42. See Robert B. Avery and others (1986), "The Use of Cash and Transaction Accounts by American Families," *Federal Reserve Bulletin*, vol. 72 (February), p. 97, table 9.

The authors of this article estimate, on the basis of a survey on individual checks, that in 2000 fewer than 2 percent of checks written had "Cash" as the payee. Writing "Cash" on the payee line is common when obtaining cash via check at a depository institution teller but may not be done when obtaining cash via check at other venues. Thus, checks made out to "Cash" represent only a portion of all checks written for cash in 2000.

43. ATM and Debit News, *EFT Data Book, 2005 Edition*, Thomson Media, www.cardforum.com.

account debits compared with the other types of institutions, likely reflecting the relatively small number of person-to-person payments made by check and ACH. The on-us share of ATM withdrawals was high for all types and sizes of depository institutions, reflecting the existence of fees for withdrawals from nonproprietary ATMs.

The use of different types of payment instruments varies across regions of the country, suggesting differences in the cost, availability, willingness to use, or willingness to accept various payment instruments. The 2004 depository institution survey showed that the use of debit cards was significantly more common, per capita, in the West than in other regions. In this region and others, some debit card payments were likely being made in lieu of payments by check, but debit cards may also have been used instead of cash or credit cards. The Northeast showed significantly less use of debit cards than other regions and, compared with estimates from the 2001 depository institution survey, a significantly slower decline in the use of checks. Individuals in the Northeast obtained more cash from ATMs, and the average value of their debit card payments was higher.

While check and ACH returns are not entirely comparable, it is interesting to note that the proportion of ACH payments that were returned was almost twice the proportion of checks that were returned. The proportion of returned checks declined from 2000 to 2003, but the proportion of returned ACH payments increased. The increase in the proportion of returned ACH payments was related not to an increase for traditional types of ACH payments, but rather for new types of ACH transactions, such as the conversion of checks to ACH payments and one-time payments over the Internet and telephone.

Data on the use of the payments system such as those presented in this article are important to policymakers, the public, and the payments industry for a variety of reasons. The information may aid in understanding the purposes for which different payment types are used, helping financial institutions, payments networks, service providers, and other payments organizations better understand and serve the public. Depository institutions can use the information to compare the relative use of payments with the relative use of payments at groups of similar depository institutions. Historical trends in the use of payments and information on patterns of substitution and replacement among payment types may aid in forecasting trends. Forecasts based on the information may help in planning payments system infrastructure and in the timing and appropriateness of new investments in determining infrastructure. Finally, the data may help policymakers and the public better understand and monitor the significant changes occurring in the U.S. payments system.

APPENDIX: SOURCES OF DATA AND METHODS OF ESTIMATION

Both the 2003 and 2000 data used to estimate the number and value of noncash payments came from two separate surveys. The estimates for 2003 came from two surveys conducted in 2004—one of depository institutions (the 2004 depository institution survey) and the other of electronic payments networks, card issuers, and card processors (the 2004 electronic payment survey).[44] The estimates for 2000 came from 2001 surveys, one of depository institutions (the 2001 depository institution survey) and the other of electronic payments networks, card issuers, and card processors (the 2001 electronic payment survey).[45]

The 2001 and 2004 depository institution surveys were similar in most respects. However, the 2001 survey collected information only about checks, whereas the 2004 survey also collected information about other debits to transaction accounts. The 2001 and 2004 electronic payment surveys were also similar. Except as noted, the descriptions of the 2004 surveys presented below also apply to the 2001 surveys.[46]

2004 Depository Institution Survey

Survey Design

The 2004 depository institution survey collected information from three types of institutions: commercial banks (including agencies and branches of foreign banks); savings institutions (savings banks and

44. Global Concepts, Inc., and International Communications Research (ICR) assisted the Federal Reserve System with the 2004 depository institution survey. See Federal Reserve System (2004), *The Depository Institutions Payments Study: A Survey of Depository Institutions for 2004 Federal Reserve Payments Study*, Global Concepts and Federal Reserve System, www.frbservices.org/Retail/pdf/2004DIPaymentStudy.pdf. Dove Consulting assisted with the 2004 electronic payment survey. See Federal Reserve Bank of Atlanta (2004), *2004 Electronic Payments Study for Retail Payments Office at the Federal Reserve Bank of Atlanta: Study Methods and Results Summary Report*, Federal Reserve Bank of Atlanta Study (December 14), www.frbservices.org/Retail/pdf/2004EPStudy.pdf.

45. Global Concepts, Inc., and Westat assisted the Federal Reserve System with the 2001 depository institution survey, and Dove Consulting assisted with the 2001 electronic payment survey.

46. See Gerdes and Walton, "The Use of Checks," for a discussion of the 2001 surveys. Also see Federal Reserve System, *Retail Payment Research Project*.

savings and loan associations); and credit unions. The types of debits surveyed were checks, ACH payments, debit card payments (both signature-based and PIN-based), and ATM withdrawals. (Wire transfers and teller window withdrawals, which create debits, as well as credit card and currency payments, were outside the scope of the survey.)

Depository institutions were asked to report, by questionnaire, the number and dollar value of debits to their accounts by each type of debit during each of the months March and April 2004. They were also asked to report the number and value of returned checks and, for all debit types except debit card transactions, the number and value of on-us debits.

The population from which the 2004 sample was drawn comprised 14,117 depository institutions (bank subsidiaries of multibank holding companies were treated as a single entity) that reported transaction deposits greater than zero as of September 2003 (June 2003 for credit unions). Based on experience with the 2001 depository institution survey, which had a 54 percent response rate, a stratified random sample of 2,700 depository institutions was estimated to be needed to produce national estimates of the number and value of debits made via check with a desired precision of at least ±5 percent for a 95 percent level of confidence.

For sampling and estimation purposes, depository institutions were separated into five groups. Commercial banks were divided into two types—domestically chartered banks and branches of foreign banks—and savings institutions were divided into two types—those federally regulated by the Office of Thrift Supervision and those regulated by states. Credit unions made up the fifth group. The largest institutions in each group, as determined by the value of their transaction deposits, and some institutions known to have highly unusual check volumes, such as issuers of rebate checks, were sampled with certainty. The remaining institutions in each group were then stratified by the value of their transaction deposits—nine strata for commercial banks (including three for foreign bank branches), five strata for credit unions, and six strata for savings institutions (three for federally regulated institutions and three for state-regulated).

Data from the 2001 survey were used to approximate the standard error that would be achieved for different sample allocations (the number of depository institutions to be sampled in each stratum, based on a sample size of 2,700), and the final sample allocation was determined so as to minimize the approximate standard error of the estimated total number of checks. Because the strata with the larger depository institutions typically had greater numbers of checks paid in the 2001 sample, and had greater variance between them, they were assigned a larger proportion of the sample by the minimization algorithm. The allocation of the sample between the depository institution types gave more weight to commercial banks because they were expected to account for a disproportionate share of checks and other account debits; but it also took into account the desirability of producing estimates for each depository institution type.

In all, 1,572 commercial banks, 328 savings institutions, and 800 credit unions were included in the sample. Responses were received from 869 commercial banks, 193 savings institutions, and 438 credit unions, giving response rates slightly higher than for the 2001 survey. All of the 44 largest commercial banks responded (this group accounted for more than half the estimated total for nearly every item in the survey). The largest savings institutions and credit unions also responded.

By the time survey data were available, data on transaction deposits as of March 31, 2004, were also available. Using those transaction deposits data, the sample and population were re-stratified to produce estimates for the 14,120 depository institutions in existence on April 30, 2004, the end of the period for which data were collected. The major change resulting from the re-stratification was an adjustment to the largest size stratum for each depository institution group so that it would be a certainty stratum (that is, all members of the stratum must have responded to the survey, although not necessarily to each item). The makeup of the strata also changed somewhat as a result of the entry and exit of some institutions between November 2003, when the sample was drawn, and April 2004, and of changes in the value of transaction deposits that occurred between September 2003, when transaction deposits used for the sample selection were reported, and March 2004.

Item Nonresponse and Imputation

Once the figures for March and April were aggregated (and annualized by multiplying the sums by 6), the desired sample dataset consisted of 42,000 cells—(1,500 depository institutions) × (14 debit categories) × (number + value). Of these, data for 12,274 cells, or 29.2 percent, were not reported. For the totals by instrument, incidence of nonresponse varied from a low of 5.6 percent for the number of checks to a high of 45.4 percent for the value of PIN-based debit card payments.

The nonresponse rates suggest that for checks, and to a lesser extent for debit cards and ATM transactions, numbers are easier to report than values, whereas for ACH transactions, values are slightly easier to report than numbers.

But, as noted in the text, some depository institutions could not accurately report ACH payments. Discussions with respondents indicated that at least some of them had difficulty distinguishing between true ACH payments and some very large-value internal funds transfers, called offset entries (which are not considered payments) that were processed in-house (on-us) on a shared platform. These offset entries were large in value but small in number, resulting in elevated average values for both on-us and total ACH transactions for some institutions.

Not all depository institutions have an automated capability to report the number and value of payments by instrument as requested by the survey. Some respondents could not report the requested items at all. Of those that could, many needed to request the information from a payments processing service provider or a correspondent depository institution or had to set up systems to collect the information specifically to respond to the survey.

To create a rectangular dataset suitable for a variety of analyses, each of the missing items was imputed using a multiple imputation procedure.[47] For each missing item, the imputation procedure used information from the other depository institutions in the same stratum that reported the missing item and from any related items that were reported by the institution with the missing item. The imputation procedure fit a linear regression model of the logarithm of the missing item (the dependent variable) to the logarithms of related items (the independent variables) and a constant term.[48] (At least one independent variable—transaction deposits—was always available.) The fitted regression yielded a predicted value and an associated standard deviation for the missing item. To arrive at an imputed value, a random deviate, drawn from a normal distribution with a mean of zero and the standard deviation from the fitted regression, was added to the predicted value. Occasionally the regressions yielded inconsistent imputations for items known to be subsets of totals (for example, for some institutions the imputations of on-us checks exceeded their total checks). In this relatively small number of cases, a different imputation was used—the one for which the ratio of the imputed subset to the total was equal to the mean of the same ratio for other depository institutions in the stratum.

This imputation procedure was repeated five times, each time using a newly drawn deviate in the calculation, to obtain five datasets containing both actual responses and imputations. All the summary statistics based on this 2004 depository institution survey are averages of estimates calculated from the five datasets. The variation among the five estimates provides information about the uncertainty in the overall estimate arising from the imputations.

Estimation

The actual and imputed data for respondents were converted to estimates for the population using a separate ratio estimator, with the value of transaction deposits being the covariate for each item. That is, for a given item and within a depository institution type–size stratum, the sum of the respondents' data was multiplied by the ratio of the transaction deposits in the population to the transaction deposits at the responding institutions. The associated sampling standard error was based on a classical statistical formula that accounts for the uncertainty arising from the use of a sample rather than a census, and on the variation among imputed figures that accounts for the uncertainty arising from the fact that some items needed to be imputed.

In terms of sampling error, the estimates turned out to be more precise than expected at the time the sample size was set. The 95 percent confidence intervals for the national estimate of checks were ±1.8 percent of the number of checks paid and ±2.2 percent of the value. This better-than-expected performance appears to be a result of a larger-than-expected number of respondents (20 percent more than for the 2001 survey), greater-than-expected response rates for the largest institutions, and less within-sample variation than for the 2001 depository institution survey. The confidence intervals for the national estimates of other debit activity were narrower than ±5 percent with four exceptions: number and value of on-us ACH credit and debit transactions that were cleared through the ACH network rather than in-house.[49] These survey items were much less

47. For an overview of multiple imputation techniques, see Donald B. Rubin (1987), *Multiple Imputation for Nonresponse in Surveys*, John Wiley and Sons (New York).

48. Using the logarithms of the data is a common approach in the regression analysis of models that posit a constant linear relationship between the percent change of the dependent variable and the percent changes of the independent variables and in which all variables are limited to nonzero values.

49. ACH credit and debit transactions were estimated separately but were aggregated in the tables in this article.

correlated with the level of transaction deposits than were the other items.

Estimates by Geographic Region and Urban or Rural Location of Deposits

Although the survey was not explicitly designed to facilitate geographic analysis of account debit patterns, the responses were sufficient, when combined with external data on each depository institution's total deposits distributed by region, to make broad comparisons possible. For each of the four regions—Northeast, South, Midwest, and West—separate estimates were calculated for single-region depository institutions (those having deposits in only one region) and multiregion depository institutions (the 322 institutions having deposits in more than one region).

The survey did not directly collect regional data from multiregion depository institutions. The geographic distribution of depository institutions' total deposits (including both transaction and savings deposits) were available, so each type of account debit for each multiregion depository institution in the population was assumed to be distributed across regions in proportion to the location of its deposits, and were allocated to regions accordingly.[50] (No such assumption was necessary to allocate data for single-region depository institutions.)

To produce the regional estimates, depository institutions' regionally allocated data were restratified by region, type, and size and by multiregion or single-region status. For each region, separate estimates were produced for single-region depository institutions and the allocated portion of multiregion depository institutions' data. New, separate ratio estimators were produced using these strata following the procedure described in the preceding section. It turned out that national estimates obtained from aggregating these regional estimates were about the same as those obtained from the original analysis and were adjusted to make the aggregates match without affecting the proportions allocated.

The assumption that the payments and transaction deposits of depository institutions are regionally distributed in proportion to the distribution of their deposits is consistent with the hypothesis that customers of multiregion depository institutions who are located in different regions exhibit payments behavior more similar to each other than do customers of different depository institutions who are located in different regions. The assumption used to construct these regional aggregates—namely, that each regional fraction of a depository institution's customers exhibit similar payments behavior—may be overly restrictive and could affect the accuracy of regional estimates. That is because the assumed allocation of transaction deposits or account debits would be too large (too small) for a region if the true allocations for the institution were lower (higher) in that region.

The uncertainties that arise from allocation of data to regions described above cause difficulties for the statistical analysis of the estimated differences among regions. If large differences actually exist between the proportions of payments a depository institution processes for a pair of regions, the assumption mutes the estimated differences between that pair of regions. It makes the two regions appear more similar than they really are. The same assumption may also create the appearance of a difference with a third region that may not exist in reality. This potential problem can be illustrated by the following hypothetical example: Suppose that check activity is higher in the Northeast than in the South and that there is no difference (in fact) between the South and the Midwest. Then our procedure for allocating the data of a depository institution with a presence in the Northeast and South may mask the difference between the Northeast and South while creating an apparent difference between the South and the Midwest.

Sampling standard errors were not calculated for the regional estimates because of uncertainty about the effects of the allocation of data for multiregion depository institutions. However, the results of cross-sectional regressions, one of which is mentioned in the body of this article, together with the similarity between the patterns of multiregion and single-region estimates as well as the regional patterns for checks identified in both the 2004 and 2001 surveys, demonstrate that regional differences do exist.

Estimates of urban and rural account debit activity were constructed using a method similar to that used to construct estimates by region. Urban areas were defined as metropolitan statistical areas, and rural areas as all other areas. Thus, some urbanized areas, such as certain outlying suburbs that surround metropolitan statistical areas, were included in the rural regions.

The 2004 Electronic Payment Survey

The 2004 electronic payments survey sent questionnaires to all electronic payments networks, card issu-

50. For credit unions, the geographic distribution of an institution's branches served as a proxy for the geographic distribution of its total deposits.

ers, and card processors to estimate the number and value of electronic payments originated in the United States in 2003 with commonly used payment instruments—general-purpose and private-label credit cards, signature-based and PIN-based debit cards, ACH payments, and electronic benefits transfers.

The collection of these data was straightforward because the processing of electronic payments is largely centralized and the respondents can generally supply accurate data on the number and value of these payments from business records. Payments for issuers that did not respond to the survey were estimated from available information, but they represented a small share of the estimated totals.

For estimates of total ACH payments, data from the 2004 depository institution survey were used to estimate the fractions of ACH transactions, by number, that were on-us and cleared in-house (separately for debit and credit transactions). The estimated fractions were combined with electronic payment survey data to estimate on-us ACH payments for 2003, and these data were added to the network ACH payments in 2003 to yield estimates for all ACH. The same fractions were used to estimate on-us ACH payments for 2000; the resulting estimates of the total number and value of ACH payments for that year are a revision from estimates provided in earlier reports. □

Community Banks and Rural Development: Research Relating to Proposals to Revise the Regulations That Implement the Community Reinvestment Act

Robert B. Avery, Glenn B. Canner, and Shannon C. Mok, of the Division of Research and Statistics, and Dan S. Sokolov, of the Division of Consumer and Community Affairs, prepared this article. Onka L. Tenkean provided research assistance.

Since 1977, the Community Reinvestment Act (CRA) has required that federally insured banking institutions—commercial banks and savings associations—be evaluated on their records of helping to meet the credit needs of their local communities, including low- and moderate-income (hereafter, lower-income) neighborhoods. In 1995, the four federal agencies responsible for bank supervision substantially revised the regulations that implement the CRA.[1] The revisions were intended to emphasize performance rather than process, to reduce unnecessary regulatory burden, and to increase consistency in CRA evaluations.

Under the 1995 regulations, "large" institutions, generally those with assets of $250 million or more, have been evaluated under a three-part test, whereas "small" institutions, generally those with assets of less than $250 million, have been subject to comparatively streamlined evaluations. Large institutions have been required to report data annually on certain types of CRA-related loans (small-business, small-farm, and community development loans) and on the geographic areas (for example, census tracts) that constitute their local communities, whereas small institutions have been exempt from such reporting.

In 2001, the agencies began reviewing the CRA regulations to determine whether they were successful in meeting the objectives that the agencies set forth in 1995. The review focused in part on the possibility of extending the eligibility for streamlined examinations and the exemption from data reporting to more institutions. In 2004 and 2005, the agencies put forth several proposals to implement these changes by raising the asset-size threshold from $250 million to $500 million or $1 billion. The proposals, and the public's comments on them, paid particular attention to how and when to evaluate the community development performance of banking institutions with assets of less than $1 billion, especially in rural areas, where such institutions have a proportionately larger presence than in urban areas. A related but separate issue that the agencies presented for public comment was how to define which bank activities in rural areas should be considered community development in CRA evaluations.

We have evaluated a large amount of data to gain insight into the potential effects of these proposals, and in this article we report the key findings of our research. Our intent is to inform deliberation over the recent proposals, not to advocate any particular view.

BRIEF DESCRIPTION OF THE CRA

The CRA encourages federally insured banking institutions to help meet the credit needs of their communities, including lower-income neighborhoods, in a way that is consistent with the safe and sound operation of those institutions.[2] In particular, the CRA directs the federal agencies responsible for bank supervision (1) to assess through examinations every institution's record of meeting such community credit needs and (2) to consider the institution's CRA record when evaluating its application for deposit insurance or for a charter, branch or other deposit facility, office relocation, or merger or acquisition.

The CRA gives the agencies broad discretion to implement the law. For example, the act does not

1. The agencies are the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS).

2. For a more expansive overview of the history of the CRA, see Griffith L. Garwood and Dolores S. Smith (1993), "The Community Reinvestment Act: Evolution and Current Issues," *Federal Reserve Bulletin*, vol. 79 (April), pp. 251–67.

define "low- or moderate-income neighborhood" or a banking institution's "community"; rather, the act leaves those definitions to the agencies. The act also leaves to the agencies the establishment of criteria for rating an institution's record of meeting its community's credit needs. Each agency has separate rule-writing authority for the institutions it supervises; but with one recent exception, the four agencies have adopted identical regulations.[3]

The 1995 regulations establish objective standards for measuring performance. Rather than providing specific lending thresholds for particular CRA ratings, however, the standards are flexible and are applied in the context of information about an institution, its community, and its competitors (broadly referred to as the institution's "performance context"). Moreover, the standards relate not only to the quantity of an institution's activities (for example, the dollar amount of mortgage loans extended) but also to the quality of those activities (that is, their correlation with the community's needs for credit).

Examiners evaluate institutions primarily on their performance in their local communities, which the regulations define as the institutions' "assessment areas." Assessment areas encircle an institution's deposit-taking facilities, such as its branches and, if applicable, its automated teller machines (ATMs). Assessment areas are composed of census tracts or aggregations of census tracts, such as counties or metropolitan statistical areas. Examiners consider an institution's performance outside its assessment area only in limited circumstances.

Transparency is an important aspect of the regulations. Every institution's CRA rating—either "outstanding," "satisfactory," "needs to improve," or "substantial noncompliance"—is made public, as is a written evaluation that explains the basis of the rating.[4] Moreover, large banking institutions must report loan data to their supervisory agencies, which make the data publicly available. Large institutions must report the number and dollar amount of their small-business and small-farm loans by individual census tract. They must also report the total number and dollar amount, but not the geographic distribution, of their community development loans. In addition, if an institution is subject to the reporting requirements of the Home Mortgage Disclosure Act (HMDA), it is required to disclose detailed information about its mortgage loans; if the institution is also large for CRA purposes, it must report geographic information for rural mortgage loans, which it otherwise does not need to report.[5]

The criteria in the 1995 regulations for evaluating an institution's performance incorporate four key distinctions. First, the criteria distinguish large banking institutions from small ones. Large banking institutions are subject to a three-part test that looks at lending, investments, and services, whereas small banking institutions face a streamlined test that concentrates on lending (see boxes "The Large-Institution Evaluation" and "The Small-Institution Evaluation"). Moreover, large banking institutions must report data to the agencies; small banking institutions need not do so.

Second, the criteria distinguish among types of banking activity: lending, investing, and providing services. The regulations require the agencies to give large banking institutions explicit sub-ratings on each of these types of activity. Although small banking institutions are not usually evaluated on their investments or services, they may improve their chances of receiving an "outstanding" CRA rating if they elect to be evaluated in those areas.

Third, the evaluation criteria reflect a distinction between area-based and recipient-based measures of performance. The CRA's measure of area is the census tract. Key area-based criteria in CRA evaluations include the proportion of an institution's retail loans, and the proportion of its branches, in lower-income census tracts. Categories of census tract income are determined by the ratio of a census tract's median family income to the median family income of the relevant surrounding area as established at the most recent decennial census. The ranges are 0–49 percent (low), 50–79 percent (moderate), 80–119 percent (middle), and 120 percent or more (upper). For a census tract in a metropolitan (urban) area, the relevant surrounding area is the metropoli-

3. Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision (1995), "Community Reinvestment Act Regulations," *Federal Register*, vol. 60 (May 4), pp. 22156, 22178.

4. CRA ratings, the type of evaluation (for example, small-institution or large-institution), the date of the evaluation, and the name of the agency that conducted the evaluation are available from the Federal Financial Institutions Examination Council (FFIEC) at www.ffiec.gov. Comprehensive written evaluations, including "sub-ratings," are available through links from the FFIEC's website to the websites of the supervisory agencies, which post the evaluations as PDF files. The sub-ratings are available in written form only; they are unavailable in a quantitative, easy-to-use format that would facilitate analysis.

5. Institutions that are large under the CRA and are covered by HMDA must report the census tracts of all properties for which loans have been extended or for which loan applications have been received unless the loan is made or the application is received in a county with a population of 30,000 or less, in which case reporting the census tract is optional. Small institutions covered by HMDA may, but need not, report the property locations (census tracts and counties) for their rural loans.

The Large-Institution Evaluation

The regulations that implement the CRA establish three tests by which the performance of most large retail banking institutions is evaluated: a lending test, an investment test, and a service test.

The *lending test* measures lending activity for many types of loan, including home mortgage, small-business, and small-farm loans. The assessment criteria are the proportion of an institution's loans in its assessment areas, the distribution of lending across borrowers of different incomes, the distribution of lending across census tracts of different incomes, the extent of community development lending, and the use of innovative or flexible lending practices to address the credit needs of lower-income individuals or areas.

The *investment test* considers a banking institution's qualified investments that benefit its assessment area or a broader statewide or regional area that includes its assessment area. A qualified investment is a lawful investment, deposit, membership share, or grant that has community development as its primary purpose.

The *service test* considers the availability of an institution's system for delivering retail banking services and judges the extent of its community development services and their innovativeness and responsiveness. Among the assessment criteria for retail banking services are the geographic distribution of an institution's branches and the availability and effectiveness of alternative systems for delivering retail banking services, such as automated teller machines, in lower-income areas and to lower-income persons.

The Small-Institution Evaluation

Small institutions are eligible for streamlined CRA evaluations and are exempt from CRA data reporting obligations. The performance of a small institution is measured by its efforts to help meet the credit needs of its assessment area. These efforts are evaluated according to the following criteria:

- the institution's overall ratio of loan dollars to deposits
- the percentage of loans or, as appropriate, other lending-related activities in the assessment area
- the institution's record of lending to borrowers of different income levels and to businesses and farms of different sizes
- the geographic distribution of the institution's loans
- the institution's record of responding to written complaints about its performance in helping to meet credit needs in assessment areas

tan area. For a census tract in a nonmetropolitan (rural) area, the relevant surrounding area is the entire nonmetropolitan region of the state. Baseline classifications of census tract income change every ten years with the release of the census.[6]

In addition to area-based measures of performance, CRA evaluations use analogous recipient-based measures. Examples include the proportion of an institution's loans extended to lower-income borrowers (in the case of mortgage and consumer loans) and to enterprises of different sizes (in the case of small-business and small-farm loans) and the proportion of an institution's services offered to lower-income individuals. The evaluation criteria classify borrowers by income in relation to the median family income of the relevant surrounding area. In doing so, the criteria use the same percentage breakdowns used to classify census tracts by income and the same metropolitan–nonmetropolitan distinction to construct the baseline. The main difference between the classifications for borrowers and those for census tracts is that baseline classifications for borrowers are updated every year, when the Department of Housing and Urban Development publishes the estimates of area family income, whereas those for census tracts are updated every ten years.

Fourth, the evaluation criteria distinguish between retail activities, which are often regarded as the traditional business of a banking institution, and community development activities, which are intended primarily to improve the welfare of lower-income people or areas. The regulation recognizes four categories of community development activity, three of which (affordable housing, community services, and economic development through small-business or small-farm financing) target certain recipients—lower-income people, small businesses, or small farms—and one of which (revitalization and stabilization) targets certain areas—lower-income census tracts. For a large institution, community development performance is a factor in the CRA sub-rating on each of the three activity-based tests (lending, investment, and service). In the case of the investment test, the sub-rating depends entirely on the institution's record of making community development investments, whereas in the case of the lending and service tests, the sub-rating depends, respectively, on the institution's record of providing retail and community development loans and on its record of providing retail and community development services.

For a small institution, unlike for a large one, community development performance is not a man-

6. Some tract classifications adjust more frequently than once a decade because of changes in the boundaries of metropolitan areas.

datory part of the evaluation. But a small institution may choose to be evaluated on its community development loans, investments, or services as a basis for possibly boosting the institution's rating from "satisfactory" to "outstanding."

THE AGENCIES' PROPOSALS TO AMEND THE CRA REGULATIONS

In 1995, when the four banking agencies adopted major amendments to the regulations that implement the CRA, they committed themselves to reviewing the amended regulations to assess the regulations' effectiveness in emphasizing performance over process, promoting consistency in evaluations, and eliminating unnecessary regulatory burden.[7] They began that review in July 2001 with the publication in the *Federal Register* of an advance notice of proposed rulemaking.[8] Since early 2004, the agencies have issued several proposals.

Recent CRA Proposals

In February 2004, the banking agencies issued identical proposals to amend their respective CRA regulations to increase the number of institutions classified as small.[9] Under the 1995 regulations, an institution is defined as small if it has less than $250 million in assets and is not a member of a holding company that has $1 billion or more in assets. Institutions not defined as small are classified as large.[10] The four agencies proposed to expand the definition of "small institution" to cover those institutions with assets of up to $500 million and to eliminate the holding company criterion.

Commenters on that proposal were deeply split. Industry commenters, seeking to reduce their regulatory burden, wanted to raise the large-institution threshold higher than was proposed (as high as $2 billion). But community groups opposed any increase in the threshold, asserting that an increase would lead institutions newly classified as small to reduce their investments in community development.

In July 2004, the OTS announced that it would raise the large-institution threshold for savings associations to $1 billion, the OCC announced that it would refrain from adopting the February proposal, and the Board stated that it would formally withdraw the proposal from consideration.[11] The Board explained that raising the large-institution threshold to $500 million was not guaranteed to yield significant cost savings for institutions and that it might significantly reduce investments in community development in some rural communities.[12]

A month later, the FDIC issued a new proposal to raise the large-institution threshold to $1 billion for FDIC-supervised institutions and to continue to evaluate institutions with assets between $250 million and $1 billion on their community development records but on a modified basis.[13] Again, commenters were divided over the proposal. Many industry commenters opposed evaluating these institutions on their community development records; many community group commenters contended that the proposed evaluation was not rigorous.

Also in August 2004, the FDIC proposed that a bank activity that benefits an individual or a community in a rural area be considered community development under the CRA, even if neither the individual nor the community is of lower income. Commenters also split on that proposal. Some expressed concern that the agency would give CRA recognition to bank investments in affluent rural areas. Some supported the proposal, however, because they favored recognizing institutions' support of infrastructure, business development, and other needs in rural areas as community development.

In November 2004, the OTS, too, proposed to recognize as community development a bank activity that benefits an individual or a community in a rural area, even if neither the individual nor the community is of lower income.[14]

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7. OCC, Board, FDIC, OTS (1995), "Community Reinvestment Act Regulations," pp. 22156, 22178.

8. Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision (2001), "Community Reinvestment Act Regulations," advance notice of proposed rulemaking, *Federal Register*, vol. 66 (July 19), p. 37602.

9. Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision (2004), "Community Reinvestment Act Regulations," *Federal Register*, vol. 69 (Feb. 6), p. 5729.

10. To be considered large, an institution must fail to meet the criteria for a small institution as of December 31 of both of the previous two calendar years.

11. The OTS implemented its increase in a final rule published on August 18, 2004. See Office of Thrift Supervision (2004), "Community Reinvestment Act Regulations," *Federal Register*, vol. 69 (Aug. 18), p. 51155.

12. See Board of Governors of the Federal Reserve System (2004), press release, July 16, www.federalreserve.gov/boarddocs/press/all/2004.

13. Federal Deposit Insurance Corporation (2004), "Community Reinvestment Act Regulations," *Federal Register*, vol. 69 (Aug. 20), p. 51611.

14. Office of Thrift Supervision (2004), "Community Reinvestment Act—Community Development, Assigned Ratings," *Federal Register*, vol. 69 (Nov. 24), p. 68257.

The Three-Agency Proposal of February 2005

In February 2005, the Board, the OCC, and the FDIC published for public comment a joint proposal, which again addressed the definitions of "small institution" and "community development" in rural areas. The proposal would modify the CRA regulations in three ways:

1. It would raise the asset threshold for a large institution from $250 million to $1 billion and would eliminate the holding company criterion. Thus, all banking institutions with less than $1 billion in assets would be exempt from CRA data reporting obligations.

2. It would create a subcategory of small institutions called "intermediate small institutions," those with assets between $250 million and $1 billion, and would subject such institutions to a two-part evaluation.[15]
   - One part would evaluate the institution's retail lending. The evaluation would use the criteria now used for small institutions (those with less than $250 million in assets)—for example, the ratio of overall loan dollars to deposits and the distribution of loans across borrowers and areas of different relative incomes. Those criteria differ little in substance from the criteria applied to the retail lending of large institutions, but the evaluation of small institutions' retail lending is, in practice, more streamlined because of their exemption from the requirement to collect or report data on loans and assessment areas.
   - A second part, given equal weight in assigning an overall CRA rating, would evaluate an intermediate small institution's community development record. Instead of considering that record in three separate tests (as does the large-institution evaluation, which now applies to intermediate small institutions), the evaluation would gather into one test all community development activities, regardless of type, including lending, investing, and providing services.

3. It would revise the definition of "community development" in rural areas—for institutions of any size. The definition in the 1995 regulations imposes a lower-income restriction on bank activities that may be credited as community development in CRA evaluations: Such activities must primarily benefit either lower-income people or lower-income areas. The agencies proposed to relax that restriction in rural areas.
   - Under the proposal, bank activities would be considered community development if they revitalized or stabilized any "underserved rural area" or provided affordable housing for any individual in any such area, even if the area was not defined as "low or moderate income." The agencies sought comment on how to identify underserved rural areas not already classified as lower-income tracts. The agencies specifically sought comment on criteria adapted from the Community Development Financial Institutions Fund's definition of an "investment area." The criteria, as adapted, would identify as underserved an area that has at least one of the following characteristics: (1) an unemployment rate of at least 1.5 times the national average, (2) a poverty rate of 20 percent or more, or (3) a population loss of 10 percent or more between the previous and most recent decennial censuses or a net migration loss of 5 percent or more over the five-year period preceding the most recent census.
   - The agencies also sought comment on an alternative proposal to liberalize the definition of a "low or moderate income" rural census tract in one of two ways, at least for the purpose of determining which area-based activities in rural areas are considered community development: (1) change the baseline for defining rural tract incomes from the nonmetropolitan state median income to the statewide median income, which is the higher of the two statistics in all but one state, or (2) raise the "low or moderate income" limit from its current level of 80 percent.

15. The proposal would leave unchanged the criteria for evaluating small institutions (those with less than $250 million in assets); as noted earlier, these criteria concentrate on retail lending (see box "The Small-Institution Evaluation"). The proposal would also leave unchanged the criteria for evaluating large institutions (those with more than $1 billion in assets), which would continue to be subject to a three-part evaluation (see box "The Large-Institution Evaluation").

EFFECTS OF RAISING THE ASSET-SIZE THRESHOLD

As noted earlier, the 2005 proposal would raise the asset-size threshold for a large institution from $250 million to $1 billion and would eliminate the holding company criterion. Institutions with asset sizes below the $1 billion threshold would be subject to a streamlined CRA lending test equivalent to that now used for small institutions; they would also be exempt from the evaluation of branching under the service test now applied to institutions with assets of more than $250 million.[16] The proposal would also create a new community development test for intermediate small institutions.

In the first part of this section, we analyze several issues related to this portion of the proposal.[17] First, we identify and describe the institutions and banking markets that would be affected by raising the threshold to $1 billion and eliminating the holding company criterion. Second, we examine the potential effect of using a streamlined version of the CRA lending test and eliminating the service (branching) test for institutions with asset sizes below the threshold. Specifically, we examine the effect of the current $250 million threshold on the retail lending and branching activities of institutions within a narrow range of the current threshold. Third, we consider whether the role of community development lending in CRA ratings has been significant.

Parties Affected by Raising the Threshold and Eliminating the Holding Company Criterion

Raising the threshold and eliminating the holding company criterion would affect both banking institutions and the communities they serve. Using 2003 as a test year, we looked at the characteristics of institutions that would have been subject to a different CRA evaluation process had the regulations proposed in February 2005 been in effect.[18] We also identified the local banking markets that might have been most affected had the threshold been raised.

Banking Institutions

As of December 31, 2003, 9,095 banking institutions were subject to the CRA (table 1). We estimate that, of those, 1,621 institutions that were considered large as of that date would be considered intermediate small or small under the agencies' 2005 CRA proposal (columns 1–3). These "status-changing" institutions constituted 18 percent of all institutions subject to the CRA, and they held 13 percent of the deposits held by all such institutions. Intermediate small institutions consisted of 1,264 institutions that had between $250 million and $1 billion in assets (column 2) and 116 institutions that had more than $1 billion in assets but which would not be considered large under the proposal because of a proposed requirement to exceed the asset threshold for two consecutive years (column 3). The "newly small" institutions consisted of the 241 institutions that had assets of less than $250 million but which nonetheless were subject to the large-institution CRA examination in 2003, generally because they were part of a bank holding company with assets of more than $1 billion (column 1).[19] These institutions would be considered small under the 2005 proposal.[20]

The 1,621 status-changing institutions differ from other CRA-covered institutions along a number of dimensions. First, 28 percent of the status-changing institutions had headquarters in nonmetropolitan areas, compared with 7 percent of institutions with assets exceeding $1 billion and 52 percent of small banking institutions. Of the status-changing institutions with headquarters in nonmetropolitan areas, 60 percent had headquarters in exurban counties (nonmetropolitan counties adjacent to metropolitan areas) and 40 percent in remote counties (counties not adjacent to metropolitan areas).[21] Second, 14 percent of the status-changing institutions had "outstanding" CRA performance ratings at their last examinations, compared with 37 percent of larger institutions and 11 percent of small institutions.

Local Banking Markets

Another way to look at the effect of raising the threshold is in terms of local banking markets. There

16. Under the proposal, intermediate small institutions would not be subject to the large-institution service test. The service test evaluates, among other things, the geographic distribution of an institution's branches and its record of opening and closing branches, as well as its record of providing community development services—that is, financial services targeted to lower-income people. Under the proposal, the branching of intermediate small institutions would no longer be evaluated although, under the proposed community development test, the community development services of such institutions would be.

17. For convenience, our research ignored the changes that the OTS made to its regulations and assumed that the OTS regulations are the 1995 regulations.

18. We used 2003 as a test year because at press time it was the latest year for which public data on retail lending activities related to the CRA were available.

19. Fourteen of the 241 institutions were not part of a multibank holding company. They had exceeded the asset-size threshold for the large-institution examination as of the beginning of 2003, but their assets had fallen below $250 million as of the end of the year. Under the 1995 regulations, these institutions had reverted to the small-institution examination as of the beginning of 2004.

20. Nearly 380 of the status-changing institutions, although covered by the large-institution examination as of December 31, 2003, had last been evaluated under the CRA as small banking institutions (data shown under the "small-institution" subcategory); consequently, they had not yet been evaluated as "large."

21. In classifying rural counties, the U.S. Department of Agriculture makes the distinction between exurban and remote, among others.

1. Banking institutions covered by the CRA, grouped by selected characteristics and distributed by asset size, as of December 31, 2003

Number except as noted

Characteristic	Type of institution, by asset size (millions of dollars)							Total		MEMO: Share of deposits (percent)
	Large institution[1]				Small institution[1]					
	Less than 250[2]	250–1,000	More than 1,000		Less than 150	150–250	More than 250[4]			
			Recent[3]	Nonrecent				Number	Percent	
Location (headquarters)										
Urban (metropolitan area)										
Center city	71	463	53	316	766	294	121	2,084	22.9	74.7
Suburban	81	456	47	101	1,633	415	153	2,886	31.7	15.0
Rural[5]										
Exurban	61	199	10	23	1,649	273	67	2,282	25.1	5.8
Remote	28	144	5	8	1,417	182	41	1,825	20.1	3.7
U.S.-affiliated area[6]	0	2	1	9	6	0	0	18	.2	.8
Rating on most recent CRA exam										
Outstanding	34	164	26	168	573	165	50	1,180	13.0	54.3
Satisfactory	185	1,050	84	282	4,405	918	293	7,217	79.4	42.9
Needs to improve	0	7	1	0	27	0	1	36	.4	.1
Substantial noncompliance	0	0	0	1	3	0	0	4	.0	.0
None (no exam in 5 years)	22	43	5	6	463	81	38	658	7.2	2.7
Type of most recent CRA exam										
Large-institution	129	909	95	412	6	2	2	1,555	17.1	80.2
Small-institution	79	291	9	3	4,973	1,075	339	6,769	74.4	12.8
Other[7]	11	21	7	36	29	6	3	113	1.2	4.3
None (no exam in 5 years)	22	43	5	6	463	81	38	658	7.2	2.7
Current regulator[8]										
Board	20	162	14	62	497	124	46	925	10.2	17.4
FDIC	136	639	57	163	3,413	627	222	5,257	57.8	24.4
OCC	70	298	22	145	1,100	280	77	1,992	21.9	44.1
OTS	15	165	23	87	461	133	37	921	10.1	14.2
All										
Number	241	1,264	116	457	5,471	1,164	382	9,095	100	100
Percent	2.7	13.9	1.3	5.0	60.1	12.8	4.2	. . .	100	100
MEMO										
Median number of days between exams	1,703	963	927	1,035	1,734	1,734	1,657	1,645	. . .	. . .
Share of deposits (percent)	.5	9.6	2.9	75.6	6.0	3.6	1.9	. . .	100	100

NOTE. Here and in subsequent tables, "CRA" means Community Reinvestment Act, and components may not sum to totals because of rounding.

1. Large institutions are banking institutions that reported 2003 data on small-business, small-farm, or community development lending as required of large institutions under the CRA. All other institutions are small institutions.

2. These institutions are generally part of multibank holding companies with assets of more than $1 billion and are currently covered by the large-institution CRA exam.

3. "Recent" institutions are banking institutions that had more than $1 billion in assets as of December 31, 2003, but not in the two consecutive years before 2003. If the asset-size threshold had been raised to $1 billion as of year-end 2003, these institutions would not yet have qualified for the large-institution CRA exam.

4. These institutions had more than $250 million in assets as of December 31, 2003, but failed to qualify for the large-institution CRA exam because they had not held this amount of assets for two consecutive years.

5. Exurban areas are counties adjacent to metropolitan areas; remote areas are counties not adjacent to metropolitan areas.

6. In this article, U.S.-affiliated areas consist of American Samoa, Guam, the Commonwealth of the Northern Mariana Islands, Puerto Rico, and the U.S. Virgin Islands.

7. "Other" exams cover strategic-plan, wholesale, and limited-purpose institutions. A strategic-plan institution develops its own plan, subject to the approval of a supervising agency, for evaluating its CRA performance. A wholesale institution does not extend home mortgage, small-business, small-farm, or consumer loans to retail customers; a limited-purpose institution offers a narrow product line, such as one composed of credit card or motor vehicle loans, to a regional or broader market. Exams for wholesale and limited-purpose institutions are limited to community development activities.

8. Current regulators are the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS).

. . . Not applicable.

SOURCES. Here and in subsequent tables, except as noted, analyses incorporate data from one or more of the following sources: unemployment, Bureau of Labor Statistics (2002); assets and business loans (as of June 30, 2003; data adjusted through December 31, 2003, to reflect changes in banking institution structure), Consolidated Reports of Condition and Income (Call Report), Federal Deposit Insurance Corporation (2003); branches and deposits (as of June 30, 2003; data adjusted through December 31, 2003, to reflect changes in banking institution structure), Summary of Deposits, Federal Deposit Insurance Corporation (2003); filings under the Home Mortgage Disclosure Act and the Community Reinvestment Act, Federal Financial Institutions Examination Council (2003); metropolitan statistical areas, Office of Management and Budget (2004); census tracts, U.S. Census Bureau (2000); net migration, Estimated Components of Population Change, Population Estimates program, U.S. Census Bureau (2000); poverty, Small Area Income and Poverty Estimates program, U.S. Census Bureau (2002); rural area designations, Urban Influence Codes, Economic Research Service, U.S. Department of Agriculture (2003).

is no universally accepted geographic definition of local banking markets, but the Federal Reserve Banks have constructed a list of local banking market definitions for reviews of the competitive effects of proposed mergers and acquisitions, and we used these definitions in our analysis.[22] Not all parts of the country have been defined for this purpose; however,

22. Local banking markets are not necessarily equivalent to CRA assessment areas. Unlike CRA assessment areas, local banking markets are not drawn from the perspective of a particular institution.

the 1,873 defined markets account for 96.7 percent of the branches and 97.7 percent of the deposits held by banking institutions nationwide (table 2). Seventy percent of banking markets are rural, but such markets account for a relatively small proportion of banking deposits nationwide (about one-eighth—data omitted from table) because most people and businesses are located in metropolitan areas.

For the market analysis, we focused on markets in which status-changing institutions play a significant role. We used two methods to characterize the roles of status-changing institutions in their markets: the percentage of a market's deposits held by status-changing institutions and the determination of whether a status-changing institution is the largest institution in the market.

The first method, the "market-share method," classifies markets by the percentage of each market's deposits held by status-changing institutions. This method assumes that an institution's propensity to invest in its market is directly related to its share of the market's deposits. (Here, we use the word "invest" in its broadest sense to include extensions of credit, services, grants, and equity investments.) The method further assumes that all institutions that shift from a large-institution examination to a small-institution examination experience the same proportional change in their propensity to invest in the market. These assumptions imply that the markets with the greatest presence (as measured by share of market deposits) of status-changing institutions will experience the largest proportional changes in banking institutions' lending and investing in the market.

2. Bank branches and deposits, grouped by location and distributed by market status of location, as of December 31, 2003

Item	Urban	Rural		U.S.-affiliated area	Total
		Exurban	Remote		
Branches					
Number					
In defined markets	66,815	10,234	7,806	0	84,855
Not in defined markets	612	1,034	606	641	2,893
Total	67,427	11,268	8,412	641	87,748
Percent					
In defined markets	99.1	90.8	92.8	0	96.7
Not in defined markets	.9	9.2	7.2	100	3.3
Total	100	100	100	100	100
Share of deposits (percent)					
In defined markets	99.4	91.8	92.7	0	97.7
Not in defined markets	.6	8.2	7.3	100	2.3
Total	100	100	100	100	100
Memo					
Number of defined markets	563	693	617	0	1,873
Share of deposits in defined markets (percent)	88.7	6.9	4.4	0	100
Share of deposits not in defined markets (percent)	21.1	26.3	14.9	37.7	100
Average number of banking institution headquarters per defined market	19.1	7.0	6.3	0	10.4

Note. In this article, markets are those defined as local banking markets by the Federal Reserve Banks; these defined areas do not cover all parts of the country. For markets that span more than one type of area, location is determined by the area with the largest percentage of market deposits. For definitions of "exurban" and "remote," see table 1, note 5. For definition of "U.S.-affiliated area," see table 1, note 6.

3. Banking markets grouped by location and distributed by share of market deposits held by institutions that would shift from large-institution to small-institution CRA examinations under the agencies' 2005 proposal, as of December 31, 2003

Percent except as noted

Location of market[1]	Share of market deposits affected (percent)					Total
	0	1–10	11–20	21–50	51–100	
Urban						
Number	88	145	123	173	34	563
Percent	15.6	25.8	21.9	30.7	6.0	100
Percent weighted by market deposits	.7	60.8	26.3	11.1	1.1	100
Rural						
Exurban						
Number	215	100	95	196	87	693
Percent	31.0	14.4	13.7	28.3	12.6	100
Percent weighted by market deposits	16.9	28.9	14.1	28.5	11.5	100
Remote						
Number	218	61	88	185	65	617
Percent	35.3	9.9	14.3	30.0	10.5	100
Percent weighted by market deposits	17.7	15.7	17.3	39.6	9.8	100
All						
Number	521	306	306	554	186	1,873
Percent	27.8	16.3	16.3	29.6	9.9	100
Percent weighted by market deposits	2.6	56.6	25.0	13.6	2.2	100

Note. See note to table 2.

1. The weighting factor for the weighted percentages is the amount of deposits in the market location as a share of total deposits.

The second method of market analysis, the "largest-institution method," classifies markets by the size of the largest institution with a presence (office) in the market regardless of the market share of that institution. This method assumes that if raising the threshold has an effect, the effect is particularly large in those markets that go from having one or more institutions that are subject to the three-part large-institution examination to having no such institutions.

As noted earlier, the market-share method identifies the share of market deposits held by status-changing institutions (table 3). As of December 31, 2003, 28 percent of the nation's 1,873 banking markets (with 3 percent of nationwide deposits) had *no* status-changing institution located within the market (column 1). Under either the market-share or the largest-institution method, those markets would presumably be unaffected by raising the threshold to $1 billion. In another one-third of markets (with 82 percent of nationwide deposits), status-changing institutions held less than 20 percent of deposits and thus, under the market-share method, would likely not see major effects (columns 2 and 3). But in roughly 10 percent of markets (with 2 percent of nationwide deposits),

4. Banking markets, grouped by location and distributed by change in CRA reporting status of largest banking institution with an office in the market, as of December 31, 2003

Percent except as noted

Location of market	Remains small	Large changes to small	Remains large	Total
Urban				
Number	25	19	519	563
Percent	4.4	3.4	92.2	100
Percent weighted by market deposits	.1	.1	99.9	100
Rural				
Exurban				
Number	51	50	592	693
Percent	7.4	7.2	85.4	100
Percent weighted by market deposits	2.2	3.0	94.8	100
Remote				
Number	98	89	430	617
Percent	15.9	14.4	69.7	100
Percent weighted by market deposits	4.3	7.5	88.2	100
All				
Number	174	158	1,541	1,873
Percent	9.3	8.4	82.3	100
Percent weighted by market deposits	.4	.6	99.0	100

NOTE. See notes to table 3.

5. Characteristics of counties in markets considered potentially most affected by an increase in the large-institution threshold to $1 billion, by method of market analysis

Percent except as noted

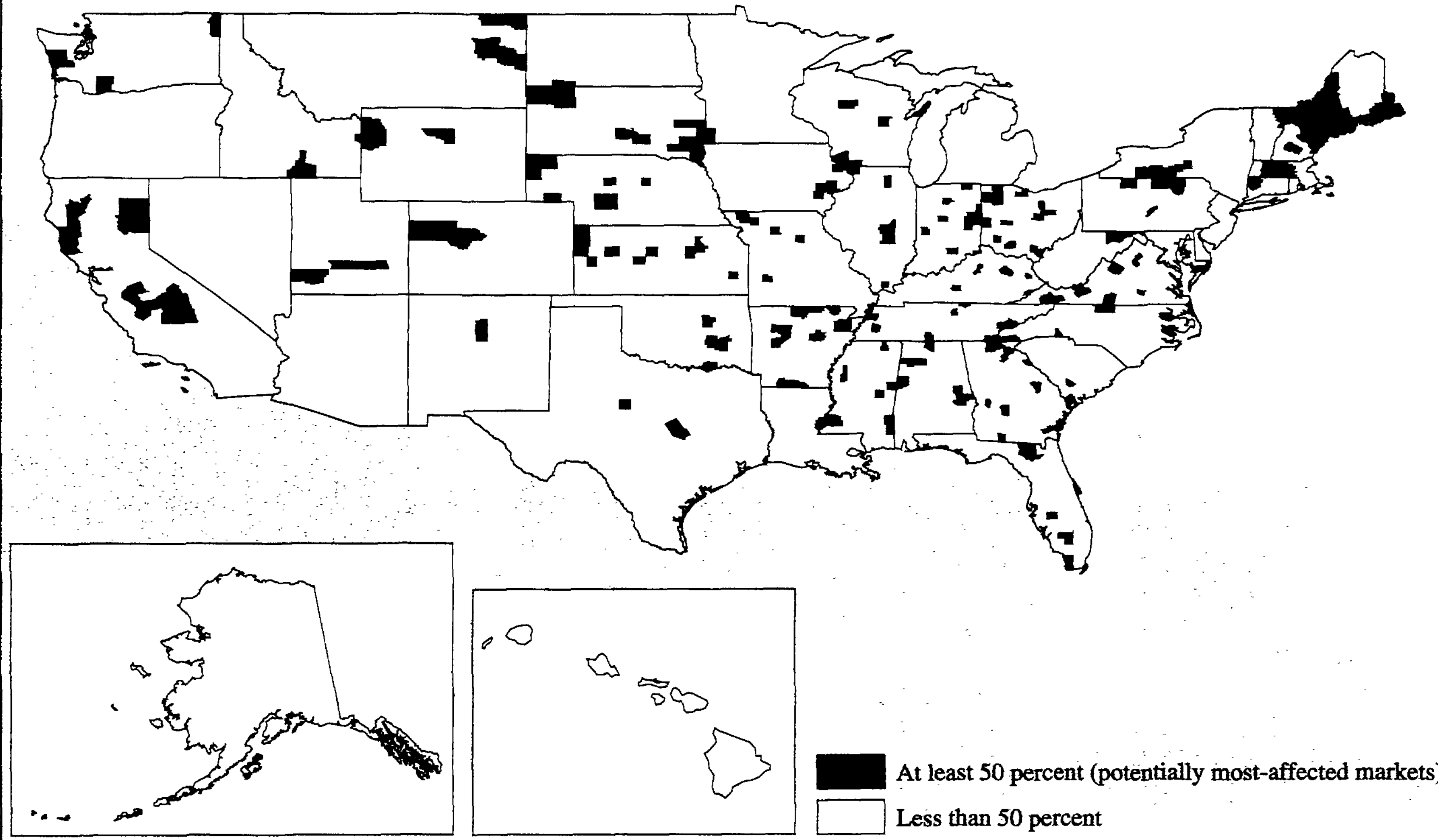
Characteristic	Method of market analysis and location of market[1]				National average for rural counties
	Market-share		Largest-institution		
	Urban	Rural	Urban	Rural	
Demographic					
Poverty rate, 2002	12.6	14.0	12.5	16.0	15.0
Income per capita, 2001 (dollars)	24,304	25,481	21,827	21,040	21,908
Real income growth rate					
1996–2001	6.8	7.0	6.2	5.7	1.7
1981–2001	33.3	33.0	30.0	26.9	28.1
Unemployment rate, 2001	5.2	5.4	5.4	5.4	5.7
Population growth rate					
1996–2001	5.8	2.8	4.6	–.1	1.7
1981–2001	22.6	22.5	13.5	.1	10.5
Net migration rate, 1995–99[2]	2.4	1.6	4.5	.7	1.2
Banking					
Branches per 10,000 persons					
Number, 2003	4.0	5.0	4.6	6.2	5.4
Change, 1998–2003	–.3	–.2	–.3	.0	–.1
Deposits					
Per capita (thousands of dollars), 2003	12.8	14.5	10.9	15.2	14.0
Change, 1998–2003	–.1	–.2	–.1	.0	–.1
MEMO: Counties (data as of 2000)					
Number	56	199	14	160	2,051[3]
Percent with no lower-income tracts	21.4	48.2	50.0	55.0	48.2[3]
Percent with only lower-income tracts	.0	3.0	7.1	7.5	5.5[3]

1. For markets that span more than one type of area, location is determined by the area with the largest percentage of market deposits. Hence, rural counties may be located in urban markets. When market boundaries do not correspond to county boundaries, the county is assigned to the market with the largest share of deposits. Under the market-share method, potentially most-affected markets are markets in which status-changing institutions (those with assets between $250 million and $1 billion) held more than 50 percent of market deposits. Under the large-institution method, potentially most-affected markets are markets in which the largest institution with an office in the market was a status-changing institution (one with assets between $250 million and $1 billion).

2. Net migration rate is calculated as the difference in migration between 1999 and 1995 relative to the estimated population in 1997.

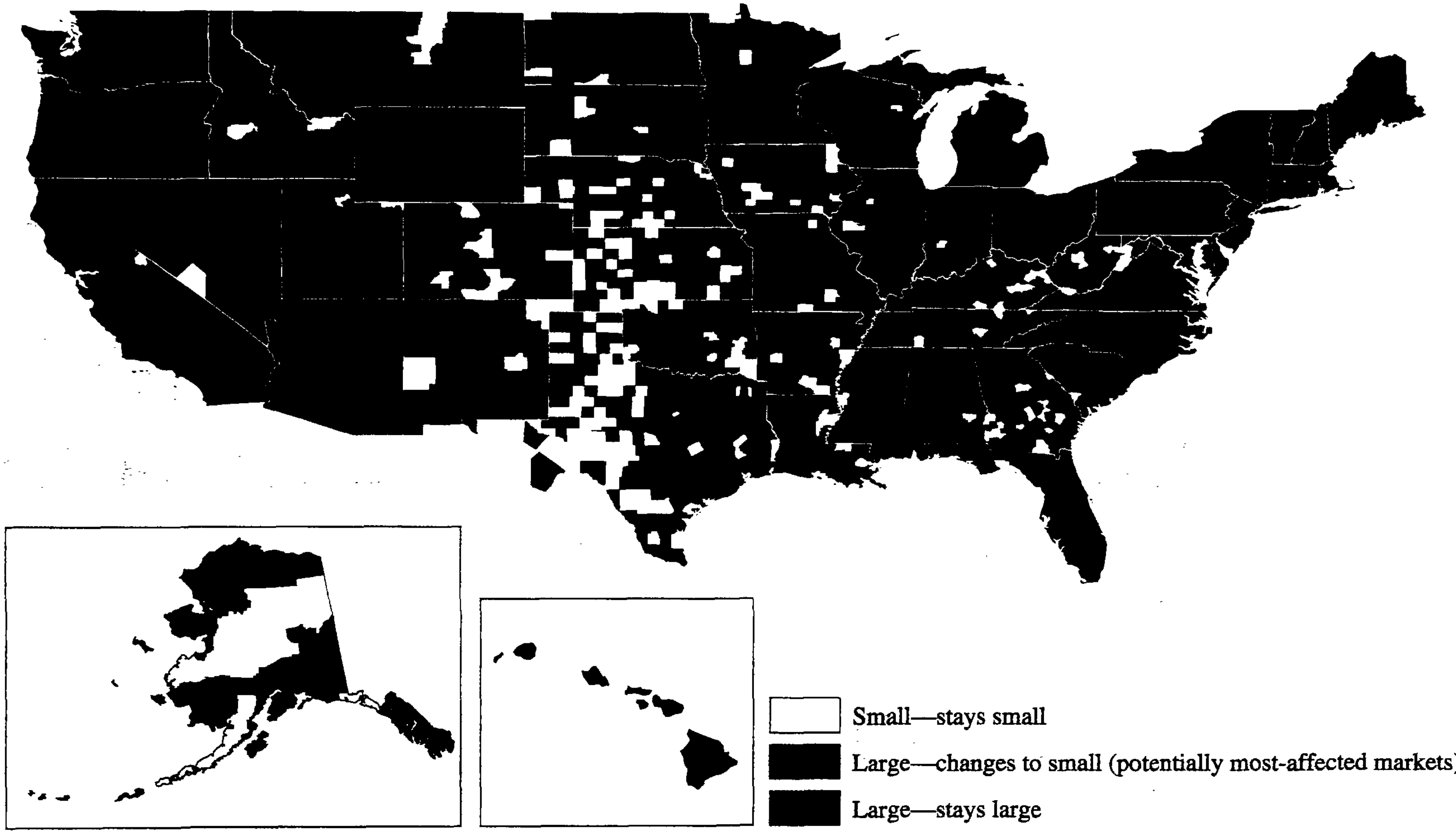
3. U.S. total.

1. Banking markets analyzed by the market-share method: Share of deposits held by status-changing institutions, as of December 31, 2003



NOTE. See table 5, note 1.

2. Banking markets analyzed by the largest-institution method: Current status of largest institution and the effect on reporting status of raising the asset-size threshold, as of December 31, 2003



NOTE. See table 5, note 1.

status-changing institutions held more than 50 percent of market deposits and, consequently, those markets have the potential to be most affected (column 5).

The largest-institution method yields a different group of potentially most affected markets (table 4). The largest institution was a status-changing institution in about 8 percent of all markets (with less than 1 percent of nationwide deposits) (column 2).

Although there is little overlap between the groups of potentially most affected markets defined by the two methods, the groups have several characteristics in common (table 5). In both groups, the markets are overwhelmingly rural, are served by few banking institutions (data omitted from table), have unemployment rates near the national rural average, and have bank branches per capita similar to the national rural average. Yet the groups of markets differ in key respects. Whereas population growth is much higher than the national rural average in the potentially most affected markets identified by the market-share method, it is notably lower than the national rural average in such markets identified by the largest-institution method. Moreover, under the market-share method, the potentially most affected markets are scattered throughout the country (figure 1), but under the largest-institution method, such markets are concentrated substantially in the Great Plains region, with much smaller concentrations in Iowa, Louisiana, Kentucky–Tennessee, and southern Georgia–northern Florida (figure 2).[23]

Results of Threshold Tests

The 2005 proposal would subject intermediate small banking institutions to the streamlined lending test currently applied to smaller institutions and would eliminate the service (branching) test for intermediate small institutions. Testing directly to determine how those changes would affect activities of intermediate small institutions is impossible. However, an inference might be drawn from the effect of the current $250 million threshold on the retail lending and branching activities of institutions with assets near this threshold. Of particular interest are the retail lending activities covered by both the large-institution and the streamlined lending tests. Our tests compare the retail lending and branching of institutions just above and just below the current large-institution threshold of $250 million (table 6). Institutions "just below" the threshold are defined here as those that had between $150 million and $250 million in assets as of December 31, 2003, and were deemed small as of that date and for the purposes of their most recent CRA performance evaluation (group 1); institutions "just above" the threshold are defined as those that had between $250 million and $350 million in assets and were deemed large as of that date and for the purposes of their most recent examination (group 2).

Banking institutions in these two groups were restricted to institutions that were independent of multibank holding companies, that had a CRA examination completed between January 1, 1999, and June 30, 2004, and that received a "satisfactory" CRA performance rating on their most recent examination in that period. Institutions with "outstanding" ratings were excluded to control for the possibility that such institutions were influenced less by the nature of their CRA examinations and more by other factors, such as institution philosophy, than were institutions with "satisfactory" ratings. Institutions with less than "satisfactory" ratings were excluded for similar reasons. Institutions with headquarters in U.S.-affiliated areas were also excluded.

The threshold test relies on sources of data that provide the same types of information for institutions just above the threshold as for institutions just below. The information consists of five balance sheet ratios constructed from dollar values provided in Call Report data supplied to federal banking agencies.[24] The ratios compose two categories: loan dollars to deposits (overall; consumer; and business, including small commercial and industrial [C&I], small commercial real estate [CRE], and small farm) and mortgage dollars to deposits (one- to four-family and multifamily).

In addition, five measures of retail lending to lower-income populations were constructed from filings pursuant to HMDA: the percentage of an institution's home-purchase and home-improvement loans extended to lower-income borrowers or census tracts and a comparable calculation for loans extended for multifamily housing in lower-income census tracts. Each of the HMDA-based measures was expressed as the difference between the percentage of the institution's retail loans made to lower-income borrowers (or borrowers that live in lower-income tracts) and the percentage of the families that live in the areas

23. The figures use counties, which approximate, rather than precisely match, banking markets.

24. "Call Report" is the informal name for the Report of Condition and Income, which commercial banking institutions must file each quarter with federal and state banking agencies. It is essentially equivalent to the Thrift Financial Report, which savings institutions must file each quarter with the Office of Thrift Supervision.

6. Lending and branching activities of banking institutions with asset sizes close to the current large-institution threshold for CRA exams, as of December 31, 2003

Percent except as noted

Item	Asset size (millions of dollars)				Memo: Crossed threshold after end of 2001[1]	
	150–250 (Group 1)	250–350 (Group 2)	350–450 (Group 3)	Less than 250[2] (Group 4)	2001	2003
Ratio of loan dollars to deposits, by type of loan						
All	78.6[a,B]	83.7[c]	78.5	88.5	85.3	85.4
Consumer	5.6[a,B]	7.0[c]	5.0	8.6	6.4[d]	5.1
Business[3]						
Commercial and industrial						
Overall	11.2	9.9	10.3	12.3	11.4	10.7
Small	9.3[a]	7.5	7.5	9.7	9.3	8.0
Commercial real estate						
Overall	19.0	20.9	19.8	20.4	17.9[d]	20.9
Small	13.9	13.1	11.8	13.2	12.8	13.5
Farm[4]						
Overall	5.5[a]	3.3	3.8	6.0	6.9	6.4
Small	6.6[a]	4.1	5.9	5.6	8.4	7.3
Ratio of mortgage dollars to deposits, by type of mortgage						
1–4 family	27.0[a,b]	29.9	27.6	31.8	33.0	29.9
Multifamily	2.2	2.6	2.5	2.2	4.0	4.7
Loans to lower-income borrowers (percentage points)[5]						
Home-purchase	−3.7	−3.3	−3.2	−4.5	...	...
Home-improvement	10.0	10.8	7.6	4.6	...	...
Loans in lower-income areas[5]						
Home-purchase	−7.8	−10.6	−4.8	−14.2	...	...
Home-improvement	−4.5	−7.5	−6.9	−.7	...	...
Multifamily	1.6	7.3	8.1	−.6	...	...
Branching activity[6]						
Branches per $100 million of deposits (number)	2.9	2.7	2.7	3.0	3.1	2.9
Branches in lower-income areas (percentage points)	−1.7	1.0	−3.5	−1.8	...	...
5-year change in such branches	.0	−1.0	−2.0	−1.5	...	...
Number of institutions	646	72	142	49	100	100

NOTE. Data are group means adjusted for state, institution (savings association or commercial bank), location (center city, suburban, exurban, or remote), and charter effects. Analysis is restricted to institutions that were examined in the past five years, that were in existence for at least one year, and that received a "satisfactory" rating on the small- or large-institution exam. Data exclude institutions with headquarters in U.S.-affiliated areas and strategic-plan, wholesale, and limited-purpose institutions (see table 1, note 7).

1. Data are for the 100 banking institutions that were subject to the small-institution evaluation in 2001 but were subject to the large-institution evaluation in 2002 and 2003. Differences are omitted for retail loans extended to lower-income borrowers, retail loans extended in lower-income areas, and some categories of branching activity because the lower-income classifications of 2001 were based on the 1990 census, whereas those of 2003 were based on the 2000 census.

2. These institutions are part of multibank holding companies with assets of more than $1 billion and are currently covered by the large-institution CRA exam.

3. Business loan ratios are calculated as of June 30, 2001, or June 30, 2003, for comparability with small-loan data. Data have been adjusted through December 2001 or December 2003 to reflect changes in banking institution structure.

4. Farm lending is measured only for rural commercial banks. Small farm contains some loans not in overall farm.

5. Data cover only urban tracts and institutions that report data under the Home Mortgage Disclosure Act. Data are the difference between the average percentage of lending to borrowers in lower-income census tracts and the average percentage of families that live in lower-income census tracts in the areas that the institutions serve.

6. Branch data are measured as of June 30, 1998; June 30, 2001; or June 30, 2003. Data have been adjusted through December 1998, December 2001, or December 2003 to reflect changes in banking institution structure. Data on lower-income areas are the difference between the percentage of branches in lower-income census tracts and the percentage of families that live in lower-income census tracts in the areas that the institutions serve.

a. Difference between group 1 and group 2 is statistically significant at the 10 percent level.

b. Difference between group 1 and group 4 is statistically significant at the 10 percent level.

B. Difference between group 1 and group 4 is statistically significant at the 1 percent level.

c. Difference between group 2 and group 3 is statistically significant at the 10 percent level.

d. Difference between ratio in 2001 and that in 2003 is statistically significant at the 10 percent level.

... Not applicable.

served by the institution who have lower incomes (or live in lower-income tracts). Because of limitations on reporting requirements for rural institutions under HMDA, the comparisons that use the HMDA-based lower-income lending measures were restricted to retail lending activities in urban areas.

We present means of these metrics for the groups above and below the threshold, adjusted to remove effects related to state, institution type (savings association or commercial bank), and headquarters location (center city, suburban, exurban, remote) as rough controls for economic and demographic factors.[25] The results are of three types. First, overall C&I lending, CRE lending (overall or small), multifamily housing, and the HMDA data measures show no statistically significant differences. Second, the

25. Every institution in the analysis had at least one comparable institution on the other side of the threshold in the same state, of the same institution type, and in the same area type.

other business loan categories do show differences that are statistically significant; however, the direction of the differences is the opposite of what would have been expected had the differences been caused by tougher evaluation criteria in the large-institution evaluation.

Third, statistically significant differences exist in the groups' ratios of overall loan dollars to deposits, consumer loan dollars to deposits, and one- to four-family mortgage dollars to deposits, and these differences go in the direction that might suggest a threshold effect. To confirm that this result reflects differences in CRA evaluation criteria and not merely in asset size, we conducted an additional comparison test. We constructed a third group of banking institutions that had between $350 million and $450 million in assets and that otherwise met the same requirements as the institutions in group 2 (group 3). A comparison of adjusted means for group 3 with those for group 2 isolates the effects of size differences because banking institutions in both groups are subject to the same type of CRA evaluation. Institutions in group 3 have *lower* ratios of overall loan dollars to deposits, consumer loan dollars to deposits, and one- to four-family mortgage dollars to deposits than have institutions in group 2 (and, in two out of three cases, lower than those of group 1 institutions), an indication that the difference between groups 1 and 2 may be caused by a factor other than the difference in CRA examination types.

We also compared adjusted means for groups 1 and 2 (and for groups 2 and 3) on three measures of branching activity: (1) the number of branches per $100 million of deposits, (2) the difference between the percentage of branches in lower-income census tracts and the percentage of the population that lives in lower-income census tracts in the areas that the institutions serve, and (3) the five-year change in the percentage of branches in lower-income areas. None of the three measures shows a significant difference among any of the groups.

As a further test for the effects of differences in CRA evaluation types, we compared independent institutions that had between $150 million and $250 million in assets (group 1) with similarly sized institutions that were subject to the large-institution evaluation criteria because of their affiliation with holding companies with assets of $1 billion or more (group 4). The ratios of overall loan dollars to deposits, consumer loan dollars to deposits, and one- to four-family mortgage dollars to deposits are the only measures with a statistically significant difference: Group 4 has higher ratios than does group 1. One should interpret these results cautiously, as they may mean only that banking institutions in holding companies are more likely than independent banking institutions to raise funds through wholesale, nondeposit markets and to be institutions focused on retail lending.

A final test for the effects of differences in CRA evaluation types examined whether banking institutions that passed the $250 million threshold measurably changed their retail lending and branching activities. Specifically, one hundred institutions covered by the large-institution CRA evaluation (though not necessarily yet evaluated as large institutions) at the end of 2002 and at the end of 2003 had been subject to the small-institution evaluation in 2001. This test, unlike the other tests, looked for any change *in an individual institution's* behavior induced by a change in evaluation type. We restricted the comparison to institutions covered by the large-institution examination for both 2002 and 2003 to ensure that ample time had elapsed for behavioral changes to result in measurable changes in balance sheet variables. We found only two statistically significant changes in retail lending or branching behavior as an institution passed through the $250 million threshold (compare columns 5 and 6), but the changes were in opposite directions: Consumer lending fell, and overall CRE lending rose.[26]

Taken together, the threshold tests provide little evidence that the nature of the CRA examination influences the retail lending and branching activities of banking institutions in the size range near the $250 million threshold. However, the threshold tests have an important limitation. The tests are limited to inferences about the behavior of institutions around the margin of the current threshold, $250 million. They suggest that raising the threshold some amount above $250 million would not have a significant effect on retail lending or branching. However, they fail to reveal what amount of increase in the threshold, if any, would result in a significant effect.

The Role of Community Development Lending

The 1995 regulations require that, for a large institution, community development lending be evaluated as only one component of the CRA lending test, which includes a wide range of other, retail types of

26. We refrained from conducting the comparison for any of the measures that use lower-income classifications because 2001 classifications were based on the 1990 census and 2003 classifications were based on the 2000 census. The change in classifications makes a comparison of lower-income activity in 2001 with lower-income activity in 2003 problematic.

lending (see box "The Large-Institution Evaluation"). Under the 2005 proposal, intermediate small institutions would be subject to a new community development test. Instead of considering community development loans, investments, and services in three separate tests, the proposal is for the three types of activity to be considered in a single test. The proposal responds in part to the argument that community development lending is more like community development investments—both are primarily for the benefit of lower-income people or areas—than like retail lending. It also responds to the argument that evaluating community development investments separately from retail lending places too much emphasis on investment vehicles, especially for smaller institutions that have limited experience with and opportunities for investments and substantially more experience with and opportunities for retail lending.

We could not test for the effects of adopting a community development test on community development loans, investments, or services. We could, however, consider whether the number or dollar amount of community development loans have played a significant role in CRA ratings. Our sample was restricted to institutions examined under the large-institution examination between January 1, 2001, and December 31, 2003. We looked at the institutions' community development lending records over the same period (table 7). The data suggest that an institution's community development lending record is largely unrelated to its overall CRA rating. The lack of relationship is most apparent among institutions with assets of more than $5 billion: Nearly one-half of the institutions with "outstanding" ratings had community development lending activity in the bottom half of their asset-size group. Among intermediate small institutions, those with "outstanding" ratings were a little more likely than their counterparts with "satisfactory" ratings to do community development lending. However, fully one-fourth of the institutions rated "outstanding" in this category did no community development lending, and about 40 percent had community development lending activity in the bottom half of their asset-size group.

Although the data provide no information about how community development lending should be treated in CRA evaluations, they do suggest that such lending is not currently critical in overall CRA ratings. The likely explanation is that, because examiners consider community development loans as part of a comprehensive lending test, other types of lending may have compensated for an institution's lack of community development loans. Another possibility is that, despite the mandate of the regulations to treat community development loans and community development investments separately, examiners implicitly treat them as substitutes.[27]

7. Rating on most recent CRA exam and community development lending during 2001–03 at large institutions, by rating and asset size of institution, as of December 31, 2003

Percent except as noted

Number of institutions and status of community development lending, by CRA rating	Asset size of institution (millions of dollars)			
	250–500	500–1,000	1,000–5,000	More than 5,000
Outstanding				
Number of institutions	23	50	92	65
Made no loans	26.1	22.0	8.7	6.2
Ranked in bottom half of asset-size class	39.1	44.0	38.0	46.2
Satisfactory				
Number of institutions	241	316	254	69
Made no loans	29.9	19.0	11.0	5.8
Ranked in bottom half of asset-size class	51.0	51.0	54.3	53.6

NOTE. Analysis is restricted to institutions that were subject to the large-institution CRA exam each year from 2001 through 2003, that were in existence for at least one year, that received an "outstanding" or "satisfactory" rating on the exam, and that had assets of more than $250 million in 2003. Data exclude strategic-plan, wholesale, or limited-purpose institutions (see table 1, note 7) and institutions with headquarters in U.S.-affiliated areas.

COMMUNITY DEVELOPMENT AND RURAL AREAS

Another part of the agencies' 2005 proposal would expand the definition of "community development" in rural, though not urban, areas. This part of the proposal would cover banking institutions of all sizes, not just intermediate small institutions.

The Problem and the Agencies' Proposed Solution

The regulations' current definition of "community development" is identical for urban and rural areas. As noted earlier, the definition covers four categories of activity, three of which (affordable housing, com-

27. Some empirical support exists for the substitutability explanation. We examined the CRA performance evaluation reports (PEs) for the twenty-three institutions in our sample that had assets between $250 million and $500 million and that received "outstanding" CRA ratings (column 1, row 1, of table 7). There is a mild negative correlation (–.2) between the dollar volume of community development lending and the investments reported in the PEs. However, some evidence also suggests that the substitutability explanation applies only to smaller institutions. An examination of the dollar volume of community development lending and the investments reported in the PEs of the fifty institutions in our sample that had assets between $500 million and $1 billion and that received "outstanding" CRA ratings (column 2, row 1) shows a significant positive correlation of .5.

8. Distribution of census tracts, population, and families, by location of tract and tract income relative to wider area, as of December 31, 2003

Percent except as noted

Census tract location and percent of median family income in area[1]	Census tracts: Number	Census tracts: Percent	Population	Families	Memo: Families with incomes less than 80 percent of MSA or non-MSA median[2]
Urban					
Center city tracts					
Income relative to MSA					
Less than 50	3,437	13.1	10.0	8.7	78.2
50–79	8,004	30.5	29.7	27.7	60.5
80–90	2,622	10.0	10.4	10.3	45.8
90–100	2,503	9.5	10.0	10.2	39.4
100–119	3,898	14.8	16.3	17.4	31.6
120 or more	5,814	22.1	23.6	25.7	19.0
Total	26,278	100	100	100	42.7
Income relative to state					
Less than 80	10,938	41.6	37.8	34.8	64.8
80–99	4,851	18.5	19.2	19.3	42.9
100–119	3,900	14.8	15.9	16.7	31.8
120 or more	6,589	25.1	27.0	29.2	18.0
Total	26,278	100	100	100	41.4
Suburban tracts					
Income relative to MSA					
Less than 50	444	1.7	1.2	1.0	76.9
50–79	4,456	16.9	15.9	14.6	57.9
80–90	3,384	12.9	12.5	12.3	45.6
90–100	4,069	15.5	15.5	15.5	38.9
100–119	6,563	25.0	25.6	26.2	30.7
120 or more	7,382	28.1	29.2	30.4	18.5
Total	26,298	100	100	100	34.5
Income relative to state					
Less than 80	4,592	17.5	15.9	14.4	59.7
80–99	6,333	24.1	23.5	23.3	42.2
100–119	6,100	23.2	23.8	24.1	30.8
120 or more	9,273	35.3	36.8	38.2	17.6
Total	26,298	100	100	100	32.6
Rural					
Exurban tracts					
Income relative to non-MSA					
Less than 50	57	.7	.5	.4	72.9
50–79	912	11.9	10.5	9.8	55.1
80–90	1,157	15.1	14.4	14.1	45.8
90–100	1,780	23.2	22.7	22.8	39.8
100–119	2,720	35.5	36.9	37.4	32.6
120 or more	1,035	13.5	15.0	15.5	23.7
Total	7,661	100	100	100	37.1
Income relative to state					
Less than 80	3,051	39.8	37.5	36.3	57.4
80–99	3,394	44.3	45.0	45.7	43.4
100–119	1,006	13.1	14.5	14.9	33.0
120 or more	210	2.7	3.0	3.1	22.9
Total	7,661	100	100	100	46.3
Remote tracts					
Income relative to non-MSA					
Less than 50	39	.8	.6	.4	72.0
50–79	794	17.1	15.0	14.4	55.8
80–90	927	19.9	18.7	18.7	46.1
90–100	1,136	24.4	23.4	23.8	39.9
100–119	1,285	27.6	29.6	30.0	32.9
120 or more	469	10.1	12.7	12.8	23.3
Total	4,650	100	100	100	39.3
Income relative to state					
Less than 80	2,240	48.2	44.6	43.9	58.6
80–99	1,764	37.9	38.4	38.9	43.7
100–119	487	10.5	12.5	12.6	33.1
120 or more	159	3.4	4.6	4.5	23.5
Total	4,650	100	100	100	48.0

8.—Continued

Percent except as noted

Census tract location and percent of median family income in area[1]	Census tracts: Number	Census tracts: Percent	Population	Families	Memo: Families with incomes less than 80 percent of MSA or non-MSA median[2]
Total urban					
Income relative to MSA					
Less than 50	3,881	7.4	5.4	4.4	78.0
50–79	12,460	23.7	22.4	20.4	59.5
80–90	6,006	11.4	11.5	11.4	45.7
90–100	6,572	12.5	12.9	13.1	39.1
100–119	10,461	19.9	21.3	22.3	31.0
120 or more	13,196	25.1	26.6	28.3	18.7
Total	52,576	100	100	100	38.2
Income relative to state					
Less than 80	15,530	29.5	26.2	23.5	63.1
80–99	11,184	21.3	21.5	21.5	42.5
100–119	10,000	19.0	20.1	20.8	31.2
120 or more	15,862	30.2	32.2	34.2	17.7
Total	52,576	100	100	100	36.5
Total rural					
Income relative to non-MSA					
Less than 50	96	.8	.5	.4	72.6
50–79	1,706	13.9	12.1	11.4	55.4
80–90	2,084	16.9	15.9	15.7	45.9
90–100	2,916	23.7	22.9	23.1	39.8
100–119	4,005	32.5	34.4	34.9	32.7
120 or more	1,504	12.2	14.2	14.6	23.6
Total	12,311	100	100	100	37.9
Income relative to state					
Less than 80	5,291	43.0	40.0	39.0	57.9
80–99	5,158	41.9	42.7	43.3	43.5
100–119	1,493	12.1	13.8	14.1	33.1
120 or more	369	3.0	3.5	3.6	23.1
Total	12,311	100	100	100	46.9

NOTE. Data from the 2000 census are reported for census tracts and metropolitan statistical areas as determined by 2004 definitions. Data exclude census tracts in U.S.-affiliated areas.

1. Income standard is the median family income in the metropolitan statistical area (MSA), nonmetropolitan portion of the state (non-MSA), or state in which the census tract is located.

2. For calculations in this column, even when tracts are classified by state standards, families are still classified by the income in the MSA or non-MSA in which the family is located.

munity services, and economic development) are defined in terms of the activity's targeting of certain *recipients* (lower-income people, small businesses, or small farms) and the fourth of which (revitalization and stabilization) is defined in terms of the activity's targeting of certain *areas*—namely, lower-income census tracts.

Some have said that the lower-income-area limitation in the fourth category, revitalization and stabilization, may unduly constrain the effectiveness of the regulations in promoting community development activities in rural areas. In response to such concerns, the agencies proposed to expand the definition of "community development" to include revitalizing or stabilizing activities in underserved rural areas. No such change was proposed for urban areas.

The problem that the agencies sought to address stems in part from the way rural census tracts are classified. As applied to rural areas, the 1995 regulations' system for classifying census-tract income has two defining characteristics. The first characteristic is that the system ignores the fact that rural areas are generally poorer than urban areas. Forty-three percent of rural census tracts in the United States (containing 40 percent of the rural population) have a median family income below 80 percent of the median family income of the state in which the tracts are located; in contrast, 30 percent of urban census tracts (containing 26 percent of the urban population) have a median family income below 80 percent of the statewide median (table 8, "Total rural" and "Total urban" categories). But the 1995 regulations classify rural census tracts relative only to a state's rural median income, not relative to the median income of the entire state, including its urban areas. Thus, the current rule classifies only 15 percent of rural tracts, not 43 percent, as lower income. In contrast, despite the higher absolute incomes of urban areas, double the proportion of urban tracts (31 percent), which are classified relative to the relevant metropolitan area income, are currently classified as lower income.

The second characteristic is that the census tract identifies pockets of lower-income populations less effectively in rural areas than in urban areas. Compared with urban census tracts, rural tracts are drawn over relatively large geographic areas, have lower population densities, and often have relatively heterogeneous populations that, when averaged, tend toward the middle (table 9). Indeed, 73 percent of all rural tracts are defined as middle income; in contrast, 44 percent of urban tracts are defined as such (percentages derived from table 8).

The large size of rural census tracts and the relative heterogeneity within them have another consequence: uneven distribution of lower-income tracts among areas that define banking institutions' markets, such as counties and assessment areas. Most rural counties (almost 60 percent) have *no* tracts that are classified as lower income under the current definition; in contrast, only 18 percent of urban counties are without any such tracts (table 9). About 44 percent of the rural assessment areas that large institutions reported under the CRA regulation in 2003 lacked any tracts classified as lower income, whereas only 14 percent of the urban assessment areas that these institutions reported lacked any such tracts. Small institutions do not report their assessment areas, though the areas are described in their performance evaluations. A rough approximation of a small institution's assessment areas—one that uses the counties in which its branches are located—suggests that 54 percent of small institutions also lack any lower-income tracts in rural areas.

The relative lack of lower-income tracts in rural areas could have different consequences. Banking institutions might invest less, or less efficiently, in

9. Characteristics of census tracts and the share of selected areas and of banking institutions without lower-income tracts, by location of tract, as of December 31, 2003

Percent except as noted

Item	Urban		Rural		Total		
	Center city	Suburban	Exurban	Remote	Urban	Rural	All
Characteristic of census tract							
Number of tracts	26,278	26,298	7,661	4,650	52,576	12,311	64,887
Average land area per tract (square miles)	5.5	28.5	147.8	322.7	17.0	213.9	54.3
Average population density per tract (population per square mile)	9,812.3	3,097.3	494.5	423.4	6,454.4	467.7	5,318.4
Average population per tract	4,145.3	4,693.8	4,163.7	3,639.6	4,419.6	3,965.7	4,333.4
Percent of national population	38.7	43.9	11.3	6.0	82.6	17.4	100.0
Share without lower-income census tracts							
Area							
County	12.0	31.9	56.9	61.3	18.0	59.0	44.8
Individual assessment area of large institution[1]	6.2	26.5	45.1	45.7	13.8	43.8	23.4
Aggregate assessment area							
Large institution	5.8	14.3	36.0	32.7	5.4	30.2	13.9
Small institution[2]	...	...	55.0	56.9	7.9	53.9	28.3

NOTE. Data exclude U.S.-affiliated areas and tracts without income information.

1. An assessment area consists of the area in which a banking institution has its main office, branches, and deposit-taking automated teller machines, as well as the surrounding areas in which the institution has originated or purchased a substantial portion of its loans. Assessment areas reported in the 2003 geographies, which were determined from information supplied by the U.S. Census Bureau, the U.S. Department of Agriculture, and the Office of Management and Budget, have been mapped onto the 2004 tract definitions, which use the Office of Management and Budget's 2004 designations of metropolitan statistical areas. Large institutions report their assessment areas each year and may have multiple assessment areas corresponding to cities or states.

2. Aggregate assessment areas were approximated by the counties in which small institutions had branches.

... Not applicable.

community-improving activities in rural areas than they might under a standard more appropriate for rural community development. Or they might shift more of their community-improving loans or investments to urban areas than they might under a standard that would give more equal area-based CRA consideration in urban and rural areas. A third possibility is that, even if the first and second possibilities failed to occur, banking institutions might receive inadequate recognition of their community-improving activities in rural areas because the activities did not meet the exact requirements to qualify as community development.

Perhaps to address these possible consequences, the 2005 proposal would expand, in two ways, the criteria under which banking institutions receive CRA consideration for community-improving activities in rural areas. First, CRA consideration would be available for activities that revitalize or stabilize "underserved rural areas," in the words of the proposal, even if the areas lack lower-income tracts. Second, the proposal would extend CRA consideration to affordable housing for any individual in an underserved rural area. The 1995 regulations limit affordable housing consideration to housing for lower-income individuals; consideration does not depend on where the lower-income individuals reside. The proposal would leave unchanged the recognition of community development activities in urban areas and the non-community-development CRA measures.

In this section, we analyze several issues related to the agencies' proposal to expand the criteria for recognizing rural community-improving activities as community development. First, we test the proposal's premise that the 1995 regulations "disfavor" community-improving activities in rural areas relative to those in urban areas. Second, we explore the implications of various options to revise the regulations on which the agencies sought public comment.

Concern about Whether the 1995 Regulations "Disfavor" Rural Areas

Research on the question of whether the 1995 regulations disfavor rural areas is constrained by the difficulties in gathering comprehensive data on community-improving activities that fail to qualify for CRA consideration and by the lack of geographic data on community development loans, investments, and services. However, geographic data are available for all other CRA-related loan products and branches, such as loans to purchase or improve homes or to finance small businesses or small farms. We used these data to test whether large institutions whose assessment areas include both urban and rural areas ("urban–rural institutions") appear to favor urban areas over rural areas in retail lending and branching activities. We also tested whether large institutions with headquarters in rural areas ("rural institutions") were less likely than similarly situated institutions with headquarters in urban areas ("urban institutions") (1) to receive "outstanding" CRA ratings or (2) to engage in community development lending.

The first test was based on the distribution of urban–rural institutions' activities between urban and rural parts of their assessment areas. We restricted the analysis to institutions covered by the large-institution examination as of December 31, 2003, because such institutions are required to report the geographic location of most of their CRA-related loans, with the notable exception of community development loans. The test involved two distinct comparisons. First, the test compared the distribution of *numbers* of retail loans between urban and rural parts with the distributions of offices, populations (families), and housing structures (owner-occupied or multifamily) between the parts. This comparison tested whether urban–rural institutions extend retail loans in the same proportion to the offices, populations, and housing structures of those areas (table 10).[28] Second, the test compared, for various types of retail loan in those institutions' assessment areas, the distribution of loan *dollars* between urban and rural parts with the distribution of deposits between the parts. The comparison tested whether urban–rural institutions extend loan dollars in the same proportion that they receive deposits in rural and urban areas (table 11). We conducted both comparisons separately for banking institutions in four asset-size categories: $250 million to $500 million, $500 million to $1 billion, $1 billion to $5 billion, and more than $5 billion.

We found that remote areas receive more retail loans as measured against the distributions of offices, populations, and housing structures and more loan dollars as measured against the distribution of deposits than do urban areas in the aggregate for banking institutions of every size category and for retail loans of almost every type considered (tables 10 and 11). For example, urban–rural institutions with assets between $500 million and $1 billion received 13.6 percent of their deposits from branches in

28. We also conducted a similar analysis that restricted the comparisons to retail loans, retail loan dollars, offices, families, housing structures, and deposits in lower-income tracts. The results for this comparison are substantially the same as those for the comparison based on the full set of census tracts.

10. Number of retail loans, offices, families, and housing structures in the assessment areas of large banking institutions with both urban and rural branches, grouped by asset size of institution and distributed by location of assessment area, as of December 31, 2003

Percent

Asset size of institution and characteristic	Urban		Rural		Total	
	Center city	Suburban	Exurban	Remote	Urban	Rural
$250 million to $500 million						
Loans						
Home-purchase	22.3	30.6	27.7	19.5	52.9	47.1
Home-improvement	10.5	32.6	38.3	18.6	43.0	57.0
Small-business or small-farm	13.7	25.2	31.6	29.6	38.8	61.1
Multifamily	42.4	24.7	24.1	8.8	67.0	33.0
Offices[1]	20.9	28.2	35.8	15.1	49.2	50.9
Families	35.1	40.8	14.6	9.4	76.0	24.0
Housing structures						
Owner-occupied	32.2	42.4	15.5	9.8	74.7	25.3
Multifamily	59.4	29.6	5.8	5.2	89.0	11.0
$500 million to $1 billion						
Loans						
Home-purchase	25.7	31.1	22.2	21.1	56.8	43.2
Home-improvement	21.5	30.6	28.4	19.5	52.1	47.9
Small-business or small-farm	19.2	23.1	27.1	30.6	42.3	57.7
Multifamily	51.6	20.6	13.5	14.3	72.2	27.8
Offices[1]	24.2	31.6	29.4	14.8	55.8	44.2
Families	33.6	46.3	11.5	8.5	79.9	20.1
Housing structures						
Owner-occupied	30.9	47.5	12.6	9.1	78.3	21.7
Multifamily	54.2	38.0	3.9	3.8	92.7	7.3
$1 billion to $5 billion						
Loans						
Home-purchase	34.6	38.4	15.6	11.4	73.0	27.0
Home-improvement	23.7	36.6	23.4	16.3	60.3	39.7
Small-business or small-farm	31.4	28.2	20.0	20.4	59.5	40.5
Multifamily	55.9	24.5	9.4	10.2	80.3	19.7
Offices[1]	32.7	34.2	22.2	10.9	66.9	33.1
Families	39.0	48.7	7.4	4.9	87.7	12.3
Housing structures						
Owner-occupied	36.2	50.8	7.9	5.2	87.0	13.0
Multifamily	57.8	37.1	2.6	2.5	94.9	5.1
More than $5 billion						
Loans						
Home-purchase	36.7	53.7	4.7	4.8	90.4	9.6
Home-improvement	29.9	54.6	8.9	6.6	84.5	15.5
Small-business or small-farm	39.1	44.8	8.2	8.0	83.9	16.1
Multifamily	59.7	34.0	3.1	3.1	93.8	6.2
Offices[1]	41.2	45.2	9.0	4.5	86.4	13.5
Families	40.0	52.6	4.0	3.3	92.7	7.3
Housing structures						
Owner-occupied	36.0	55.9	4.4	3.7	91.9	8.1
Multifamily	59.3	38.2	1.2	1.3	97.5	2.5

NOTE. Analysis is restricted to institutions that were examined in the past five years under the large-institution CRA exam, that were in existence for at least one year, that received an "outstanding" or "satisfactory" rating on the exam, and that had assets of more than $250 million in 2003. Data exclude strategic-plan, wholesale, and limited-purpose institutions (see table 1, note 7) and institutions with headquarters in U.S.-affiliated areas. Data also exclude census tracts in U.S.-affiliated areas. For definition of assessment area, see table 9, note 1.

1. Offices consist of headquarters and branches.

remote areas and extended 18.0 percent of their home-purchase loans, 20.6 percent of their home-improvement loans, and 23.9 percent of their small-farm or small-business loans in such areas.[29]

The data for exurban areas are more difficult to interpret than are the data for remote areas. Generally, urban–rural institutions make more retail loans per family in exurban areas than in urban areas (data derived from table 10). But such institutions extend fewer retail loan dollars per deposit dollar in exurban areas than in urban areas (data derived from table 11). This apparent inconsistency may be explained by the fact that the majority of the urban–rural institutions in our sample, particularly the smaller ones, have headquarters in exurban areas. The deposit data may reflect a practice by some of those institutions of booking deposits to their headquarters regardless of the locale from which deposits originated.

The tendency of urban–rural institutions to make more retail loans to their rural components than to their urban components also holds true at the level of the individual institution. With one exception, more than one-half of the institutions in every size category

29. In two size classes (the largest and the smallest), remote areas received fewer multifamily loans as measured against the distribution of families than did other areas. However, in both cases, remote areas received more multifamily loans as measured against multifamily housing structures, arguably a better measure of comparison.

11. Retail loan amounts and deposits in the assessment areas of large banking institutions with urban and rural branches, grouped by asset size of institution and distributed by location of assessment area, as of December 31, 2003
Percent

Asset size of institution and loan amounts and deposits	Urban		Rural		Total	
	Center city	Suburban	Exurban	Remote	Urban	Rural
$250 million to $500 million						
Loans						
Home-purchase	24.9	34.4	24.8	16.0	59.2	40.8
Home-improvement	12.1	40.6	33.0	14.2	52.7	47.3
Small-business or small-farm	19.4	26.0	27.0	27.6	45.3	54.7
Multifamily	38.0	32.9	23.9	5.2	71.0	29.0
Deposits	20.1	23.7	40.3	15.9	43.8	56.2
$500 million to $1 billion						
Loans						
Home-purchase	27.2	36.0	18.8	18.0	63.2	36.8
Home-improvement	20.7	31.6	27.1	20.6	52.3	47.7
Small-business or small-farm	26.6	25.7	23.7	23.9	52.3	47.6
Multifamily	58.9	20.5	9.8	10.7	79.4	20.5
Deposits	29.8	29.1	27.5	13.6	58.9	41.1
$1 billion to $5 billion						
Loans						
Home-purchase	34.9	43.3	12.0	9.7	78.2	21.7
Home-improvement	24.5	43.5	19.2	12.8	68.0	32.0
Small-business or small-farm	40.0	32.2	14.3	13.6	72.2	27.9
Multifamily	57.8	29.4	6.0	6.8	87.2	12.8
Deposits	43.3	29.3	18.8	8.5	72.6	27.3
More than $5 billion						
Loans						
Home-purchase	36.5	57.1	2.9	3.4	93.6	6.4
Home-improvement	27.1	61.1	6.2	5.5	88.2	11.7
Small-business or small-farm	41.7	43.6	7.4	7.2	85.3	14.6
Multifamily	59.8	37.2	1.3	1.7	97.0	3.0
Deposits	59.8	32.7	5.2	2.3	92.5	7.5

NOTE. See general note to table 10.

extended more retail loans per family, per owner-occupied housing structure, or per multifamily housing structure to the rural parts of their assessment areas than to the urban parts (table 12). The exception was multifamily loans for institutions in the smallest size category. When measured in terms of retail loan dollars per deposit dollar, the results were somewhat mixed. For example, the rural parts appeared to get more home-improvement loans but fewer home-purchase loans than did the urban parts.[30]

The second test compared rural institutions with similarly situated urban institutions in two respects: the likelihood of receiving an "outstanding" CRA rating and the level of engagement in community development lending. The sample in this test used the same size categories as the sample in the first test and was also restricted to institutions covered under the large-institution evaluation procedures. The second test, however, eliminated the requirement that an institution have both urban and rural parts in its assessment areas.

30. The calculations of retail loan dollars per deposit dollars tend to show higher lending to the urban part than do the calculations of retail loan numbers per population because retail loans in urban areas are generally larger than in rural areas, a reflection of higher property values.

The evidence suggests that rural banking institutions with assets of less than $1 billion are not less likely to receive "outstanding" ratings than are urban institutions with assets of less than $1 billion (table 13). Exurban institutions with assets between $250 million and $500 million are somewhat less likely to receive "outstanding" ratings than are their urban counterparts, but exurban institutions with assets between $500 million and $1 billion are significantly more likely to do so. Few institutions with assets exceeding $1 billion have headquarters in rural areas; those in that category are less likely to receive "outstanding" CRA ratings than are institutions that have assets exceeding $1 billion and headquarters in urban areas.

The evidence offers modest support for the conclusion that rural institutions do less community development lending than do similarly sized urban institutions. In each asset-size category under $5 billion, the percentage of rural institutions that reported no community development lending in 2003 was comparable to the percentage of similarly sized urban institutions that did so (data derived from table 13). However, for every asset-size category, with one exception, rural institutions that reported community development lending for 2003 made a smaller dollar amount

12. Proportion of large banking institutions with both urban and rural branches that overserve parts of their assessment areas in terms of either number of loans or loan amount, by asset size of institution, type of loan, and location of assessment area, as of December 31, 2003

Percent

Loan measure and loan type	Rural			Urban
	Exurban	Remote	Total	
Number of loans, by asset size of institution				
$250 million to $500 million				
Home-purchase	55.6	35.5	62.9	37.1
Home-improvement	63.2	35.1	77.2	22.8
Small-business or small-farm	51.8	38.7	59.9	40.1
Multifamily	32.1	17.3	43.2	56.8
$500 million to $1 billion				
Home-purchase	53.8	43.2	65.1	34.9
Home-improvement	55.3	42.7	68.0	32.0
Small-business or small-farm	56.2	43.8	66.9	33.1
Multifamily	39.3	29.5	53.6	46.4
$1 billion to $5 billion				
Home-purchase	65.8	44.7	71.1	28.9
Home-improvement	67.6	47.9	76.8	23.2
Small-business or small-farm	60.8	45.8	67.3	32.7
Multifamily	40.6	32.3	53.4	46.6
More than $5 billion				
Home-purchase	49.5	49.5	53.8	46.2
Home-improvement	66.7	51.9	64.2	35.8
Small-business or small-farm	64.0	64.0	67.4	32.6
Multifamily	51.8	43.5	61.2	38.8
Loan amount, by asset size of institution				
$250 million to $500 million				
Home-purchase	29.0	32.3	37.9	62.1
Home-improvement	39.5	37.7	52.6	47.4
Small-business or small-farm	28.5	37.2	48.2	51.8
Multifamily	19.8	17.3	29.6	70.4
$500 million to $1 billion				
Home-purchase	26.0	37.9	44.4	55.6
Home-improvement	36.7	38.0	52.7	47.3
Small-business or small-farm	31.5	43.8	49.4	50.6
Multifamily	23.2	21.4	34.8	65.2
$1 billion to $5 billion				
Home-purchase	30.3	46.1	41.4	58.6
Home-improvement	50.0	49.3	62.0	38.0
Small-business or small-farm	26.8	47.1	41.8	58.2
Multifamily	15.0	22.6	26.3	73.7
More than $5 billion				
Home-purchase	34.4	62.4	50.5	49.5
Home-improvement	54.3	77.8	66.7	33.3
Small-business or small-farm	40.4	75.3	69.7	30.3
Multifamily	11.8	31.8	21.2	78.8

NOTE. See general note to table 10. Overserving by an institution in part of its assessment areas is measured by the ratio of the number of loans or the aggregate loan amount in that part to the number of owner-occupied housing structures (in the case of home-purchase and home-improvement loans), or to the number of families (in the case of small-business or small-farm loans), or to the number of multifamily housing structures (in the case of multifamily loans) in that part. An institution overserves in part of its assessment areas for a particular loan type if the ratio in the part, either for number of loans or loan amount, exceeds the average ratio for all the institution's assessment areas.

of community development loans than did urban institutions. The exception was remote institutions with assets between $500 million and $1 billion. These institutions had higher community development loan dollar amounts than did the combination of same-sized center-city and suburban institutions.

13. Share of large banking institutions that received an "outstanding" rating on their most recent large-institution CRA exam and the extent of community development lending among large institutions, by asset size of institution and location of headquarters, as of December 31, 2003

Characteristic and asset size of institution	Urban		Rural	
	Center city	Suburban	Exurban	Remote
"Outstanding" rating				
$250 million to $500 million				
Number	137	163	95	62
Percent	8.0	9.8	6.3	14.5
$500 million to $1 billion				
Number	184	171	47	39
Percent	13.0	13.5	29.8	15.4
$1 billion to $5 billion				
Number	217	113	32	12
Percent	29.0	28.3	3.1	16.2
More than $5 billion				
Number	144	24	7	1
Percent	52.1	45.8	.0	.0
Made community development loans in 2003[1]				
$250 million to $500 million				
Percent	63.0	53.8	56.3	53.8
Average amount (thousands of dollars)	3,833	3,164	2,074	1,346
$500 million to $1 billion				
Percent	74.7	65.3	55.6	73.5
Average amount (thousands of dollars)	7,321	5,117	2,363	7,009
$1 billion to $5 billion				
Percent	84.0	74.5	68.0	72.7
Average amount (thousands of dollars)	24,073	22,106	9,070	13,338
More than $5 billion				
Percent	90.8	84.2	100.0	100.0
Average amount (thousands of dollars)	291,814	188,318	19,945	6,716

NOTE. See general note to table 10.

1. Average amount of loans was among institutions with such lending.

This evidence on community development lending, however, is indirect and inconclusive. For example, it excludes any measure of community development investments or services. Moreover, because we lack information about the location of community development loans, inferences drawn from locations of institutions' headquarters are subject to dispute.

In sum, the retail lending and branching measures used here provide little evidence that banking institutions collectively or individually underserve rural areas, with the possible exception of community development lending. Moreover, there is no evidence that a lower percentage of rural-based institutions receive "outstanding" CRA performance ratings (at least for such institutions with less than $1 billion in assets).

Rural Areas That Would Be Affected by the Agencies' Proposed Options

The agencies sought comment on several alternative definitions of CRA-eligible rural census tracts. Each alternative satisfies five basic principles. First, each alternative would permit an institution to know, when it decided to make a loan or investment, whether or not the loan or investment would qualify as community development. Second, each alternative would rely on measures that change no more often than annually and in most cases change much less frequently than that. Third, each alternative would rely on purely objective statistical criteria that could be applied mechanically and without judgment. Fourth, each alternative would be easy to apply: Any required calculations would be straightforward or would be obviated by the government's publication of a list of eligible areas. Fifth, each alternative would rely on readily available, government-produced data.

The three alternatives that we considered were (1) moving the income threshold for CRA-eligible rural tracts from 80 percent to 90 percent or 100 percent of the statewide nonmetropolitan median family income, (2) changing the baseline for determining the CRA eligibility of rural tracts from the statewide nonmetropolitan median family income to the statewide median family income, and (3) adopting a modified version of the criteria used by the Community Development Financial Institutions Fund (CDFI Fund) to identify "investment areas."

The fund uses four alternative criteria of interest here to classify geographic areas (tracts, counties, or other aggregations) as investment areas. According to the fund, an area qualifies as an investment area if it has (1) a median family income that is less than 80 percent of the relevant metropolitan median family income or the national metropolitan median family income, whichever is higher, in the case of a metropolitan area, or a median family income that is less than 80 percent of the relevant statewide nonmetropolitan median family income or the national nonmetropolitan median family income, whichever is higher, in the case of a nonmetropolitan area; (2) an unemployment rate of at least 1.5 times the national average; (3) a poverty rate of 20 percent or more; (4) a population loss of 10 percent or more between the previous and most recent censuses or a net migration loss of 5 percent or more over the five-year period preceding the most recent census.[31] Data for unemployment, poverty, and population are updated annually at the county level and decennially at the tract level.

To permit comparison with the current rule, we modified the fund's criteria. Instead of using the fund's income criterion, we used the CRA's. That is, we treated as CRA-eligible any tracts currently classified as lower income (using, in rural areas, the current CRA baseline of the nonmetropolitan statewide median family income) *and* any tracts currently classified as middle income that are located in a county that meets any of criteria 2 through 4. Thus, in this article, when we refer to the "modified CDFI Fund criteria," we use a modification of the first fund criterion, the one based on income.

There are two key differences between the fund's criteria, which use non-income measures of community need, and the other alternatives, each of which relies solely on a relative tract-income criterion. First, the fund's criteria use measures for which data are at the county level, not the tract level. Second, the fund's county-level criteria use measures that are updated annually; income data at the tract level, in contrast, are updated only every ten years.[32] Consequently, the way in which the fund's criteria identify CRA-eligible areas is different from that in which the income-based alternatives do, and the difference can result in different outcomes.

Our analysis expands on the agencies' proposal in two main respects. The agencies proposed to apply the alternatives outlined earlier only to rural areas and only for the purpose of qualifying activities as community development. Our analysis evaluates the alternatives on those terms but goes beyond those terms. In particular, we show the implications of adopting these alternatives in urban areas, divided into central-city and suburban components, and in rural areas, divided into exurban and remote components. We also show the implications of adopting the alternatives for the purpose of evaluating other CRA-related activities, such as retail lending (table 14).

We computed the effects of the alternatives on the coverage of rural and urban census tracts and on the retail lending activities that would have counted as CRA-related if the alternatives had been in effect in 2003 (we assumed that banking institutions had not altered their behavior). We compared each alternative with actual 2003 retail lending activities adjusted for changes, implemented in 2004, in the definitions and boundaries of metropolitan statistical areas.[33]

31. Community Development Financial Institutions Fund, U.S. Department of the Treasury (2004), "Community Development Financial Institutions Program," *Federal Register*, vol. 69 (May 11), p. 26259. The fund's definition of an investment area contains an additional criterion, which states that the area has "significant unmet needs for loans, equity investments, or financial services." We disregarded this criterion because the fund refrained from defining it in objective, quantitative terms.

32. The two population criteria that we use in our adaptation of the fund's criteria are based on 2000 census data.

33. Institutions that filed 2003 HMDA and CRA small-business data used census tract definitions based on the 2000 census. Metropolitan area boundaries based on the 2000 census were not implemented

14. Comparison of effects, on census tracts and on counties, of options for defining census tracts as CRA-eligible, by location of tract, as of December 31, 2003

Percent

Item	Urban		Rural		Total		
	Center city	Suburban	Exurban	Remote	Urban	Rural	All
Current rule							
Less than 80 percent of MSA or non-MSA median[1]							
CRA-eligible tracts	43.5	18.6	12.6	17.9	31.1	14.6	28.0
Population	39.7	17.2	11.1	15.6	27.7	12.6	25.1
Loans							
Small-business or small-farm	30.7	16.7	10.9	13.1	22.5	11.9	15.8
Home-purchase	20.3	13.8	9.1	12.7	16.8	10.7	12.9
Multifamily	43.2	23.0	14.9	13.3	33.5	14.3	25.5
Branches	33.1	20.6	13.8	15.7	25.8	14.7	18.6
Deposits	38.9	22.1	15.2	16.7	30.0	15.9	20.9
Counties without CRA-eligible tracts	12.0	31.9	56.9	61.3	18.0	59.0	44.8
Counties with only CRA-eligible tracts	.6	2.8	1.7	4.8	2.4	3.2	2.9
Options							
Less than 90 percent of MSA or non-MSA median[1]							
CRA-eligible tracts	53.5	31.5	27.8	37.8	42.5	31.6	40.4
Population	50.1	29.7	25.4	34.3	39.3	28.5	37.4
Loans							
Small-business or small-farm	41.2	33.5	27.4	36.4	38.7	31.6	34.2
Home-purchase	30.2	30.4	25.2	34.7	33.0	29.5	30.7
Multifamily	54.7	39.6	28.2	30.7	48.0	29.1	40.1
Branches	43.9	39.7	32.3	40.8	43.9	36.4	39.0
Deposits	50.0	41.5	33.7	41.6	48.3	37.5	41.3
Counties without CRA-eligible tracts	8.5	13.2	29.5	31.3	5.9	30.4	21.9
Counties with only CRA-eligible tracts	1.9	9.7	6.8	18.3	8.5	12.4	11.1
Less than 100 percent of MSA or non-MSA median[1]							
CRA-eligible tracts	63.0	47.0	51.0	62.3	55.0	55.3	55.1
Population	60.0	45.2	48.1	57.7	52.1	51.4	52.0
Loans							
Small-business or small-farm	52.5	54.2	52.8	65.8	56.7	58.8	58.1
Home-purchase	42.4	49.8	50.7	62.4	50.2	56.1	54.0
Multifamily	65.9	58.9	49.7	53.8	63.9	51.2	58.6
Branches	56.1	59.7	58.3	69.4	61.7	63.6	63.0
Deposits	60.7	60.9	59.7	69.8	64.9	64.6	64.7
Counties without CRA-eligible tracts	5.8	3.2	10.0	10.3	1.3	10.1	7.1
Counties with only CRA-eligible tracts	4.1	20.4	21.3	42.3	17.1	31.5	26.5
Less than 80 percent of state median[2]							
CRA-eligible tracts	41.6	17.5	39.8	48.2	29.5	43.0	32.1
Population	37.8	15.9	37.5	44.6	26.2	40.0	28.6
Loans							
Small-business or small-farm	32.4	15.9	40.0	46.9	21.4	43.2	35.2
Home-purchase	22.0	13.8	38.3	45.5	16.4	41.6	32.8
Multifamily	44.1	21.4	38.3	37.6	32.3	38.0	34.7
Branches	34.6	19.6	46.2	51.8	24.8	48.9	40.5
Deposits	40.4	20.9	47.3	52.4	28.7	49.8	42.4
Counties without CRA-eligible tracts	12.2	37.4	18.7	24.4	23.2	21.5	22.1
Counties with only CRA-eligible tracts	1.2	3.2	15.3	28.2	2.8	21.6	15.0
Modified CDFI Fund criteria[3]							
Combined							
CRA-eligible tracts	49.1	22.9	29.6	38.1	36.0	32.8	35.4
Population	45.1	21.5	27.9	34.5	32.6	30.2	32.1
Loans							
Small-business or small-farm	36.4	22.5	31.1	38.6	28.0	34.6	32.2
Home-purchase	26.6	20.3	30.3	36.1	23.3	33.0	29.6
Multifamily	49.0	28.8	29.1	31.3	39.1	29.9	35.3
Branches	38.9	26.5	33.9	41.3	31.6	37.5	35.4
Deposits	44.2	27.9	34.9	42.1	35.4	38.3	37.3
Counties without CRA-eligible tracts	11.2	29.6	45.9	44.1	16.9	45.1	35.3
Counties with only CRA-eligible tracts	1.6	7.8	24.3	33.7	6.8	28.9	21.2

Each of the proposals would substantially increase the number of rural tracts that are CRA-eligible—that is, eligible for area-based community development activities. Currently, 14.6 percent of rural census tracts are classified as CRA-eligible; these tracts contain 12.6 percent of the rural population. Raising the threshold to 90 percent for rural areas would roughly equate the percentages of urban and rural tracts classified as CRA-eligible, at about 31 percent; raising the threshold to 100 percent would qualify 55 percent of rural tracts as CRA-eligible. Similarly, changing the baseline for classifying rural tracts to the state-

for filings related to HMDA and the CRA until 2004. In constructing the numbers we report here, we use the 2004 definitions of metropolitan statistical areas.

14.—Continued

Item	Urban		Rural		Total		
	Center city	Suburban	Exurban	Remote	Urban	Rural	All
Modified CDFI Fund criteria (continued)							
Unemployment							
CRA-eligible tracts	46.0	20.5	23.7	26.8	33.3	24.9	31.7
Population	42.1	19.1	22.4	24.3	29.9	23.1	28.7
Loans							
Small-business or small-farm	33.2	20.0	23.7	22.8	25.5	23.3	24.1
Home-purchase	22.9	17.6	22.2	23.4	20.4	22.8	21.9
Multifamily	45.7	26.4	24.5	21.9	36.6	23.6	31.1
Branches	35.3	23.9	26.4	25.1	28.7	25.8	26.8
Deposits	40.8	25.3	27.6	25.9	32.7	26.8	28.9
Counties without CRA-eligible tracts	11.6	30.6	49.3	55.9	17.3	52.5	40.3
Counties with only CRA-eligible tracts	1.2	5.7	14.7	16.3	5.1	15.5	11.8
Poverty							
CRA-eligible tracts	45.5	19.1	19.0	25.8	32.3	21.6	30.3
Population	41.5	17.7	17.3	23.7	28.9	19.5	27.2
Loans							
Small-business or small-farm	31.6	17.7	18.0	22.4	23.5	20.1	21.3
Home-purchase	21.2	15.1	17.1	21.6	18.1	19.2	18.8
Multifamily	44.3	23.6	19.8	19.7	34.3	19.8	28.2
Branches	33.7	21.7	20.9	25.1	26.9	22.9	24.3
Deposits	39.4	23.2	22.1	25.9	31.0	23.9	26.4
Counties without CRA-eligible tracts	12.0	31.5	54.9	57.0	17.8	55.9	42.7
Counties with only CRA-eligible tracts	.6	4.4	12.3	17.6	3.9	14.9	11.1
Population loss							
CRA-eligible tracts	47.8	21.0	15.2	25.7	34.4	19.2	31.5
Population	43.5	19.4	13.3	22.0	30.7	16.3	28.2
Loans							
Small-business or small-farm	33.9	18.8	14.5	24.9	24.7	19.4	21.3
Home-purchase	24.1	16.0	12.9	22.3	19.3	17.2	17.9
Multifamily	46.2	25.1	16.5	20.5	35.9	18.0	28.4
Branches	36.7	22.7	17.8	28.3	28.2	22.9	24.7
Deposits	42.3	24.2	19.1	29.2	32.3	24.0	26.9
Counties without CRA-eligible tracts	11.6	31.1	54.1	51.2	17.8	52.7	40.6
Counties with only CRA-eligible tracts	1.0	3.9	5.7	17.8	3.1	11.6	8.6
MEMO							
Number of tracts	26,278	26,298	7,661	4,650	52,576	12,311	64,887

NOTE. See general note to table 9, and for description of lending and branch data reported in 2003 geographies, see related description for assessment areas in table 9, note 1. Analysis is restricted to lending done within assessment areas and excludes institutions not covered by the CRA.

1. Median family income in census tract as a percentage of the median family income in the metropolitan statistical area (MSA) or nonmetropolitan portion of the state (non-MSA) in which the census tract is located.

2. Median family income in census tract as a percentage of the median family income in the state in which the census tract is located.

3. For description of modification to CDFI Fund criteria, see text.

CDFI Fund Community Development Financial Institutions Fund.

wide median but retaining the 80 percent threshold-would qualify 43 percent of rural tracts as CRA-eligible.[34]

We also calculated the effects of adopting the modified CDFI Fund criteria. Using the criteria to identify middle-income tracts that would be CRA-eligible would classify 33 percent of rural census tracts as lower income, a proportion nearly equal to the 31 percent of urban census tracts currently classified as CRA-eligible (see "Current rule" and "Modified CDFI Fund criteria" categories). When each of the unemployment, poverty, and population loss criteria is applied separately, the proportion of rural tracts classified as CRA-eligible is 25 percent, 22 percent, and 19 percent respectively. Applying the modified CDFI Fund criteria to urban tracts would have a comparatively modest effect, increasing the number of urban tracts classified as CRA-eligible from 31 percent to 36 percent. The general patterns described in this paragraph and in the previous one are also found when the unit of analysis is the proportion of population in CRA-eligible tracts.

We also profiled the economic and demographic characteristics of the tracts now classified as lower income and of the additional tracts that would be CRA-eligible under each of the alternatives (table 15). The profile reveals that, in rural areas, the exurban and remote tracts *currently* classified as lower income have similar average characteristics along most dimensions (although the number of tracts in exurban and remote areas is different). In urban

34. Rhode Island is the only state in which the nonmetropolitan area median income is higher than the overall state median income.

15. Characteristics of CRA-eligible census tracts and counties and of those that would be added under options for defining census tracts as CRA-eligible, by location of tract, as of December 31, 2003

Percent except as noted

Item	Urban		Rural		Total		
	Center city	Suburban	Exurban	Remote	Urban	Rural	All
Current rule							
Less than 80 percent of MSA or non-MSA median[1]							
Tract (average characteristics)							
Number added	11,441	4,900	969	833	16,341	1,802	18,143
Share of families with income							
Less than or equal to poverty level	23.9	15.6	22.9	23.1	21.4	23.0	21.6
Less than 50 percent of MSA or non-MSA median[1]	43.8	35.3	34.5	34.7	41.3	34.6	40.6
Between 50 percent and 80 percent of MSA or non-MSA median[1]	22.7	24.8	22.2	22.6	23.3	22.4	23.2
Median family income (dollars)	30,067	36,343	27,741	27,090	31,949	27,440	31,501
Median relative to MSA or non-MSA	57.5	66.6	69.6	69.0	60.2	69.3	61.1
Housing							
Median house value (dollars)	98,973	94,019	53,528	51,056	97,480	52,389	92,969
Median house age (years)	30.6	33.1	33.9	35.1	31.4	34.5	31.7
Occupancy by owner	35.3	48.1	53.5	53.3	39.2	53.5	40.6
Vacancy rate[2]	9.8	9.2	15.6	18.4	9.7	16.9	10.4
Population							
Over age 65	10.7	12.7	14.1	14.6	11.3	14.4	11.6
Minority[3]	66.7	45.9	40.8	33.4	60.4	37.4	58.1
County (average characteristics)							
Population change, 1990–2000	1.1	1.2	1.1	1.0	1.1	1.1	1.1
Net migration rate, 1995–99[4]	–1.3	2.4	.8	–.9	–.2	.0	–.2
Poverty rate, 2002	14.1	11.4	17.5	19.3	13.3	18.3	13.8
Unemployment rate, 2001	6.0	5.6	7.6	7.2	5.9	7.4	6.1
Options							
Less than 90 percent of MSA median or non-MSA median[1]							
Tract (average characteristics)							
Number added	2,622	3,384	1,157	927	6,006	2,084	8,090
Share of families with income							
Less than or equal to poverty level	10.0	8.2	13.7	13.3	9.0	13.5	10.2
Less than 50 percent of MSA or non-MSA median[1]	23.9	22.8	24.4	24.1	23.3	24.3	23.5
Between 50 percent and 80 percent of MSA or non-MSA median[1]	21.9	22.9	21.4	21.9	22.4	21.6	22.2
Median family income (dollars)	44,231	45,911	34,668	34,489	45,178	34,588	42,450
Median relative to MSA or non-MSA	85.1	85.2	85.6	85.3	85.2	85.5	85.3
Housing							
Median house value (dollars)	121,304	103,360	64,487	59,496	111,172	62,269	98,569
Median house age (years)	34.1	35.9	37.2	38.2	35.1	37.6	35.7
Occupancy by owner	52.3	63.8	61.3	59.3	58.8	60.4	59.2
Vacancy rate[2]	6.4	8.1	15.4	18.6	7.3	16.8	9.8
Population							
Over age 65	13.0	14.0	15.8	16.7	13.6	16.2	14.2
Minority[3]	40.5	24.7	19.7	15.6	31.6	17.9	28.1
County (average characteristics)							
Population change, 1990–2000	1.1	1.2	1.1	1.0	1.1	1.1	1.1
Net migration rate, 1995–99[4]	.1	3.0	2.4	.3	1.8	1.5	1.7
Poverty rate, 2002	13.0	10.5	14.7	15.4	11.6	15.0	12.5
Unemployment rate, 2001	5.8	5.4	6.6	6.1	5.6	6.3	5.8
Less than 100 percent of MSA median or non-MSA median[1]							
Tract (average characteristics)							
Number added	5,125	7,453	2,937	2,063	12,578	5,000	17,578
Share of families with income							
Less than or equal to poverty level	9.0	7.1	11.9	11.7	7.9	11.8	9.0
Less than 50 percent of MSA or non-MSA median[1]	21.8	20.3	21.7	21.8	20.9	21.7	21.1
Between 50 percent and 80 percent of MSA or non-MSA median[1]	20.9	21.6	20.4	20.8	21.3	20.6	21.1
Median family income (dollars)	46,727	48,883	36,962	36,682	48,004	36,847	44,830
Median relative to MSA or non-MSA	89.0	90.6	91.3	90.6	90.3	91.0	90.5
Housing							
Median house value (dollars)	125,857	110,561	68,236	64,522	116,781	66,704	102,523
Median house age (years)	34.6	36.1	37.4	38.5	35.5	37.8	36.2
Occupancy by owner	54.6	66.4	63.0	61.1	61.6	62.2	61.8
Vacancy rate[2]	6.1	7.5	15.0	17.5	7.0	16.1	9.6
Population							
Over age 65	13.2	13.7	15.7	16.8	13.5	16.1	14.3
Minority[3]	37.2	21.5	16.6	13.5	27.9	15.3	24.4
County (average characteristics)							
Population change, 1990–2000	1.1	1.2	1.1	1.0	1.1	1.1	1.1
Net migration rate, 1995–99[4]	.2	2.8	2.3	.5	1.7	1.5	1.7
Poverty rate, 2002	12.8	10.3	14.1	14.4	11.3	14.2	12.1
Unemployment rate, 2001	5.8	5.3	6.4	5.7	5.5	6.1	5.7

See footnotes on page 228.

areas, however, the center-city and suburban tracts with this classification are largely dissimilar. Further, a comparison of lower-income tracts in urban and rural areas reveals differences in most characteristics. The differences between suburban and exurban tracts are a case in point: Exurban tracts have higher pov-

15.—Continued

Percent except as noted

Item	Urban: Center city	Urban: Suburban	Rural: Exurban	Rural: Remote	Total: Urban	Total: Rural	Total: All
Less than 80 percent of state median[5]							
Tract (average characteristics)							
Number added	902	1,100	2,082	1,407	2,002	3,489	5,491
Share of families with income							
Less than or equal to poverty level	14.2	11.8	12.7	12.4	12.9	12.6	12.7
Less than 50 percent of MSA or non-MSA median[1]	23.9	22.9	22.5	22.6	23.4	22.6	22.9
Between 50 percent and 80 percent of MSA or non-MSA median[1]	20.6	21.2	20.5	21.1	20.9	20.7	20.8
Median family income (dollars)	37,626	39,441	35,969	35,755	38,623	35,883	36,882
Median relative to MSA or non-MSA	88.0	88.6	90.3	89.0	88.3	89.7	89.2
Housing							
Median house value (dollars)	98,707	92,916	66,651	62,111	95,517	64,821	76,000
Median house age (years)	32.9	35.5	37.4	38.2	34.3	37.7	36.5
Occupancy by owner	51.7	59.6	61.9	60.8	56.1	61.4	59.5
Vacancy rate[2]	7.6	9.9	15.7	18.1	8.8	16.6	13.8
Population							
Over age 65	12.8	14.1	15.9	16.7	13.5	16.2	15.3
Minority[3]	48.5	33.9	18.7	14.5	40.5	17.0	25.6
County (average characteristics)							
Population change, 1990–2000	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Net migration rate, 1995–99[4]	–.8	.6	2.5	.9	.0	1.9	1.2
Poverty rate, 2002	16.6	14.0	14.6	15.0	15.2	14.7	14.9
Unemployment rate, 2001	7.2	6.9	6.5	6.0	7.1	6.3	6.6
Modified CDFI Fund criteria[6]							
Combined							
Tract (average characteristics)							
Number added	1,466	1,133	1,296	939	2,599	2,235	4,834
Share of families with income							
Less than or equal to poverty level	10.8	9.2	13.6	13.3	10.1	13.5	11.7
Less than 50 percent of MSA or non-MSA median[1]	20.8	18.4	21.6	22.0	19.8	21.8	20.7
Between 50 percent and 80 percent of MSA or non-MSA median[1]	18.4	19.0	18.4	19.2	18.6	18.8	18.7
Median family income (dollars)	46,066	46,384	36,635	36,788	46,204	36,699	41,810
Median relative to MSA or non-MSA	97.2	99.5	96.7	94.3	98.2	95.7	97.1
Housing							
Median house value (dollars)	125,820	107,152	66,391	62,328	117,679	64,686	93,151
Median house age (years)	34.8	35.2	36.9	38.1	35.0	37.4	36.1
Occupancy by owner	53.8	65.2	64.4	60.8	58.8	62.9	60.7
Vacancy rate[2]	6.6	8.2	15.2	18.3	7.3	16.5	11.6
Population							
Over age 65	13.7	13.0	14.7	15.9	13.4	15.2	14.3
Minority[3]	47.2	32.2	25.6	19.6	40.6	23.1	32.5
County (average characteristics)							
Population change, 1990–2000	1.1	1.1	1.1	1.0	1.1	1.1	1.1
Net migration rate, 1995–99[4]	–4.7	–1.6	.9	–2.1	–3.4	–.3	–2.0
Poverty rate, 2002	18.6	14.9	17.6	17.0	17.0	17.3	17.2
Unemployment rate, 2001	7.8	8.1	8.6	7.3	7.9	8.0	8.0
Unemployment							
Tract (average characteristics)							
Number added	653	502	848	412	1,155	1,260	2,415
Share of families with income							
Less than or equal to poverty level	13.3	11.4	12.4	13.5	12.5	12.8	12.6
Less than 50 percent of MSA or non-MSA median[1]	21.8	19.8	21.0	22.3	20.9	21.5	21.2
Between 50 percent and 80 percent of MSA or non-MSA median[1]	17.5	19.0	18.7	19.4	18.1	18.9	18.6
Median family income (dollars)	44,263	43,430	37,586	37,341	43,901	37,506	40,564
Median relative to MSA or non-MSA	98.1	98.0	96.8	93.6	98.0	95.7	96.8
Housing							
Median house value (dollars)	157,326	110,582	71,274	72,214	136,980	71,581	102,828
Median house age (years)	33.8	34.0	37.5	38.3	33.9	37.8	35.9
Occupancy by owner	49.4	64.1	65.8	60.3	55.8	64.0	60.1
Vacancy rate[2]	6.4	10.2	14.5	20.5	8.0	16.5	12.4
Population							
Over age 65	12.9	11.9	15.0	15.5	12.4	15.2	13.9
Minority[3]	53.2	33.9	21.4	22.0	44.9	21.6	32.7
County (average characteristics)							
Population change, 1990–2000	1.1	1.2	1.1	1.1	1.2	1.1	1.1
Net migration rate, 1995–99[4]	–2.0	2.4	2.1	.8	–.1	1.7	.8
Poverty rate, 2002	21.5	16.0	16.3	17.2	19.1	16.6	17.8
Unemployment rate, 2001	9.9	10.8	10.0	10.2	10.3	10.0	10.2

See footnotes on page 228.

erty rates, vacancy rates, and unemployment rates and lower absolute incomes, house values, and population growth rates than do suburban tracts.

Although the specific tracts *added* by each alternative are different, their economic and demographic characteristics are similar. Under any of the alterna-

15.—Continued

Percent except as noted

Item	Urban		Rural		Total		
	Center city	Suburban	Exurban	Remote	Urban	Rural	All
Poverty							
Tract (average characteristics)							
Number added	521	131	485	368	652	853	1,505
Share of families with income							
Less than or equal to poverty level	15.0	18.8	17.4	18.1	15.8	17.7	16.9
Less than 50 percent of MSA or non-MSA median[1]	23.1	22.6	24.1	24.9	23.0	24.4	23.8
Between 50 percent and 80 percent of MSA or non-MSA median[1]	17.1	18.3	17.6	18.4	17.3	17.9	17.7
Median family income (dollars)	42,919	34,671	33,820	32,122	41,262	33,087	36,629
Median relative to MSA or non-MSA	97.3	96.0	95.0	91.8	97.1	93.7	95.1
Housing							
Median house value (dollars)	165,803	74,434	56,220	51,471	147,360	54,172	94,491
Median house age (years)	33.7	31.2	35.9	36.5	33.2	36.2	34.9
Occupancy by owner	45.9	61.1	63.7	63.9	49.0	63.8	57.4
Vacancy rate[2]	6.7	11.9	16.0	15.5	7.7	15.8	12.3
Population							
Over age 65	12.8	11.1	14.3	14.7	12.5	14.5	13.6
Minority[3]	60.9	59.1	37.7	28.7	60.6	33.8	45.4
County (average characteristics)							
Population change, 1990–2000	1.1	1.2	1.1	1.0	1.1	1.1	1.1
Net migration rate, 1995–99[4]	−4.0	1.3	.6	−.6	−2.9	.1	−1.2
Poverty rate, 2002	24.7	24.0	22.3	23.2	24.6	22.7	23.5
Unemployment rate, 2001	9.0	11.5	7.8	7.7	9.5	7.8	8.5
Population loss							
Tract (average characteristics)							
Number added	1,124	613	194	364	1,737	558	2,295
Share of families with income							
Less than or equal to poverty level	9.3	7.1	14.1	11.1	8.5	12.1	9.4
Less than 50 percent of MSA or non-MSA median[1]	20.8	17.0	21.1	20.2	19.4	20.5	19.7
Between 50 percent and 80 percent of MSA or non-MSA median[1]	18.6	19.0	18.0	19.3	18.7	18.9	18.7
Median family income (dollars)	48,241	49,149	36,513	39,179	48,561	38,252	46,055
Median relative to MSA or non-MSA	96.9	101.1	98.7	96.5	98.3	97.3	98.1
Housing							
Median house value (dollars)	135,845	106,363	55,698	59,298	125,444	58,046	109,067
Median house age (years)	35.8	36.3	35.6	38.2	36.0	37.3	36.3
Occupancy by owner	52.5	65.9	58.8	58.9	57.3	58.8	57.6
Vacancy rate[2]	6.2	6.5	16.7	17.2	6.3	17.0	8.9
Population							
Over age 65	14.5	14.0	14.3	16.4	14.3	15.7	14.6
Minority[3]	44.6	30.3	28.1	17.6	39.5	21.2	35.1
County (average characteristics)							
Population change, 1990–2000	1.0	1.0	1.0	.9	1.0	.9	1.0
Net migration rate, 1995–99[4]	−6.8	−6.1	−7.1	−7.6	−6.6	−7.4	−6.8
Poverty rate, 2002	18.2	13.8	17.0	14.5	16.6	15.4	16.3
Unemployment rate, 2001	6.8	6.1	6.3	5.1	6.6	5.5	6.3

NOTE. Data exclude tracts in U.S.-affiliated areas and tracts without income information.

1. See table 14, note 1.
2. Vacant housing units as a percentage of total housing units.
3. Non-whites or people of Hispanic origin.
4. Difference between net migration in 1999 and net migration in 1995 as a percentage of the population in 1997.
5. See table 14, note 2.
6. For description of modification to CDFI Fund criteria, see text.

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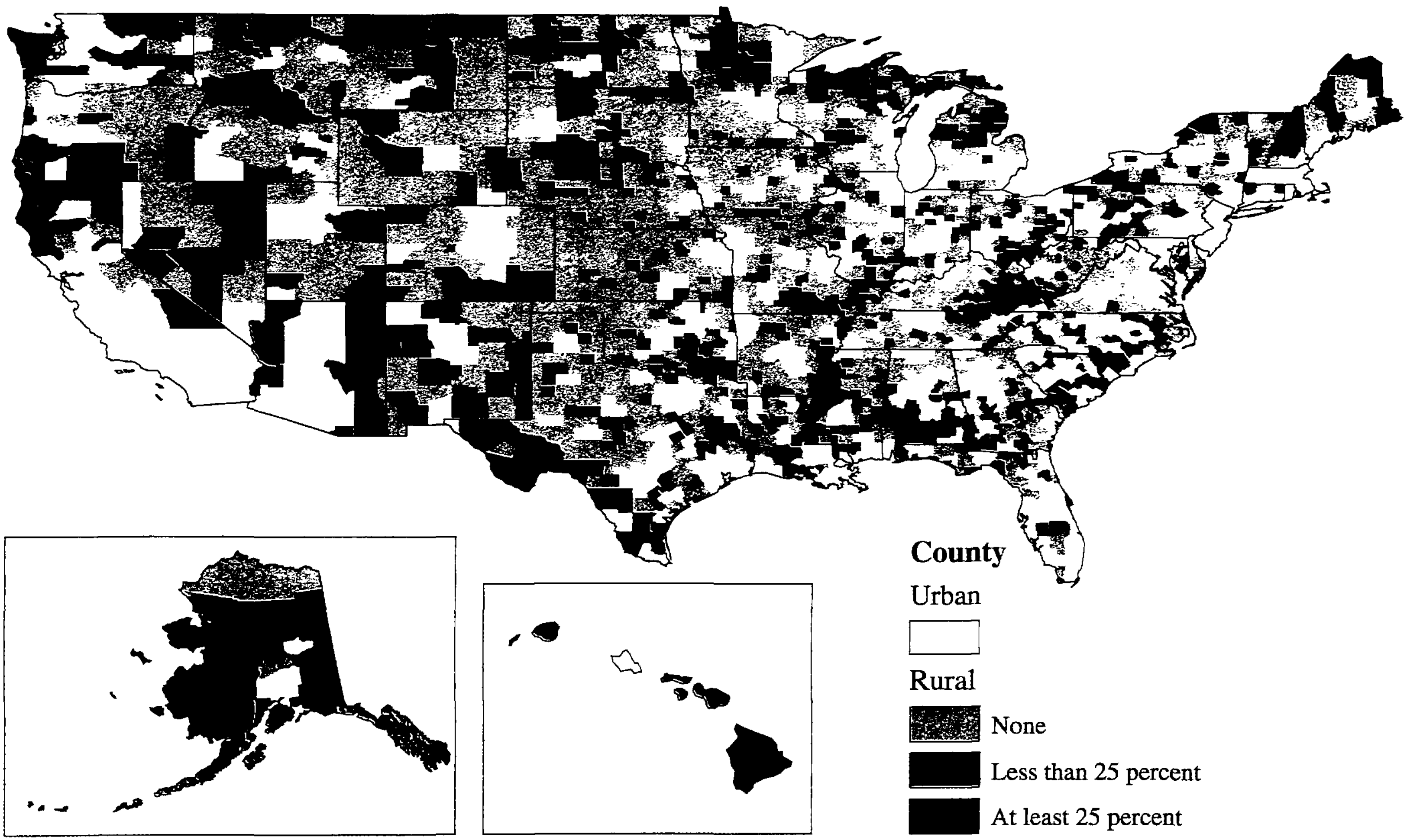
tives for expanding the class of rural CRA-eligible tracts, the rural tracts that would be newly classified as CRA-eligible show more-favorable economic characteristics than do the rural tracts currently classified as such. The relationship of the newly classified rural CRA-eligible tracts to urban tracts currently classified as CRA-eligible is complicated. Under any of the alternatives, the newly added rural CRA-eligible tracts would have lower poverty, unemployment, and population growth rates and higher owner-occupancy and vacancy rates than would the current urban CRA-eligible tracts; median incomes for both types of tract would be about the same. Moreover, the rural tracts that would be added under the alternatives that contribute the most rural tracts (100 percent of median family income and 80 percent of statewide median family income) show, not unexpectedly, the most-favorable economic characteristics.

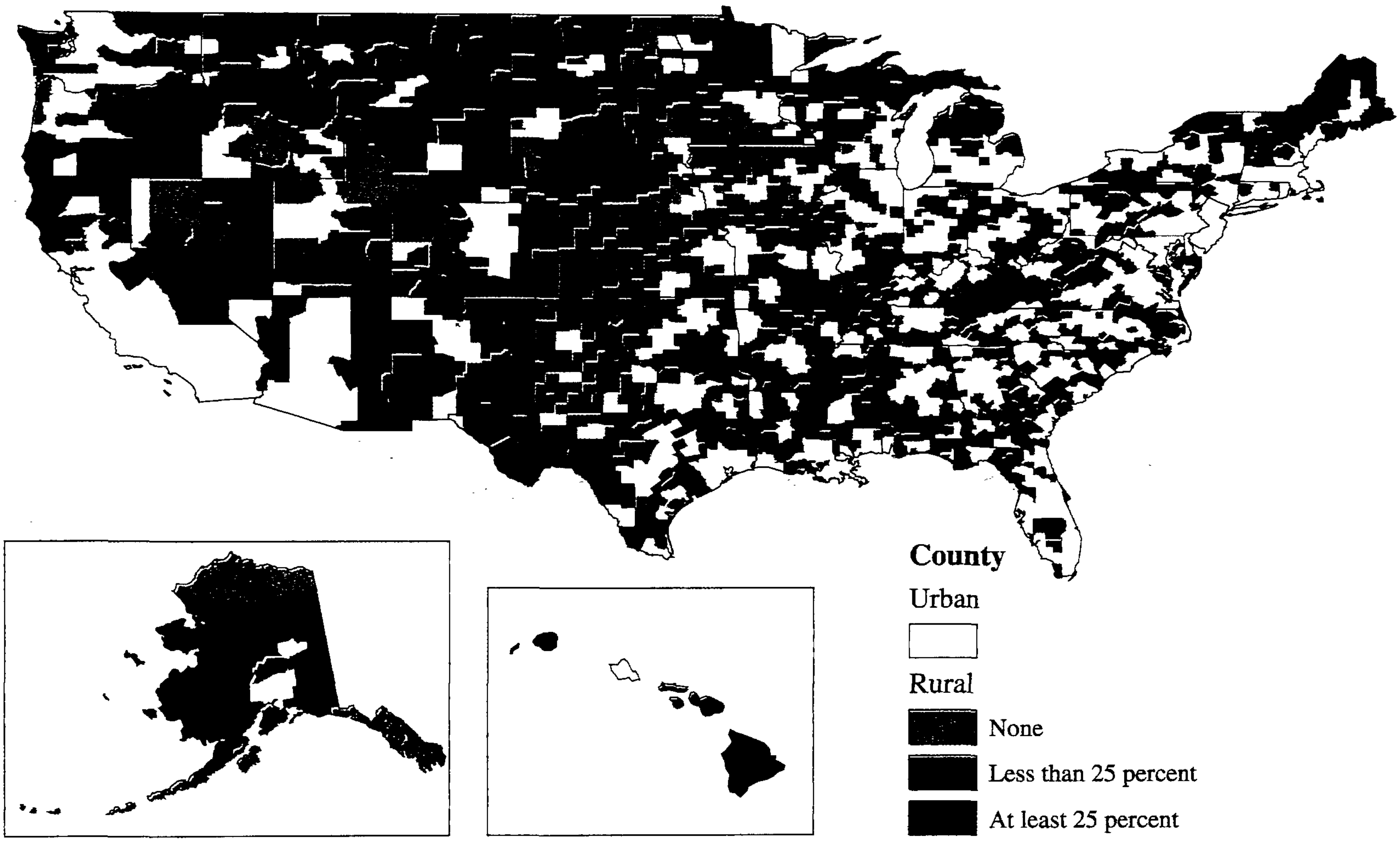
When compared with the current rule (figure 3), each alternative adds a different set of newly CRA-eligible rural tracts with significantly different geographic distributions. That is, with one exception, each alternative—raising the threshold from the current level to 90 percent (figure 4) or 100 percent (figure 5), changing the baseline to the statewide median income (figure 6), and adding the CDFI Fund's non-income criteria to the current 80 percent income rule (figure 7)—adds a set of tracts that differs from the other sets in terms of composition (the tracts that make it up), economic and

3. Census tracts in rural counties: Share that is CRA-eligible under current rule, as of December 31, 2003



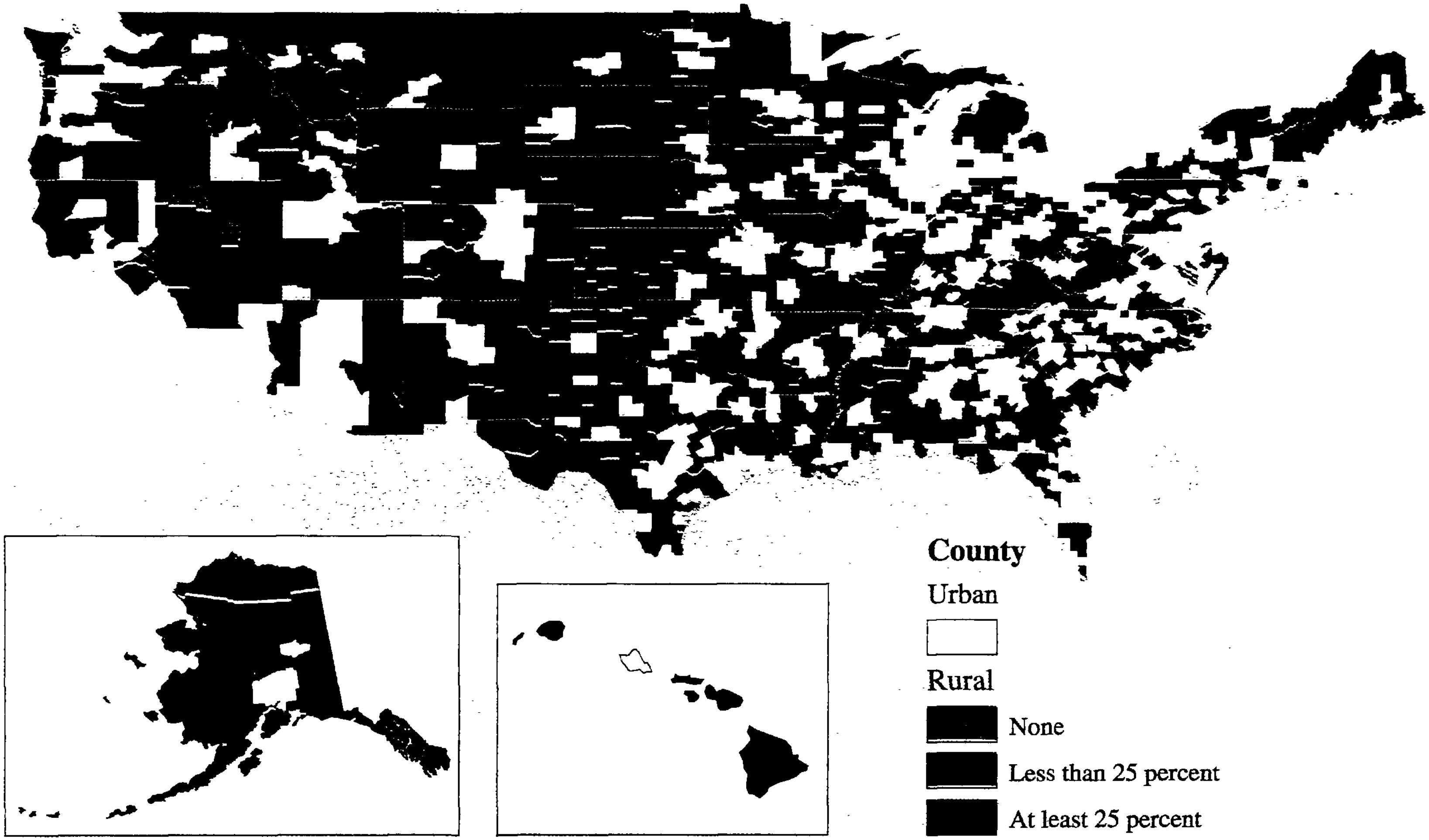
NOTE. Under the current rule, a rural census tract is CRA-eligible if the median family income in the tract is less than 80 percent of the median family income in the nonmetropolitan portion of the state.

4. Census tracts in rural counties: Share that is CRA-eligible if the income standard is set to less than 90 percent of the median in the nonmetropolitan portion of the state, as of December 31, 2003



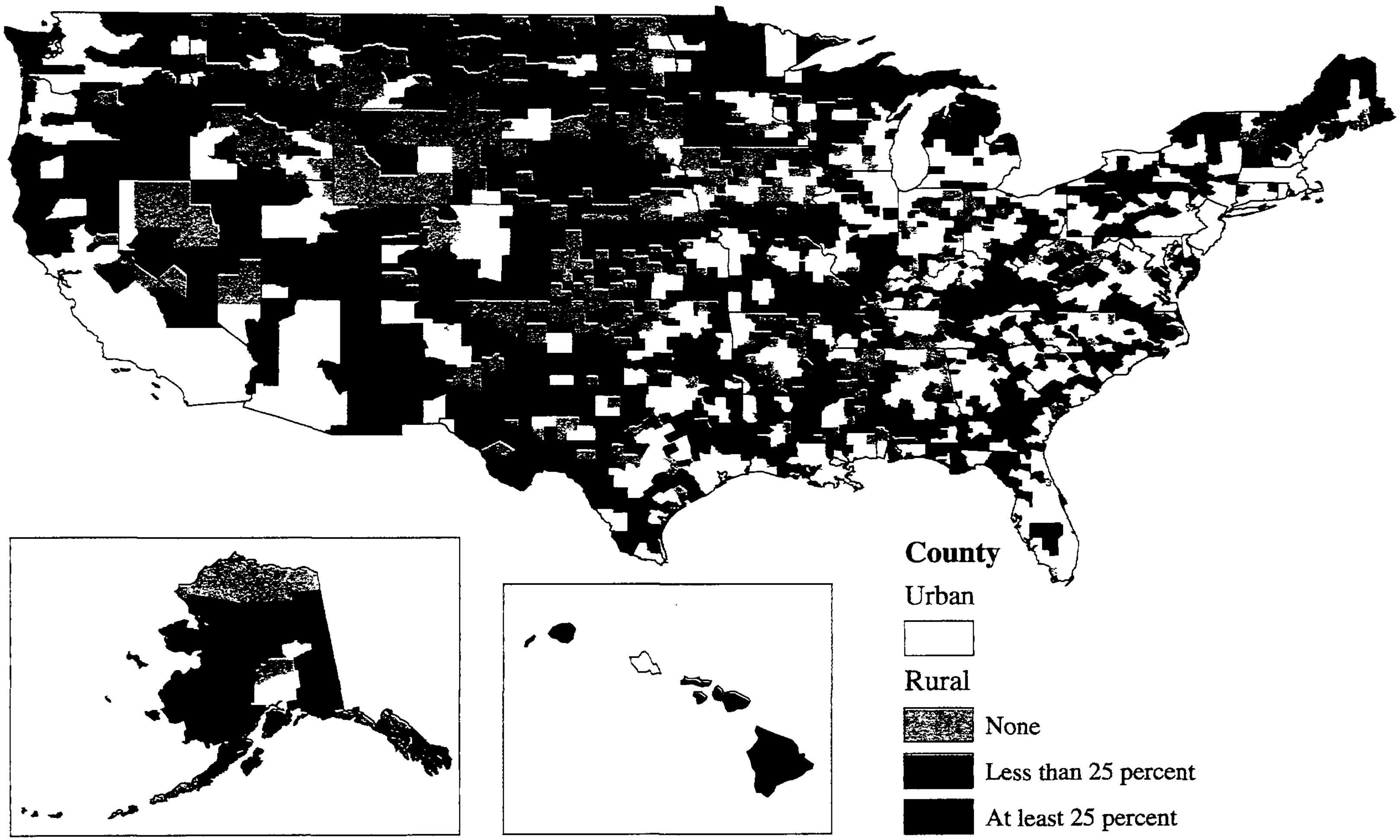
NOTE. Under this option, a rural census tract would be CRA-eligible if the median family income in the tract was less than 90 percent of the median family income in the nonmetropolitan portion of the state.

5. Census tracts in rural counties: Share that is CRA-eligible if the income standard is set to less than 100 percent of the median in the nonmetropolitan portion of the state, as of December 31, 2003



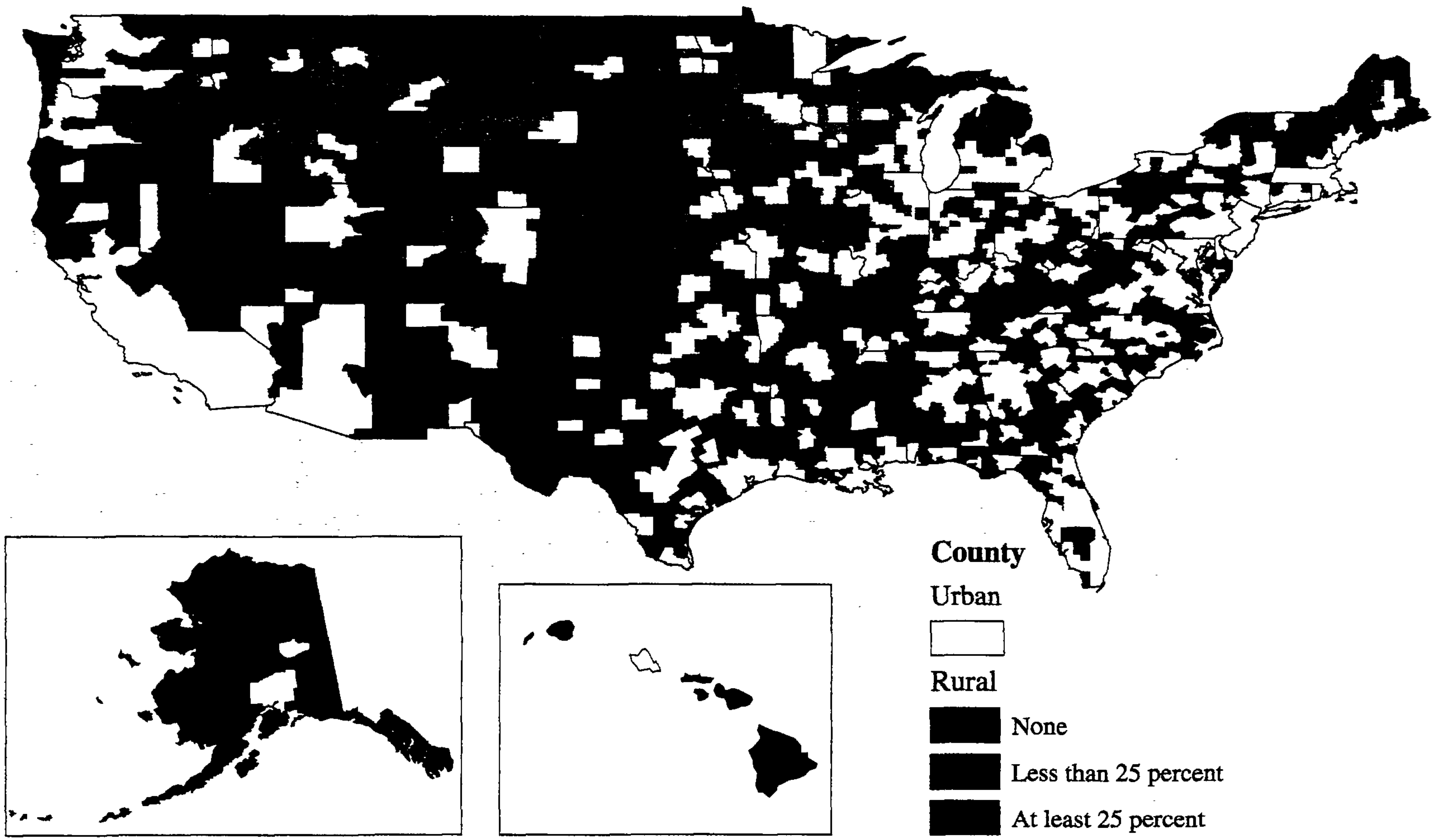
NOTE. Under this option, a rural census tract would be CRA-eligible if the median family income in the tract was less than 100 percent of the median family income in the nonmetropolitan portion of the state.

6. Census tracts in rural counties: Share that is CRA-eligible if the current 80 percent income standard is broadened from the nonmetropolitan portion of the state to the entire state, as of December 31, 2003



NOTE. Under this option, a rural census tract would be CRA-eligible if the median family income in the tract was less than 80 percent of the median family income in the entire state.

7. Census tracts in rural counties: Share that would be CRA-eligible if the standard is broadened from the current 80 percent income standard to include any of the CDFI Fund's non-income criteria, as of December 31, 2003



NOTE. Under this option, a rural census tract would be CRA-eligible if it met the income criteria specified by the current rule (see note to figure 3) or if it met one of the following non-income criteria established by the Community Development Financial Institutions Fund (CDFI Fund) for determining an investment area: an unemployment rate of at least 1.5 times the national average; a poverty rate of 20 percent or more; or a population loss of 10 percent or more between the previous and most-recent censuses or a net migration loss of 5 percent or more over the five-year period preceding the most recent census (see text discussion of table 14).

16. Number and share of rural banking institutions whose number of CRA-eligible census tracts in their assessment areas would increase under options for defining census tracts as CRA-eligible, as of December 31, 2003

Item	Income-based options			Modified CDFI Fund criteria			
	Percent of non-MSA median		Less than 80 percent of state median	Combined	Individual		
	Less than 90	Less than 100			Unemployment	Poverty	Population loss
Large institutions							
Currently with no CRA-eligible tracts							
Number	300	300	300	300	300	300	300
Rural institutions with increase in CRA-eligible tracts							
Number	155	231	200	49	27	11	18
Percent	51.7	77.0	66.7	16.3	9.0	3.7	6.0
Average increase (percentage points)	21.2	41.9	32.4	54.4	62.6	42.9	40.7
Currently with some CRA-eligible tracts							
Number	695	695	695	695	695	695	695
Rural institutions with increase in CRA-eligible tracts							
Number	629	679	650	369	243	183	152
Percent	90.5	97.7	93.5	53.1	35.0	26.3	21.9
Average increase (percentage points)	16.4	37.2	27.0	27.5	23.7	20.0	14.8
Assessment areas currently with no CRA-eligible tracts							
Number	1,268	1,268	1,268	1,268	1,268	1,268	1,268
Rural assessment areas with increase in CRA-eligible tracts							
Number	615	976	788	194	110	37	66
Percent	48.5	77.0	62.1	15.3	8.7	2.9	5.2
Average increase (percentage points)	31.2	51.7	43.7	77.1	77.0	82.0	72.4
Assessment areas currently with some CRA-eligible tracts							
Number	1,629	1,629	1,629	1,629	1,629	1,629	1,629
Rural assessment areas with increase in CRA-eligible tracts							
Number	1,312	1,557	1,406	658	412	303	192
Percent	80.5	95.6	86.3	40.4	25.3	18.6	11.8
Average increase (percentage points)	18.5	36.7	28.3	40.3	37.7	35.0	26.1
Small institutions[1]							
Currently with no CRA-eligible tracts							
Number	2,141	2,141	2,141	2,141	2,141	2,141	2,141
Rural institutions with increase in CRA-eligible tracts							
Number	1,152	1,870	1,476	389	161	75	201
Percent	53.8	87.3	68.9	18.2	7.5	3.5	9.4
Average increase (percentage points)	32.7	57.4	47.9	83.8	85.7	88.4	80.7
Currently with some CRA-eligible tracts							
Number	1,831	1,831	1,831	1,831	1,831	1,831	1,831
Rural institutions with increase in CRA-eligible tracts							
Number	1,409	1,731	1,551	681	306	421	192
Percent	77.0	94.5	84.7	37.2	16.7	23.0	10.5
Average increase (percentage points)	23.2	41.4	34.1	47.6	42.8	45.6	40.0

NOTE. See general note to table 9. A rural banking institution is an institution whose assessment area contains at least one rural census tract. For definition of relative tract income, see table 8, note 1. For description of CDFI Fund criteria, see text discussion of table 14. For definition of large and small institutions, see table 1, note 1. For description of assessment areas, see table 9, note 1.

1. Rural assessment areas were approximated by the rural counties in which small institutions had branches. These approximations were used to determine whether any of the census tracts served by small institutions would become CRA-eligible.

CDFI Fund Community Development Financial Institutions Fund.

demographic characteristics, and location. For example, of the 3,559 rural tracts added by adopting the modified CDFI Fund criteria or raising the threshold to 90 percent, only 760 (one-fifth) would be added by *both* options (data omitted from tables). Moreover, the modified CDFI Fund criteria themselves would add largely dissimilar sets of tracts: 18 percent of rural tracts that meet one or more of the criteria meet two or more of them, and less than 2 percent of rural tracts that meet one or more of the criteria meet all three criteria.[35] The exception to the pattern is that substantial overlap exists between raising the threshold to 100 percent and using the statewide median income as the baseline. Of the 5,188 rural tracts that would be added by either alternative, 64 percent would be added by *both* options.

The alternatives can also be evaluated from the perspective of banking institutions. For example, 30 percent of large institutions with at least one branch in a rural area currently have no CRA-eligible tracts in any of their rural assessment areas (table 9).[36] Under each of the three income-based

35. See David A. McGranahan and Calvin L. Beale (2002), "Understanding Rural Population Loss," *Rural America*, vol. 17 (Winter). The article is available on the website of the Economic Research Service, U.S. Department of Agriculture (www.ers.usda.gov). The authors found that the rural areas with population loss are distinct from those with high poverty.

36. Assessment areas of small institutions are approximated by the counties in which they have branches.

alternatives (raising the threshold to 90 percent or 100 percent or changing the baseline to the statewide median income), more than one-half of those institutions would have at least one CRA-eligible tract in at least one of their rural assessment areas (table 16). In contrast, under the alternative of the modified CDFI Fund criteria, only 16 percent of those institutions now without any rural CRA-eligible tracts would have at least one; however, the 16 percent would on average have 54 percent of the rural tracts they serve classified as CRA-eligible. Although the income-based measures affect many more institutions, the average effect on each institution is much smaller. For example, the typical institution that experienced a change under the statewide-median-income alternative would end up with 30 percent of its tracts classified as CRA-eligible. The difference arises from the operation of the modified CDFI Fund criteria at the county level: In our analysis, if a county meets a criterion, then all of its middle-income tracts become CRA-eligible. Each of the other, income-based alternatives is likely to affect only a portion of the middle-income tracts in a given county.

Summary of Findings

The data and the analyses reported in this article may be useful in evaluating recent proposals to revise the CRA regulations. Because of data limitations, much of the analysis uses indirect rather than direct tests. From these tests, several findings emerge.

First, we found little evidence of differences in retail lending or branching between institutions just below and just above the $250 million threshold that currently distinguishes institutions with small-institution evaluations from those with large-institution evaluations. Nor did we find evidence that institutions graduating from the small-institution evaluation to the large-institution evaluation significantly change their retail lending or branching behavior, at least in the first two years in which they are covered by the large-institution evaluation. However, the analysis was limited to inferences about the behavior of institutions around the margin of the current threshold, $250 million. Although the evidence suggests that raising the threshold some amount above $250 million would not have a significant effect on retail lending or branching, it fails to reveal what amount of increase in the threshold, if any, would result in a significant effect.

Second, in our investigation of the relationship of community development lending to overall CRA ratings for institutions examined under the large-institution examination, we found fairly consistent evidence that such lending plays a relatively limited role in determining overall CRA ratings. Indeed, a significant minority of institutions received "outstanding" ratings and reported no community development loans for three years; this finding holds true in each of several categories of institution asset size.

Third, we found little evidence to support the hypothesis that rural areas receive fewer retail loans or branches from CRA-covered institutions than do urban areas or that rural institutions have more difficulty in achieving "outstanding" ratings. Indeed, smaller rural institutions are equally or more likely to receive "outstanding" ratings than are smaller urban institutions. However, we found modest evidence that rural institutions are somewhat less likely to do any community development lending than are comparable urban institutions and that they make a lower volume of community development loans. These facts support the agencies' restriction of proposed revisions in the criteria for area-based CRA consideration to community development activities.

Finally, in our comparison of several proposals to expand area-based CRA consideration in rural areas, we found that all of the proposals would raise the number of CRA-eligible tracts in rural areas to the same percentage (or higher) as in urban areas. And all would add tracts with better economic characteristics than the tracts classified as lower-income under the 1995 regulations. However, each proposal adds a different set of tracts, affects a different number of banking institutions, and, in the case of institutions that are affected, affects them to different degrees. □

Report on the Condition of the U.S. Banking Industry: Fourth Quarter, 2004

Total assets of reporting bank holding companies rose $393.2 billion (or 4.0 percent) in the fourth quarter of 2004, to $10.3 trillion—the first time that this total has exceeded $10 trillion. The two largest asset categories—loans, and securities and money market assets—each increased roughly $170 billion, accounting for most of total asset growth.

For loans, this increase represented growth of 3.5 percent, with $152.3 billion of the increase occurring at the fifty large bank holding companies. Growth was most pronounced in the commercial real estate, home equity, and credit card categories. A sign of the invigorated lending market, reporting bank holding companies increased their unused commitments to lend $253.4 billion (5.5 percent) for the quarter and $725.8 billion (17.7 percent) for the full year. Over both intervals, nearly all the growth took place at the fifty large institutions.

The increase of 4.7 percent in securities and money market assets was largely attributable to a large foreign-owned securities-oriented firm (Barclay's Group US, Inc.) with total assets of $180.7 billion becoming a bank holding company in the fourth quarter. This event coincided with the exit of a smaller foreign-owned securities-oriented firm (CIBC Delaware Holdings, Inc., with $37.4 billion in assets) that ceased being a bank holding company with the sale during the period of its U.S. bank subsidiary. The entering firm had a larger trading portfolio ($42.0 billion) and much larger holdings of short-term money market assets ($90.0 billion), contributing considerably to aggregate growth. These effects aside, the fifty large bank holding companies added $30.6 billion (1.0 percent) to their holdings of securities and money market assets, while all other bank holding companies added $7.4 billion (1.6 percent).

Deposits increased significantly but less rapidly than assets, growing $186.2 billion (3.7 percent). Core deposits rose over the quarter, but large-denomination time deposits increased more sharply. Borrowings increased $76.8 billion (2.5 percent) overall, also influenced by developments at a few firms. The addition of the large securities-oriented bank holding company (and exit of a smaller one) added $58.3 billion, and increased borrowing at a large insurance-oriented bank holding company (MetLife) added $35.4 billion. Similarly, the aforementioned change in the population of reporting bank holding companies was the primary reason that other liabilities increased $94.2 billion. Risk-based regulatory capital ratios remained steady over the quarter. Although the leverage ratio declined 12 basis points, to 6.64 percent, all three regulatory capital ratios remained considerably above the standards for well-capitalized companies.

Net income fell off modestly in the fourth quarter, declining 1.4 percent from the previous quarter, to $28.8 billion. Net interest income fell despite the increases in loans and other interest-earning assets, as a flatter yield curve and heightened competitive pressure in loan pricing eroded net interest margins to 3.26 percent (down 0.21 percent). Non-interest expense rose a modest 1.0 percent, even including expenses related to 2004's many mergers. Cushioning the negative factors, non-interest income rose 1.2 percent (reflecting better trading and mortgage-servicing revenues), and provisions for loan losses declined 2 percent.[1]

Asset quality improved yet again in the quarter as nonperforming assets fell to 0.82 percent of loans and related assets. Despite the decline in provisions, improved asset quality allowed reporting bank holding companies to reduce their allowance for loan losses by a further $1.3 billion.

For the full year, net income of reporting bank holding companies reached $113.5 billion, an increase of 5.1 percent over 2003 despite an 11-basis-point narrowing of net interest margins. Return on average assets and return on average equity declined somewhat, reflecting robust asset growth and merger-related expansion of stockholder's equity respectively.

1. To better reflect the components of net income, the accompanying tables have been adjusted so that non-interest income no longer includes realized gains and losses on securities.

1. Financial characteristics of all reporting bank holding companies in the United States

Millions of dollars except as noted, not seasonally adjusted

Account or ratio[1, 2]	2000	2001	2002	2003	2004	2003			2004			
						Q2	Q3	Q4	Q1	Q2	Q3	Q4
Balance sheet												
Total assets	**6,745,836**	**7,486,952**	**7,990,945**	**8,880,545**	**10,339,429**	**8,726,133**	**8,751,183**	**8,880,545**	**9,348,190**	**9,699,421**	**9,946,162**	**10,339,429**
Loans	3,728,570	3,832,553	4,080,049	4,435,863	5,111,690	4,301,114	4,376,319	4,435,863	4,606,523	4,792,622	4,937,021	5,111,690
Securities and money market	2,197,434	2,568,705	2,866,857	3,302,240	3,850,580	3,230,018	3,190,602	3,302,240	3,592,416	3,628,469	3,678,595	3,850,580
Allowance for loan losses	-60,376	-68,833	-74,798	-73,835	-74,610	-74,627	-73,926	-73,835	-76,617	-76,398	-75,902	-74,610
Other	880,209	1,154,528	1,118,837	1,216,278	1,451,770	1,269,628	1,258,189	1,216,278	1,225,867	1,354,729	1,406,448	1,451,770
Total liabilities	**6,227,975**	**6,901,281**	**7,350,200**	**8,177,562**	**9,450,301**	**8,046,202**	**8,063,922**	**8,177,562**	**8,603,836**	**8,925,650**	**9,093,036**	**9,450,301**
Deposits	3,771,749	4,025,769	4,357,245	4,705,043	5,249,255	4,599,696	4,605,545	4,705,043	4,846,062	5,003,107	5,063,083	5,249,255
Borrowings	1,991,564	2,073,770	2,244,331	2,630,168	3,091,158	2,525,842	2,572,084	2,630,168	2,867,443	2,917,437	3,014,311	3,091,158
Other[3]	464,662	801,743	748,624	842,351	1,109,889	920,664	886,293	842,351	890,331	1,005,107	1,015,641	1,109,889
Total equity	**517,861**	**585,671**	**640,745**	**702,983**	**889,128**	**679,932**	**687,261**	**702,983**	**744,354**	**773,771**	**853,126**	**889,128**
Off-balance-sheet												
Unused commitments to lend[4]	3,297,511	3,481,744	3,650,669	4,097,531	4,823,303	3,756,486	3,887,357	4,097,531	4,350,930	4,420,733	4,569,881	4,823,303
Securitizations outstanding[5]	n.a.	276,717	295,001	298,348	353,978	285,286	290,328	298,348	308,543	314,258	313,436	353,978
Derivatives (notional value, billions)[6]	43,608	48,276	57,886	72,914	89,124	68,353	69,452	72,914	79,271	83,107	84,721	89,124
Income statement												
Net income[7]	73,168	66,510	85,731	107,950	113,497	26,983	28,177	29,545	30,826	25,808	29,186	28,767
Net interest income	197,759	224,535	246,048	257,537	286,253	64,685	66,120	68,072	68,769	73,217	73,755	72,246
Provisions for loan losses	27,699	40,758	45,107	33,075	28,784	9,197	8,246	8,944	7,163	6,989	7,489	7,846
Non-interest income	200,903	219,016	221,532	250,639	273,524	64,372	65,423	69,991	68,023	73,195	67,714	68,549
Non-interest expense	258,213	302,146	296,964	316,330	364,862	79,972	81,678	86,323	84,262	102,042	90,373	91,263
Security gains or losses	-606	4,352	4,598	5,771	5,524	2,694	596	655	1,987	997	1,960	508
Ratios (percent)												
Return on average equity	15.19	11.86	14.11	16.28	14.27	16.37	16.81	17.25	17.13	13.47	14.06	13.31
Return on average assets	1.13	.91	1.11	1.26	1.16	1.27	1.29	1.34	1.34	1.06	1.18	1.11
Net interest margin[8]	3.58	3.61	3.74	3.51	3.41	3.56	3.53	3.59	3.46	3.52	3.47	3.26
Efficiency ratio[7]	62.77	66.03	62.50	61.67	62.60	62.36	61.91	62.33	61.69	62.11	63.54	64.21
Nonperforming assets to loans and related assets	1.09	1.44	1.44	1.15	.82	1.33	1.23	1.15	1.09	.97	.89	.82
Net charge-offs to average loans	.66	.91	1.04	.84	.67	.88	.86	.98	.72	.66	.61	.71
Loans to deposits	98.86	95.20	93.64	94.28	97.38	93.51	95.02	94.28	95.06	95.79	97.51	97.38
Regulatory capital ratios												
Tier 1 risk-based	8.84	8.92	9.22	9.58	9.41	9.31	9.53	9.58	9.53	9.38	9.40	9.41
Total risk-based	11.80	11.92	12.28	12.60	12.28	12.32	12.54	12.60	12.48	12.28	12.30	12.28
Leverage	6.81	6.68	6.72	6.87	6.64	6.79	6.77	6.87	6.88	6.67	6.76	6.64
Number of reporting bank holding companies	1,727	1,842	1,979	2,134	2,253	2,064	2,120	2,134	2,192	2,210	2,240	2,253

Footnotes appear on p. 240.

2. Financial characteristics of fifty large bank holding companies in the United States

Millions of dollars except as noted, not seasonally adjusted

Account or ratio[2, 9]	2000	2001	2002	2003	2004	2003			2004			
						Q2	Q3	Q4	Q1	Q2	Q3	Q4
Balance sheet												
Total assets	**5,507,787**	**5,882,246**	**6,243,212**	**6,901,577**	**7,940,955**	**6,806,767**	**6,825,187**	**6,901,577**	**7,338,392**	**7,528,335**	**7,726,752**	**7,940,955**
Loans	2,934,979	2,953,665	3,136,678	3,381,963	3,925,111	3,290,399	3,348,415	3,381,963	3,534,690	3,668,300	3,772,804	3,925,111
Securities and money market	1,849,888	2,054,945	2,285,222	2,633,690	2,968,226	2,567,101	2,538,590	2,633,690	2,910,826	2,895,327	2,937,667	2,968,226
Allowance for loan losses	–49,186	–56,512	–61,091	–59,233	–59,380	–60,138	–59,235	–59,233	–61,757	–61,338	–60,692	–59,380
Other	772,107	930,150	882,404	945,157	1,106,999	1,009,406	997,418	945,157	954,633	1,026,046	1,076,974	1,106,999
Total liabilities	**5,096,893**	**5,433,581**	**5,756,182**	**6,370,790**	**7,251,931**	**6,294,212**	**6,304,621**	**6,370,790**	**6,770,661**	**6,938,022**	**7,069,330**	**7,251,931**
Deposits	2,845,631	3,021,096	3,257,657	3,508,261	3,942,375	3,435,534	3,431,483	3,508,261	3,624,929	3,754,261	3,787,308	3,942,375
Borrowings	1,813,934	1,878,921	2,042,479	2,360,766	2,721,165	2,267,749	2,316,577	2,360,766	2,610,435	2,637,680	2,735,250	2,721,165
Other[3]	437,329	533,564	456,046	501,764	588,392	590,929	556,561	501,764	535,297	546,082	546,772	588,392
Total equity	**410,894**	**448,665**	**487,030**	**530,787**	**689,025**	**512,555**	**520,567**	**530,787**	**567,731**	**590,313**	**657,423**	**689,025**
Off-balance-sheet												
Unused commitments to lend[4]	3,075,664	3,238,472	3,386,455	3,802,454	4,489,800	3,470,355	3,594,931	3,802,454	4,049,808	4,106,493	4,240,809	4,489,800
Securitizations outstanding[5]	n.a.	271,825	289,320	292,312	348,986	279,083	284,134	292,312	304,545	307,878	307,325	348,986
Derivatives (notional value, billions)[6]	43,559	48,195	57,801	72,750	88,744	68,213	69,308	72,750	79,090	82,887	84,512	88,744
Income statement												
Net income[7]	60,436	52,619	68,451	87,857	90,492	21,760	23,169	24,498	25,364	19,490	23,171	23,557
Net interest income	153,462	166,608	183,719	192,171	213,810	48,327	49,963	51,206	51,864	54,023	55,177	54,478
Provisions for loan losses	24,108	35,852	39,380	28,563	25,338	8,010	7,070	7,871	6,394	6,205	6,698	6,744
Non-interest income	181,707	174,504	172,705	195,908	213,393	50,465	51,758	55,618	54,154	56,152	52,088	54,954
Non-interest expense	216,969	224,451	215,807	229,270	267,909	58,241	60,254	63,204	61,979	75,404	65,503	68,101
Security gains or losses	–601	4,316	5,008	5,190	4,634	2,349	483	632	1,636	677	1,707	541
Ratios (percent)												
Return on average equity	15.86	12.24	14.72	17.52	14.77	17.52	18.27	18.88	18.43	13.31	14.42	14.02
Return on average assets	1.14	.92	1.13	1.32	1.19	1.32	1.35	1.43	1.40	1.03	1.20	1.19
Net interest margin[8]	3.44	3.39	3.56	3.35	3.25	3.40	3.40	3.47	3.31	3.32	3.32	3.16
Efficiency ratio[7]	62.67	63.43	59.65	58.59	59.51	59.29	59.03	58.97	58.72	58.27	60.50	61.60
Nonperforming assets to loans and related assets	1.17	1.57	1.56	1.22	.84	1.41	1.30	1.22	1.14	1.00	.91	.84
Net charge-offs to average loans	.75	1.04	1.21	.97	.80	1.04	1.00	1.13	.88	.78	.72	.83
Loans to deposits	103.14	97.77	96.29	96.40	99.56	95.78	97.58	96.40	97.51	97.71	99.62	99.56
Regulatory capital ratios												
Tier 1 risk-based	8.21	8.24	8.52	8.83	8.59	8.57	8.83	8.83	8.79	8.64	8.64	8.59
Total risk-based	11.46	11.59	11.95	12.20	11.85	11.93	12.19	12.20	12.06	11.89	11.86	11.85
Leverage	6.43	6.25	6.26	6.38	6.17	6.31	6.30	6.38	6.38	6.15	6.24	6.17

Footnotes appear on p. 240.

3. Financial characteristics of all other reporting bank holding companies in the United States

Millions of dollars except as noted, not seasonally adjusted

Account[1, 10]	2000	2001	2002	2003	2004	2003 Q2	2003 Q3	2003 Q4	2004 Q1	2004 Q2	2004 Q3	2004 Q4
Balance sheet												
Total assets	**1,179,815**	**1,291,472**	**1,415,874**	**1,551,826**	**1,708,712**	**1,511,952**	**1,518,413**	**1,551,826**	**1,589,816**	**1,634,419**	**1,674,192**	**1,708,712**
Loans	769,242	824,735	889,216	974,580	1,104,277	936,117	950,786	974,580	1,001,254	1,039,136	1,076,582	1,104,277
Securities and money market	319,020	357,476	406,422	444,967	466,243	448,650	439,584	444,967	459,839	457,512	458,796	466,243
Allowance for loan losses	−10,922	−11,957	−13,269	−14,185	−14,830	−13,957	−14,206	−14,185	−14,475	−14,718	−14,915	−14,830
Other	102,476	121,218	133,505	146,464	153,022	141,141	142,249	146,464	143,199	152,489	153,729	153,022
Total liabilities	**1,078,257**	**1,175,659**	**1,285,653**	**1,410,440**	**1,551,059**	**1,372,657**	**1,379,967**	**1,410,440**	**1,444,354**	**1,489,548**	**1,519,841**	**1,551,059**
Deposits	914,290	990,558	1,081,607	1,174,218	1,286,968	1,143,286	1,152,364	1,174,218	1,207,152	1,233,046	1,259,508	1,286,968
Borrowings	143,028	159,229	172,810	201,634	223,481	194,844	194,470	201,634	197,959	218,586	220,193	223,481
Other[3]	20,939	25,873	31,237	34,589	40,609	34,528	33,133	34,589	39,244	37,916	40,140	40,609
Total equity	**101,558**	**115,813**	**130,221**	**141,385**	**157,653**	**139,294**	**138,446**	**141,385**	**145,462**	**144,870**	**154,351**	**157,653**
Off-balance-sheet												
Unused commitments to lend[4]	212,784	233,098	252,308	282,164	320,132	273,591	278,701	282,164	287,740	299,222	311,754	320,132
Securitizations outstanding[5]	n.a.	4,567	4,942	4,893	2,877	5,205	5,116	4,893	2,875	3,000	2,757	2,877
Derivatives (notional value, billions)[6]	32	51	53	67	79	74	67	67	71	65	67	79
Income statement												
Net income[7]	12,436	13,752	16,492	17,692	19,340	4,633	4,506	4,144	4,770	4,763	4,956	4,851
Net interest income	43,566	46,324	51,106	53,266	57,492	13,295	13,207	13,665	13,888	14,026	14,582	14,996
Provisions for loan losses	3,420	4,469	5,094	4,295	3,215	1,098	1,056	1,133	804	792	805	814
Non-interest income	16,090	22,339	24,528	27,514	26,392	7,282	6,944	6,679	6,700	6,620	6,530	6,542
Non-interest expense	38,132	44,446	47,066	51,551	53,647	12,995	12,735	13,461	13,178	13,157	13,347	13,965
Security gains or losses	−10	745	670	989	552	400	131	187	291	117	129	15
Ratios (percent)												
Return on average equity	13.09	12.50	13.47	13.00	13.08	13.59	13.24	11.91	13.44	13.14	13.27	12.51
Return on average assets	1.11	1.12	1.23	1.19	1.19	1.25	1.20	1.08	1.22	1.19	1.20	1.15
Net interest margin[8]	4.32	4.21	4.26	4.00	3.94	4.02	3.93	3.98	3.98	3.90	3.93	3.96
Efficiency ratio[7]	62.27	63.86	61.26	63.10	62.85	63.69	62.84	65.98	63.19	63.11	63.15	63.88
Nonperforming assets to loans and related assets	.77	.97	1.02	.98	.77	1.09	1.03	.98	.96	.87	.85	.77
Net charge-offs to average loans	.32	.43	.46	.39	.25	.37	.36	.51	.22	.25	.23	.31
Loans to deposits	84.14	83.26	82.21	83.00	85.80	81.88	82.51	83.00	82.94	84.27	85.48	85.80
Regulatory capital ratios												
Tier 1 risk-based	11.76	12.18	12.42	12.47	12.35	12.51	12.46	12.47	12.51	12.38	12.36	12.35
Total risk-based	13.24	13.76	14.06	14.20	14.01	14.21	14.18	14.20	14.23	14.08	14.03	14.01
Leverage	8.49	8.76	8.87	8.99	9.11	8.93	8.91	8.99	9.04	9.05	9.09	9.11
Number of other reporting bank holding companies	1,652	1,779	1,916	2,071	2,198	2,001	2,057	2,071	2,130	2,148	2,182	2,198

Footnotes appear on p. 240.

4. Nonfinancial characteristics of all reporting bank holding companies in the United States

Millions of dollars except as noted, not seasonally adjusted

Account	2000	2001	2002	2003	2004	2003 Q2	2003 Q3	2003 Q4	2004 Q1	2004 Q2	2004 Q3	2004 Q4
Bank holding companies that qualify as financial holding companies [11, 12]												
Domestic												
Number	300	389	435	452	474	441	449	452	465	471	477	474
Total assets	4,497,781	5,440,842	5,921,277	6,610,312	7,462,510	6,438,319	6,451,785	6,610,312	6,845,700	7,069,908	7,264,913	7,462,510
Foreign-owned [13]												
Number	9	10	11	12	14	11	11	12	13	14	14	14
Total assets	502,506	621,442	616,254	710,441	1,376,325	732,695	729,244	710,441	995,454	1,117,732	1,194,542	1,376,325
Total U.S. commercial bank assets [14]	**6,129,534**	**6,415,909**	**6,897,447**	**7,397,818**	**8,207,170**	**7,325,350**	**7,293,920**	**7,397,818**	**7,614,504**	**7,850,644**	**8,040,967**	**8,207,170**
By ownership												
Reporting bank holding companies	5,657,210	5,942,575	6,429,738	6,940,992	7,785,424	6,863,154	6,842,727	6,940,992	7,165,651	7,409,186	7,599,384	7,785,424
Other bank holding companies	229,274	230,464	227,017	219,222	209,251	222,998	217,035	219,222	213,193	211,725	208,764	209,251
Independent banks	243,050	242,870	240,692	237,604	212,495	239,198	234,157	237,604	235,660	229,733	232,819	212,495
Assets associated with nonbanking activities [12, 15]												
Insurance	n.a.	426,462	372,405	437,503	579,113	405,297	419,575	437,503	468,168	583,073	579,785	579,113
Securities broker–dealers	n.a.	n.a.	630,851	656,775	719,242	659,701	686,049	656,775	713,794	710,485	756,869	719,242
Thrift institutions	102,218	91,170	107,422	133,056	191,201	124,640	143,578	133,056	139,713	156,033	162,396	191,201
Foreign nonbank institutions	132,629	138,977	145,344	170,600	216,758	160,515	162,789	170,600	195,472	226,055	230,566	216,758
Other nonbank institutions	1,234,714	1,674,267	561,712	686,367	1,128,279	737,434	736,515	686,367	837,269	861,333	873,677	1,128,279
Number of bank holding companies engaged in nonbanking activities [12, 15]												
Insurance	n.a.	143	96	102	99	93	102	102	100	101	98	99
Securities broker–dealers	n.a.	n.a.	47	50	43	50	46	50	49	48	45	43
Thrift institutions	50	38	32	27	27	31	29	27	29	27	25	27
Foreign nonbank institutions	25	32	37	41	39	40	39	41	41	40	40	39
Other nonbank institutions	633	743	880	1,042	1,031	945	992	1,042	1,009	1,030	1,049	1,031
Foreign-owned bank holding companies [13]												
Number	21	23	26	27	29	27	27	27	27	28	28	29
Total assets	636,669	764,411	762,901	934,088	1,537,203	946,847	947,254	934,088	1,146,258	1,271,844	1,350,458	1,537,203
Employees of reporting bank holding companies (full-time equivalent)	1,859,930	1,985,981	1,992,559	2,034,358	2,162,036	2,019,953	2,031,029	2,034,358	2,099,072	2,085,671	2,133,267	2,162,036
Assets of fifty large bank holding companies [9, 17]												
Fixed panel (from table 2)	5,507,787	5,882,246	6,243,212	6,901,577	7,940,955	6,806,767	6,825,187	6,901,577	7,338,392	7,528,335	7,726,752	7,940,955
Fifty large as of reporting date	5,319,129	5,732,621	6,032,000	6,666,488	7,940,955	6,587,000	6,602,255	6,666,488	7,045,844	7,385,384	7,644,504	7,940,955
Percent of all reporting bank holding companies	78.90	76.60	75.50	75.10	76.80	75.50	75.40	75.10	75.40	76.10	76.90	76.80

NOTE. All data are as of the most recent period shown. The historical figures may not match those in earlier versions of this table because of mergers, significant acquisitions or divestitures, or revisions or restatements to bank holding company financial reports. Data for the most recent period may not include all late-filing institutions.

1. Covers top-tier bank holding companies except (1) those with consolidated assets of less than $150 million and with only one subsidiary bank and (2) multibank holding companies with consolidated assets of less than $150 million, with no debt outstanding to the general public and not engaged in certain nonbanking activities.

2. Data for all reporting bank holding companies and the fifty large bank holding companies reflect merger adjustments to the fifty large bank holding companies. Merger adjustments account for mergers, acquisitions, other business combinations and large divestitures that occurred during the time period covered in the tables so that the historical information on each of the fifty underlying institutions depicts, to the greatest extent possible, the institutions as they exist in the most recent period. In general, adjustments for mergers among bank holding companies reflect the combination of historical data from predecessor bank holding companies.

The data for the fifty large bank holding companies have also been adjusted as necessary to match the historical figures in each company's most recently available financial statement.

In general, the data are not adjusted for changes in generally accepted accounting principles.

3. Includes minority interests in consolidated subsidiaries.

4. Includes credit card lines of credit as well as commercial lines of credit.

5. Includes loans sold to securitization vehicles in which bank holding companies retain some interest, whether through recourse or seller-provided credit enhancements or by servicing the underlying assets. Securitization data were first collected on the FR Y-9C report for June 2001.

6. The notional value of a derivative is the reference amount of an asset on which an interest rate or price differential is calculated. The total notional value of a bank holding company's derivatives holdings is the sum of the notional values of each derivative contract regardless of whether the bank holding company is a payor or recipient of payments under the contract. The actual cash flows and fair market values associated with these derivative contracts are generally only a small fraction of the contract's notional value.

7. Income statement subtotals for all reporting bank holding companies and the fifty large bank holding companies exclude extraordinary items, the cumulative effects of changes in accounting principles, and discontinued operations at the fifty large institutions and therefore will not sum to Net income. The efficiency ratio is calculated excluding nonrecurring income and expenses.

8. Calculated on a fully-taxable-equivalent basis.

9. In general, the fifty large bank holding companies are the fifty largest bank holding companies as measured by total consolidated assets for the latest period shown. Excludes a few large bank holding companies whose commercial banking operations account for only a small portion of assets and earnings.

10. Excludes predecessor bank holding companies that were subsequently merged into other bank holding companies in the panel of fifty large bank holding companies. Also excludes those bank holding companies excluded from the panel of fifty large bank holding companies because commercial banking operations represent only a small part of their consolidated operations.

11. Exclude qualifying institutions that are not reporting bank holding companies.

12. No data related to financial holding companies and only some data on nonbanking activities were collected on the FR Y-9C report before implementation of the Gramm–Leach–Bliley Act in 2000.

13. A bank holding company is considered "foreign-owned" if it is majority-owned by a foreign entity. Data for foreign-owned companies do not include data for branches and agencies of foreign banks operating in the United States.

14. Total assets of insured commercial banks in the United States as reported in the commercial bank Call Report (FFIEC 031 or 041, Reports of Condition and Income). Excludes data for a small number of commercial banks owned by other commercial banks that file separate call reports yet are also covered by the reports filed by their parent banks. Also excludes data for mutual savings banks.

15. Data for thrift, foreign nonbank, and other nonbank institutions are total assets of each type of subsidiary as reported in the FR Y-9LP report. Data cover those subsidiaries in which the top-tier bank holding company directly or indirectly owns or controls more than 50 percent of the outstanding voting stock and that has been consolidated using generally accepted accounting principles. Data for securities broker–dealers are net assets (that is, total assets, excluding intercompany transactions) of broker–dealer subsidiaries engaged in activities pursuant to the Gramm–Leach–Bliley Act, as reported on schedule HC-M of the FR Y-9C report. Data for insurance activities are all insurance-related assets held by the bank holding company as reported on schedule HC-I of the FR Y-9C report.

Beginning in 2002:Q1, insurance totals exclude intercompany transactions and subsidiaries engaged in credit-related insurance or those engaged principally in insurance agency activities. Beginning in 2002:Q2, insurance totals include only newly authorized insurance activities under the Gramm–Leach–Bliley Act.

16. Aggregate assets of thrift subsidiaries were affected significantly by the conversion of Charter One's thrift subsidiary (with assets of $37 billion) to a commercial bank in the second quarter of 2002 and the acquisition by Citigroup of Golden State Bancorp (a thrift institution with assets of $55 billion) in the fourth quarter of 2002.

17. Changes over time in the total assets of the time-varying panel of fifty large bank holding companies are attributable to (1) changes in the companies that make up the panel and (2) to a small extent, restatements of financial reports between periods.

n.a. Not available

SOURCE. Federal Reserve Reports FRY-9C and FR Y-9LP, Federal Reserve National Information Center, and published financial reports.

Announcements

FEDERAL OPEN MARKET COMMITTEE STATEMENTS

The Federal Open Market Committee decided on February 2, 2005, to raise its target for the federal funds rate 25 basis points, to 2½ percent.

The Committee believes that, even after this action, the stance of monetary policy remains accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity. Output appears to be growing at a moderate pace despite the rise in energy prices, and labor market conditions continue to improve gradually. Inflation and longer-term inflation expectations remain well contained.

The Committee perceives the upside and downside risks to the attainment of both sustainable growth and price stability for the next few quarters to be roughly equal. With underlying inflation expected to be relatively low, the Committee believes that policy accommodation can be removed at a pace that is likely to be measured. Nonetheless, the Committee will respond to changes in economic prospects as needed to fulfill its obligation to maintain price stability.

Voting for the FOMC monetary policy action were: Alan Greenspan, Chairman; Timothy F. Geithner, Vice Chairman; Ben S. Bernanke; Susan S. Bies; Roger W. Ferguson, Jr.; Edward M. Gramlich; Jack Guynn; Donald L. Kohn; Michael H. Moskow; Mark W. Olson; Anthony M. Santomero; and Gary H. Stern.

In a related action, the Board of Governors unanimously approved a 25-basis-point increase in the discount rate, to 3½ percent. In taking this action, the Board approved the requests submitted by the Boards of Directors of the Federal Reserve Banks of Boston, New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco.

The Federal Open Market Committee decided on March 22, 2005, to raise its target for the federal funds rate 25 basis points, to 2¾ percent.

The Committee believes that, even after this action, the stance of monetary policy remains accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity. Output evidently continues to grow at a solid pace despite the rise in energy prices, and labor market conditions continue to improve gradually. Though longer-term inflation expectations remain well contained, pressures on inflation have picked up in recent months and pricing power is more evident. The rise in energy prices, however, has not notably fed through to core consumer prices.

The Committee perceives that, with appropriate monetary policy action, the upside and downside risks to the attainment of both sustainable growth and price stability should be kept roughly equal. With underlying inflation expected to be contained, the Committee believes that policy accommodation can be removed at a pace that is likely to be measured. Nonetheless, the Committee will respond to changes in economic prospects as needed to fulfill its obligation to maintain price stability.

Voting for the FOMC monetary policy action were: Alan Greenspan, Chairman; Timothy F. Geithner, Vice Chairman; Ben S. Bernanke; Susan S. Bies; Roger W. Ferguson, Jr.; Edward M. Gramlich; Jack Guynn; Donald L. Kohn; Michael H. Moskow; Mark W. Olson; Anthony M. Santomero; and Gary H. Stern.

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AMENDMENTS TO REGULATION CC, APPENDIX A

The Federal Reserve Board announced on February 8, 2005, amendments to appendix A of Regulation CC (Availability of Funds and Collection of Checks) that reflect the restructuring of the Federal Reserve's check-processing operations in the Sixth District. These amendments are the first in a series of amendments to appendix A that will take place through the first quarter of 2006, associated with the previously announced restructuring of the Reserve Banks' check-processing operations.

Appendix A provides a routing number guide that helps depository institutions determine the maximum permissible hold periods for most deposited checks. As of March 26, 2005, the Birmingham Branch office of the Federal Reserve Bank of Atlanta no longer processes checks, and banks served by that office have been reassigned to the Reserve Bank's head office in Atlanta. To ensure that the information in appendix A accurately describes the structure of check-processing operations within the Federal Reserve System, the final rule deletes the reference in appendix A to the Atlanta Reserve Bank's Birmingham Branch office and reassigns the routing numbers listed thereunder to the Reserve Bank's head office. To coincide with the effective date of the underlying check-processing changes, the amendments became effective March 26, 2005. As a result of these changes, some checks deposited in the affected regions that were nonlocal checks became local checks subject to shorter permissible hold periods.

The Federal Reserve Board announced on February 17, 2005, amendments to appendix A of Regulation CC that reflect the restructuring of the Federal Reserve's check-processing operations in the Fourth, Seventh, and Eleventh Districts.

As of April 16, 2005, the Detroit Branch office of the Federal Reserve Bank of Chicago no longer processes checks, and banks served by that office have been reassigned to the head office of the Federal Reserve Bank of Cleveland. As of April 23, 2005, the Houston Branch office of the Federal Reserve Bank of Dallas no longer processes checks, and banks served by that office have been reassigned to that Reserve Bank's head office. To ensure that the information in appendix A accurately describes the structure of check-processing operations within the Federal Reserve System, the final rule (1) deletes the reference in appendix A to the Chicago Reserve Bank's Detroit Branch office and reassigns the routing numbers listed thereunder to the Cleveland Reserve Bank's head office, and (2) deletes the reference in appendix A to the Dallas Reserve Bank's Houston Branch office and reassigns the routing numbers listed thereunder to that Reserve Bank's head office. To coincide with the effective date of the underlying check-processing changes, the amendments became effective April 16, 2005, and April 23, 2005, respectively. As a result of these changes, some checks deposited in the affected regions that were nonlocal checks became local checks subject to shorter permissible hold periods.

Request for Comments on Proposed Revisions to Regulations Implementing the Community Reinvestment Act

The Federal Reserve Board invited public comment on February 25, 2005, on proposed revisions to its regulations implementing the Community Reinvestment Act (CRA) that are intended to reduce regulatory burden on community banks while making CRA evaluations more effective in encouraging banks to meet community development needs.

The Board's notice of proposed rulemaking is identical to proposals approved by the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation on February 22, 2005. The proposal would introduce the following:

- Exempt banks with assets between $250 million and $1 billion, referred to as *intermediate-small banks*, from the data reporting obligations the current CRA regulations imposed on banks with assets larger than $250 million.

- Subject intermediate small banks to a two-part test (retail lending and community development) instead of the current three-part test (lending, investment, and service). For intermediate-small banks, a satisfactory community development rating, as well as a satisfactory retail lending rating, would be necessary for an overall rating of "satisfactory."

- Revise the definition of *community development* for all banks of any size to make it more responsive to the community development needs of rural areas.

- Clarify when illegal lending practices—for example, by a bank's affiliate—might reduce the bank's CRA rating.

The proposal addresses concerns expressed by the Board in July 2004 when it withdrew a February 2004 proposal to raise the small-bank threshold to $500 million. The Board expressed concern in July that the proposal was not certain to yield significant cost savings for banks, but might reduce community development capital in some rural communities. The current proposal would deliver greater cost savings while maintaining scrutiny of banks' community development records, though on a more flexible basis. The proposal would also refine the definition of *community development* in rural areas to make the regulations more effective in encouraging rural development.

Request for Comments on Proposal to Amend Regulation CC

The Federal Reserve Board requested public comment on March 1, 2005, on a proposal to amend its Regulation CC (Availability of Funds and Collection of Checks) to set forth rules governing remotely created checks. In place of a signature, a remotely created check generally bears a statement that the customer authorized the check or the check bears the customer's printed or typed name.

Remotely created checks can be useful payment devices. For example, a debtor can authorize a credit card company to create a remotely created check by telephone. This may enable the debtor to pay the credit card bill in a timely manner and avoid late charges. However, remotely created checks are vulnerable to fraud because they do not bear a signature or other readily verifiable indication that payment has been authorized.

To help reduce the potential for fraud, the proposed amendments to Regulation CC would create transfer and presentment warranties under which the depository bank would warrant that the remotely created check that it is transferring or presenting to the paying bank is authorized by the person on whose account the check is drawn. The proposed warranties would apply only to banks and would ultimately shift liability for losses attributable to an unauthorized remotely created check from the paying bank to the depository bank. These amendments would not affect the rights of checking account customers, as they are already not liable for unauthorized checks drawn on their accounts.

Adoption of Final Rule on Trust Preferred Securities

The Federal Reserve Board adopted on March 1, 2005, a final rule that allows the continued limited inclusion of trust preferred securities in the tier 1 capital of bank holding companies (BHCs). Under the final rule, trust preferred securities and other restricted core capital elements will be subject to stricter quantitative limits.

The Board's final rule limits restricted core capital elements to 25 percent of all core capital elements, net of goodwill less any associated deferred tax liability. Internationally active BHCs, defined as those with consolidated assets greater than $250 billion or on-balance-sheet foreign exposure greater than $10 billion, will be subject to a 15 percent limit. But they may include qualifying mandatory convertible preferred securities up to the generally applicable 25 percent limit. Amounts of restricted core capital elements in excess of these limits generally may be included in tier 2 capital. The final rule provides a five-year transition period, ending March 31, 2009, for application of the quantitative limits.

The requirement for trust preferred securities to include a call option has been eliminated, and standards for the junior subordinated debt underlying trust preferred securities eligible for tier 1 capital treatment have been clarified.

The final rule addresses supervisory concerns, competitive equity considerations, and the accounting for trust preferred securities. The final rule also strengthens the definition of regulatory capital by incorporating longstanding Board policies regarding the acceptable terms of capital instruments included in banking organizations' tier 1 or tier 2 capital.

Proposal to Discontinue Services for Definitive Municipal Securities

The Federal Reserve Board approved on February 28, 2005, the Federal Reserve Banks' proposal to stop providing services to depository institutions for the collection and processing of definitive municipal securities. The Reserve Banks will stop accepting deposits of bonds and coupons on September 30, 2005, and will complete the withdrawal from the noncash collection service on December 30, 2005.

Definitive municipal securities are registered or bearer bonds that have been issued by state and local governments with interest coupons in certificated or physical form. Municipal bond and coupon volume has been declining since the passage of the Tax Equity and Fiscal Responsibility Act of 1982, which effectively eliminated the issuance of municipal bearer bonds. The noncash collection service is provided centrally by the Jacksonville Branch of the Federal Reserve Bank of Atlanta and, in 2004, represented less than 0.2 percent of the Reserve Banks' total priced financial services costs.

The withdrawal from this service is prompted by the declining volume of definitive municipal securities, the Reserve Banks' expected underrecovery of costs for providing the service in future years, and the availability of reasonable private-sector alternatives. With the exit of the Reserve Banks, depository institution customers of the noncash collection service could instead use a private-sector service provider, such as the Depository Trust Company or a correspondent bank, to collect their definitive municipal bonds and coupons or could present these items for payment directly to the paying agent.

Passing of Henry Czerwinski, Former First Vice President, Kansas City Federal Reserve Bank

On February 11, 2005, Henry Czerwinski, Former First Vice President, Federal Reserve Bank of Kansas City, died as a result of a massive heart attack at his home in Nokomis, Florida. Former First Vice President Czerwinski joined the Bank in 1959 as an audit trainee and retired in 1994 after thirty-four years of service.

Implementation of Basel II Framework

The federal banking and thrift institution agencies released on January 27, 2005, an interagency statement on implementation of the Basel II framework and the qualification process for the framework's "advanced approaches."

Implementation of Web-Based Central Data Repository

The federal banking agencies announced on January 28, 2005, a new implementation plan for the Central Data Repository (CDR)—an Internet-based system created to modernize and streamline the ways that agencies collect, validate, manage, and distribute financial data submitted by banks in quarterly "Call Reports." Although banks will not be required to submit Call Report data to the CDR until October 2005, the agencies plan to make the CDR available for testing by banks and software vendors beginning early summer 2005.

Originally scheduled for implementation in October 2004, rollout of the CDR was postponed to address industry feedback and allow more time for system testing and enrollment. The new implementation plan resulted from discussions with industry representatives, including software vendors, trade associations, and a number of banks from across the country that participate in the Financial Institutions Focus Group for the CDR project. The new plan provides additional time for each group to participate in testing to help ensure a smooth integration of the new technology into the Call Reporting process.

Beginning this summer, the CDR will be made available to banks for enrollment and testing of their ability to access the system. Also, during this period, software vendors will be working with the agencies to prepare for the final test of system readiness in August 2005. Full system implementation, planned for October, will mark the first time all institutions will be required to file their Call Report data using the new CDR.

Through the use of new open data exchange standards (known as "eXtensible Business Reporting Language," or XBRL), the CDR system will facilitate faster delivery of accurate Call Report data. All users of the data—financial institutions, the public, and banking regulators—are expected to benefit from this improved, more timely flow of financial institution information.

This initiative—the Call Report Modernization Project—is an interagency effort under the auspices of the Federal Financial Institutions Examination Council (FFIEC). Additional project details and other important information are posted on the FFIEC's web site at www.FFIEC.gov/FIND.

Federal Reserve Board and FDIC Issue Enforcement Actions against The NorCrown Trust and Charles Kushner

The Federal Reserve Board and the Federal Deposit Insurance Corporation announced on February 10, 2005, the issuance of joint enforcement actions against The NorCrown Trust and Charles Kushner.

The NorCrown Trust controls NorCrown Bank, Livingston, New Jersey. Charles Kushner is the trustee of The NorCrown Trust and a former chairman of NorCrown Bank.

The joint order requires that The NorCrown Trust and Charles Kushner pay civil money penalties totaling at least $12.5 million, to divest The NorCrown Trust's shares of NorCrown Bank, and to transfer the shares to a voting trust administered by an independent trustee until the divestiture is completed. The joint order also prohibits Mr. Kushner from participating in the conduct of the affairs of any financial institution or holding company.

The Federal Reserve Board also issued an order upon consent under the Bank Holding Company Act requiring other individuals and trusts with relationships to The NorCrown Trust to cooperate in implementing the divestiture plan.

The enforcement actions resolve allegations that The NorCrown Trust and Charles Kushner violated the Change in Bank Control Act, the Bank Holding Company Act, or both, in a series of transactions from 1995 through 1997, that led to the formation of The NorCrown Trust, which never received the Federal Reserve's approval to become a bank holding company. The joint order also resolves allegations of violations of Regulation O (Loans to Executive Officers, Directors, and Principal Shareholders of Member Banks) and sections 23A and 23B of the Federal Reserve Act relating to transactions with NorCrown Bank.

Federal Reserve Board and FDIC Issue Written Agreement Associated with The NorCrown Trust

The Federal Reserve Board and the Federal Deposit Insurance Corporation announced on February 25, 2005, the execution of a joint written agreement by and among the Federal Reserve Bank of New York and the Federal Deposit Insurance Corporation with David Bodner and Murray Huberfeld. The written agreement requires that Mr. Bodner and Mr. Huberfeld comply with the prior approval requirements of section 19 of the Federal Deposit Insurance Act.

The agreement pertains to allegations that Mr. Bodner and Mr. Huberfeld did not seek the prior approval of the FDIC under section 19 of the Federal Deposit Insurance Act before an investment was made in what became The NorCrown Trust, an unregistered bank holding company that owns more than 99 percent of the voting shares of NorCrown Bank, Livingston, New Jersey, an insured state nonmember bank.

This joint written agreement follows joint enforcement actions announced on February 10, 2005, against The NorCrown Trust and Charles Kushner.

Comment Period Extended on Proposed Data Collection Changes for Shared National Credits

The federal banking and thrift institution regulatory agencies agreed on February 11, 2005, to extend the comment period for forty-five days on the proposed changes to the data collection process that supports the Shared National Credit review of large syndicated loans. The proposal was published in the *Federal Register* on December 20, 2004.

The deadline was extended in response to requests from several banks asking the agencies to provide an additional period to review, analyze, and submit comments on the proposed interagency statement.

The public comment period on the interagency statement ended on April 7, 2005. The scope and comment process for this interagency statement remained as stated in the original *Federal Register* notice of December 20, 2004.

Final Guidance Issued on Overdraft Protection Programs

The federal bank and credit union regulatory agencies announced on February 18, 2005, final joint guidance to assist insured depository institutions in the disclosure and administration of overdraft protection programs.

Depository institutions may offer overdraft protection programs to transaction account customers as an alternative to traditional ways of covering overdrafts. In response to concerns about the marketing, disclosure, and implementation of these programs, the agencies published for comment proposed interagency guidance on overdraft protection programs in June 2004. The final joint guidance responds to comments received by consumer and community groups, individual consumers, depository institutions, trade associations, vendors offering overdraft protection products, other industry representatives, and state agencies.

The final joint guidance contains three primary sections: Safety and Soundness Considerations; Legal Risks; and Best Practices. The Safety and Soundness discussion seeks to ensure that financial institutions offering overdraft protection programs adopt adequate policies and procedures to address credit, operational, and other associated risks.

The Legal Risks discussion alerts institutions of the need to comply with all applicable federal and state laws, and advises institutions to have their overdraft protection programs reviewed by legal counsel to ensure overall compliance before implementation. Several federal consumer compliance laws are outlined in the guidance.

The Best Practices section addresses the marketing and communications that accompany the offering of overdraft protection programs as well as the disclosure and operation of these programs. Some of these best practices include: avoiding the promotion of poor account management; providing a clear explanation of the discretionary nature of the overdraft protection program; clearly disclosing fees; explaining the effect of transaction clearing policies on the overdraft fees consumers may incur; and monitoring program usage. The agencies also advise insured depository institutions to distinguish overdraft protection services from "free" account features, to prominently distinguish balances from overdraft protection funds availability, and to alert consumers before a transaction triggers any fees.

The guidance is being issued by the Federal Reserve Board, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency and was published in the *Federal Register*. The joint document is on the Board's web site at www.federalreserve.gov/boarddocs/press/bcreg/2005/20050218/attachment.pdf.

ADVISORY ON CONFIDENTIALITY OF SUPERVISORY RATINGS

The federal banking and thrift institution regulatory agencies issued on February 28, 2005, an interagency advisory to remind financial institutions that they are prohibited by law from disclosing their CAMELS rating and other nonpublic supervisory information without permission from the appropriate federal banking agency.

The advisory is prompted by insurers who have requested or required banks and savings associations to disclose their CAMELS rating during the underwriting process for directors and officers liability coverage.

As a result of actions by insurers, the agencies have requested the assistance of the National Association of Insurance Commissioners in notifying insurance companies that the practice of requesting or requiring CAMELS ratings should be discontinued.

PROPOSED REVISIONS TO COMMUNITY REINVESTMENT ACT REGULATIONS

The federal banking agencies published on March 11, 2005, a joint notice of proposed rulemaking in the *Federal Register* that would revise certain provisions in their regulations implementing the Community Reinvestment Act (CRA).

The revisions are intended to reduce regulatory burden on community banks while making CRA evaluations more effective in encouraging banks to meet community development needs.

GUIDANCE ON RESPONSE PROGRAMS FOR SECURITY BREACHES

The federal banking and thrift institution regulatory agencies jointly issued on March 23, 2005, *Interagency Guidance on Response Programs for Unauthorized Access to Customer Information and Customer Notice.*

The guidance interprets the agencies' customer information security standards and states that financial institutions should implement a response program to address security breaches involving customer information.

The response program should include procedures to notify customers about incidents of unauthorized access to customer information that could result in substantial harm or inconvenience to the customer.

The guidance provides that "when a financial institution becomes aware of an incident of unauthorized access to sensitive customer information, the institution should conduct a reasonable investigation to promptly determine the likelihood that the information has been or will be misused."

"If the institution determines that misuse of its information about a customer has occurred or is reasonably possible, it should notify the affected customer as soon as possible," the guidance states. However, notice may be delayed if an appropriate law enforcement agency determines that notification will interfere with a criminal investigation.

Under the guidance, a financial institution should notify its primary federal regulator of a security breach involving sensitive customer information, whether or not the institution notifies its customers.

The guidance was issued by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision.

REQUEST FOR COMMENT ON PROPOSED CLASSIFICATION OF COMMERCIAL CREDIT EXPOSURES

The federal banking and thrift institution regulatory agencies requested comment on March 28, 2005, on proposed changes to the supervisory framework for the classification of commercial credit exposures.

The proposed guidance would replace the current commercial loan classification system categories—"special mention," "substandard," and "doubtful"—with a two-dimensional framework. The two-dimensional rating system has one dimension that measures the risk of the borrower defaulting (borrower rating) and a second focuses on the loss severity the institution would likely incur in the event of the borrower's default (facility rating). Facility ratings would be required for only those borrowers rated default, typically a very small proportion of all commercial exposures.

The proposed framework would increase consistency among the agencies in assessing the credit risk in an institution's commercial loan portfolio. It also more closely aligns the determination of a facility's accrual status with an institution's allowance for loan and lease loss methodology and rating assessment process.

Comments on the proposed guidance are requested by June 30, 2005. Specific information on how to file a comment is contained in the *Federal Register* notice.

Answers Released to Frequently Asked Questions about New HMDA Data

The federal banking, credit union, and thrift institution supervisory agencies, along with the Department of Housing and Urban Development, released on March 31, 2005, a set of "Answers to Frequently Asked Questions" (FAQs) that addresses the new home loan price data disclosed this year for the first time under the Home Mortgage Disclosure Act (HMDA).

This release coincides with the date that lenders must make their HMDA data available to the public upon request. The FAQs will aid users with their evaluation and interpretation of the data and will be posted on each of the agencies' web sites.

The new loan price data are intended to advance enforcement of consumer protection and anti-discrimination laws and improve mortgage market efficiency. Loan price data and other HMDA data can be used by the agencies and others as a screening tool to identify aspects of the higher-priced mortgage market that warrant a closer look to determine whether there is abuse or discrimination. Also, lenders, community groups, government agencies, and others can use the data to identify opportunities for private or public investment.

A full understanding of the data, including its limitations, will help ensure that the data are used effectively to advance the goals of HMDA. The data, for example, do not include certain determinants of credit risk that may explain higher loan prices, such as the borrower's credit history, loan-to-property-value ratio, and consumer debt-to-income ratio. Consequently, the HMDA data are not, by themselves, a basis for definitive conclusions regarding whether a lender discriminates unlawfully against particular borrowers or takes unfair advantage of them.

The FAQs are part of a larger effort by the Federal Reserve Board, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and the Department of Housing and Urban Development to promote the informed use of the 2004 data. The agencies will also engage in educational outreach to state and local agencies, trade associations, and consumer- and community-based organizations.

In September 2005 the Federal Financial Institutions Examination Council will release the annual summary statistical reports for each lender and an aggregate report for each Metropolitan Statistical Area. Concurrently, staff of the Federal Reserve Board will publish an article analyzing the 2004 data in the *Federal Reserve Bulletin*.

HMDA, which was enacted by the Congress in 1975, requires most mortgage lenders located in metropolitan areas to collect data about their housing-related lending activity, report the data annually to the government, and make the data publicly available. Initially, HMDA required reporting of the geographic location of originated and purchased home loans. In 1989 the Congress expanded HMDA data to include information about denied home loan applications and the race, sex, and income of applicants and borrowers. In 2002 the Federal Reserve Board amended the HMDA regulations to require lenders to report price data for certain higher-priced home mortgage loans, and other new data.

December 2004 Update to the *Bank Holding Company Supervision Manual*

The December 2004 update to the *Bank Holding Company Supervision Manual* has been published (supplement no. 27). The new supplement includes supervisory and BHC inspection guidance on the following subjects:

1. *Revised Uniform Agreement on the Classification of Assets and Appraisal of Securities Held by Banks and Thrift Institutions.* The section on the inspection reporting of consolidated classified and special-mention assets and other transfer-risk problems has been revised to incorporate this June 15, 2004, revised Uniform Agreement (the uniform agreement) that was jointly issued by the federal banking and thrift institution agencies. The uniform agreement sets forth the definitions of the classification categories and the specific examination procedures and information for classifying bank assets, including securities. The June 2004 revision did not change the classification of loans in the uniform agreement. The uniform agreement addresses, among other items, the treatment of rating differences, multiple security ratings, and split or partially rated securities. It also eliminates the automatic classification for sub-investment-grade debt securities. The uniform agreement's classification categories also apply to the classification of assets held by the subsidiaries of banks and bank holding companies. See SR letter 04–9.

2. *Tying Arrangements.* The section on "Tie-In Considerations of the BHC Act" has been revised to incorporate an August 18, 2003, Board interpretation and a February 2, 2004, Board staff interpretation on tying arrangements pertaining to section 106 of the Bank Holding Company Act Amendments of 1970 (section 106). These two interpretations state that bank customers that receive securities-based credit can be required to hold their pledged securities as collateral at an account of a bank holding company's or bank's broker–dealer affiliate. Section 106 generally prohibits a bank from conditioning the availability or price of one product or service (the *tying product*, or the *desired product*) on a requirement that a customer obtain another product or service (the *tied product*) from the bank or an affiliate of the bank.

3. *"Guidance on Accepting Accounts from Foreign Governments, Foreign Embassies, and Foreign Political Figures."* A new section *"Establishing Accounts for Foreign Governments, Embassies, and Political Futures"* conveys the June 15, 2004, interagency advisory that was issued by the federal bank and thrift institution agencies (agencies) and the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN). The advisory responds to inquiries the agencies and FinCEN received on whether financial institutions should do business and establish account relationships with those foreign customers cited in the advisory. Banking organizations are advised that the decision to accept or reject such a foreign-account is a decision they should make after considering the factors outlined in the advisory, including the institution's business objectives and its ability to manage the risk.

Financial institutions should be aware that there are varying degrees of risk associated with these accounts, depending on the customer and the nature of the services provided. Institutions should take appropriate steps to manage these risks, consistent with sound practices and applicable anti-money-laundering laws and regulations. This advisory is primarily directed to financial institutions located in the United States. The boards of directors of bank holding companies, however, should consider whether the advisory should be applied to their other U.S. subsidiaries' financial and other services. See SR letter 04–10.

4. *Risk-Based Capital Requirements for Asset-Backed Commercial Paper Programs.* The sections "Examiners' Guidelines for Assessing the Adequacy of Capital of BHCs" and "Credit-Supported and Asset-Backed Commercial Paper" have been updated to include the Board's July 17, 2004, approval (effective September 30, 2004) of its revisions to the risk-based capital requirements for asset-backed commercial paper (ABCP) programs sponsored by state member banks and bank holding companies (collectively, banking organizations). See appendix A of the Board's Regulation Y (12 CFR 225, appendix A).

Under the Board's revised risk-based capital rule, a banking organization that qualifies as a primary beneficiary and must consolidate an ABCP program that is defined as a variable interest entity under generally accepted accounting principles (see the Financial Accounting Standards Board's Interpretation FIN 46-R) may exclude the consolidated ABCP program's assets from risk-weighted assets, provided that it is the sponsor of the ABCP program. Such banking organizations must hold risk-based capital against any credit enhancement or liquidity facility that they provide to the ABCP program. In particular, a banking organization must hold risk-based capital against eligible ABCP liquidity facilities with an original maturity of one year or less that provide liquidity support to ABCP by applying a new 10 percent credit-conversion factor to such facilities. When calculating the banking organization's tier 1 and total capital, any associated minority interests must also be excluded from tier 1 and total capital. Certain inspection objectives and inspection procedures were also revised to incorporate this revised rule for ABCP programs.

5. *Providing Limited Fleet-Management Services to Nonleased Vehicles.* The section on "Leasing Personal or Real Property" has been revised to incorporate a Board staff legal opinion that was requested by a foreign banking organization (FBO) that is treated as a bank holding company (BHC). The FBO, as a BHC, engages in leasing activities that the Board has authorized in Regulation Y, section 225.28(b)(3) (12 CFR 225.28(b)(3)). The FBO asked if a BHC may provide, as an incidental nonbank activity, fleet-management services to some nonleased vehicles in accordance with its Regulation Y-authorized leasing activities. In a December 19, 2003, opinion, the Board stated that the provision of fleet-management services to some nonleased vehicles is an activity incidental to the BHC's authorized leasing activities, provided the BHC's leasing subsidiary limits its fleet-management services involving vehicles not subject to a Regulation Y permissible lease to no more than 15 percent of the fleet-management revenues, and to 5 percent of the total leasing revenues of the leasing subsidiary. See the December 19, 2003, Board staff opinion and Regulation Y, 12 CFR 225.28(b)(3), footnote 5.

A more detailed summary of changes is included with the update package. Copies of the new supplement were shipped directly by the publisher to the Reserve Banks for the distribution to examiners and other System staff members. The public may obtain the *Manual* and the updates (including pricing information) from Publications Fulfillment, Mail Stop 127, Board of Governors of the Federal Reserve System, 20th and C Streets, N.W., Washington, DC 20551; telephone (202) 452-3244; or send facsimile to (202) 728-5886. The *Manual* is also available on the Board's public web site at www.federalreserve.gov/boarddocs/supmanual/. The manual's next update will be issued with an effective date of July 2005. Thereafter, semiannual updates are planned.

IMPROVEMENTS TO THE FEDERAL RESERVE BOARD'S WEB SITE

The Federal Reserve Board announced on February 17, 2005, improvements to its web site to make the statistical releases and historical data easier to use.

The statistical releases are now grouped by subject area instead of frequency of release (for example, daily or weekly). The subject areas are principal economic indicators, bank asset quality, bank assets and liabilities, bank structure data, business finance, exchange rates and international data, flow of funds accounts, household finance, industrial activity, interest rates, and money stock and reserve balances. The redesigned page also now incorporates links to Board surveys, such as the Survey of Consumer Finances. The redesigned index is online at www.federalreserve.gov/releases/default.htm.

Since 1914 the Board has published statistical information on the U.S. economy and banking industry in various formats. Titles and numbers of the statistical releases have changed through the years. A new publication on the Board's web site, *The Federal Reserve Board Statistical Release Publications History*, can be used to trace these changes. The publications history is online at www.federalreserve.gov/releases/releasehistory/about.htm

POSTING OF INDUSTRIAL PRODUCTION AND CAPACITY UTILIZATION RELEASE (G.17)

The Federal Reserve Board's report on Industrial Production and Capacity Utilization (G.17) for March 2005, was inadvertently posted, as the result of human error, on the Board's public web site fifteen minutes before the release time of 9:15 a.m. EDT on April 15, 2005.

MEETING OF THE CONSUMER ADVISORY COUNCIL

The Federal Reserve Board announced on February 23, 2005, that the Consumer Advisory Council would hold its next meeting on Thursday, March 17, 2005. The meeting was held in Dining Room E, Terrace level, in the Board's Martin Building. The session began at 9:00 a.m. and was open to the public.

The Council's function is to advise the Board on the exercise of its responsibilities under various consumer financial services laws and on other matters on which the Board seeks its advice. Time permitting, the Council planned to discuss the following topics:

- Home Mortgage Disclosure Act Data
- Truth in Lending Act
- Community Reinvestment Act and Community Development
- Electronic Fund Transfer Act

MINUTES OF THE BOARD'S DISCOUNT RATE MEETINGS

The Federal Reserve Board released on March 2, 2005, the minutes of its discount rate meetings from January 3, 2005, through February 2, 2005.

APPROVALS OF DISCOUNT RATE ACTIONS

The Federal Reserve Board approved on March 23, 2005, an action by the Board of Directors of the Federal Reserve Bank of Kansas City increasing the discount rate at the Bank from 3½ percent to 3¾ percent, effective immediately.

The Federal Reserve Board approved on March 24, 2005, an action by the Board of Directors of the Federal Reserve Bank of Dallas increasing the discount rate at the Bank from 3½ percent to 3¾ percent, effective immediately.

ENFORCEMENT ACTIONS

The Federal Reserve Board and the Federal Deposit Insurance Corporation announced enforcement actions against The NorCrown Trust and other individuals on February 10, 2005, and February 25, 2005. The enforcement actions appear on pages 244–45.

The Federal Reserve Board announced on March 1, 2005, the issuance of a final decision and order of prohibition against Kenneth L. Coleman, a former employee of PNC Bank and Mellon Bank, N.A., both of Pittsburgh, Pennsylvania. The order, the result of an action brought by the Office of the Comptroller of the Currency, prohibits Mr. Coleman from participating in the conduct of the affairs of any financial institution or holding company.

Assessments of Civil Money Penalties

The Federal Reserve Board announced on March 16, 2005, the issuance of a consent order of assessment of a civil money penalty against the First Interstate Bank, Billings, Montana, a state member bank. First Interstate Bank, without admitting to any allegations, consented to the issuance of the order in connection with its alleged violations of the Board's Regulations implementing the National Flood Insurance Act.

The order requires First Interstate Bank to pay a civil money penalty of $15,750, which will be remitted to the Federal Emergency Management Agency for deposit into the National Flood Mitigation Fund.

The Federal Reserve Board announced on March 16, 2005, the issuance of a consent order of assessment of a civil money penalty against the HomeFederal Bank, Columbus, Indiana, a state member bank. HomeFederal Bank, without admitting to any allegations, consented to the issuance of the order in connection with its alleged violations of the Board's Regulations implementing the National Flood Insurance Act.

The order requires HomeFederal Bank to pay a civil money penalty of $57,250, which will be remitted to the Federal Emergency Management Agency for deposit into the National Flood Mitigation Fund.

The Federal Reserve Board announced on March 16, 2005, the issuance of a consent order of assessment of a civil money penalty against the Midwest Bankcentre, St. Louis, Missouri, a state member bank. Midwest Bankcentre, without admitting to any allegations, consented to the issuance of the order in connection with its alleged violations of the Board's Regulations implementing the National Flood Insurance Act.

The order requires Midwest Bankcentre to pay a civil money penalty of $2,450, which will be remitted to the Federal Emergency Management Agency for deposit into the National Flood Mitigation Fund.

Cease and Desist Orders

The Federal Reserve Board announced on January 27, 2005, the issuance of a consent order to cease and desist against Riggs National Corporation, Washington, D.C., a bank holding company. Riggs National Corporation, without admitting to any allegations, consented to the issuance of the order to address management, capital, and contingency planning matters.

The Federal Reserve Board simultaneously announced the termination of the May 14, 2004, consent order to cease and desist against Riggs National Corporation and Riggs International Banking Corporation, Miami, Florida, an Edge corporation. This action reflects the closing of the Edge corporation as of December 31, 2004.

In a separate, coordinated action, the Office of the Comptroller of the Currency announced on January 27, 2005, the modification of its consent order to cease and desist dated May 13, 2004, against Riggs Bank, N.A., McLean, Virginia.

In another action, Riggs Bank, N.A., pleaded guilty on January 27, 2005, to criminal violations of the Bank Secrecy Act relating to the bank's failure to timely and accurately report suspicious transactions.

The Federal Reserve Board announced on February 2, 2005, the issuance of a consent cease and desist order against Banco de Chile, Santiago, Chile, and Banco de Chile's Miami branch. The order addresses Bank Secrecy Act and anti-money-laundering compliance at Banco de Chile's Miami branch.

In a separate, coordinated action, the Office of the Comptroller of the Currency announced on February 2, 2005, the issuance of a consent order against Banco de Chile and Banco de Chile's New York branch.

The Federal Reserve Board announced on March 31, 2005, the issuance of a cease and desist order against Eagle National Holding Company, Doral, Florida, a registered bank holding company that owns and controls the Eagle National Bank of Miami, Doral, Florida.

Written Agreements

The Federal Reserve Board announced on January 28, 2005, the execution of a written agreement by and between the Asian Bank, Philadelphia, Pennsylvania, and the Federal Reserve Bank of Philadelphia.

The Federal Reserve Board announced on February 9, 2005, the execution of a written agreement by and between Bank of America Corporation, Charlotte, North Carolina, a bank holding company, and the Federal Reserve Bank of Richmond.

In separate, coordinated actions, the Office of the Comptroller of the Currency announced the execution of a formal agreement with Bank of America, N.A., Charlotte, North Carolina, a wholly owned subsidiary of Bank of America Corporation, and the U.S. Securities and Exchange Commission announced the execution of an administrative cease and desist order against Banc of America Capital Management, LLC, a registered investment adviser, BACAP Distributors, LLC, a registered investment adviser, and Banc of America Securities, LLC, a registered investment adviser and broker–dealer.

The Federal Reserve Board announced on March 1, 2005, the execution of a written agreement by and between Huntington Bancshares, Incorporated, Columbus, Ohio, a bank holding company, and the Federal Reserve Bank of Cleveland.

The written agreement addresses deficiencies relating to the company's corporate governance, internal audit, risk management, and internal controls over financial reporting, accounting policies and procedures, and regulatory reporting.

In a separate, coordinated action, the Office of the Comptroller of the Currency announced the execution of a formal agreement with Huntington National Bank, Columbus, Ohio, a wholly owned subsidiary of Huntington Bancshares, Incorporated.

Termination of Enforcement Actions

The Federal Reserve Board announced on January 28, 2005, the termination of the enforcement actions listed below. The Federal Reserve's enforcement action web site, www.federalreserve.gov/boarddocs/enforcement, reports the terminations as they occur.

- Citizens Deposit Bank and Trust Company, Vanceburg, Kentucky
  Written agreement dated September 29, 2000
  Terminated October 29, 2004

- Southern Commercial Bank, St. Louis, Missouri
  Written agreement dated June 10, 2003
  Terminated December 29, 2004

- BANKFIRST Corporation, Sioux Falls, South, Dakota
  Written agreement dated April 23, 2003
  Terminated January 6, 2005

On February 16, 2005, the Federal Reserve Board announced the termination of the following enforcement actions.

- Metamora Bancorp, Inc., Metamora, Ohio, and The Metamora State Bank, Metamora, Ohio
  Written agreement dated December 10, 2002
  Terminated January 31, 2005

- Independent Southern Bancshares, Inc., Employee Stock Ownership Trust and Independent Southern Bancshares, Inc., Brownsville, Tennessee
  Written agreement dated September 6, 2000
  Terminated August 18, 2004

- Banco Atlantico, S.A., Barcelona, Spain, and Banco Atlantico, S.A. New York Agency, New York, New York
  Written agreement dated June 3, 1999
  Terminated August 20, 2004

On February 23, 2005, the Federal Reserve Board announced the termination of the enforcement action below.

- Rurban Financial Corp., Defiance, Ohio, and The State Bank and Trust Company, Defiance, Ohio
  Written agreement dated July 5, 2002
  Terminated February 17, 2005

CHANGES IN BOARD STAFF

The Board of Governors approved on January 19, 2005, the following officer actions in the Division of Consumer and Community Affairs (DCCA) in conjunction with a reorganization of the division to enhance effectiveness:

Tonda Price was promoted to associate director for Consumer Compliance Supervision. She joined the Board in 1983 and was employed in the Division of Information Technology. Ms. Price joined DCCA as a manager in 1993 and was promoted to assistant director in 2002. She holds a BS in mathematics and economics from Norfolk State College and an MBA from the New York Institute of Technology.

Terri Johnsen was appointed associate director for Analysis and Communications. Ms. Johnsen joined the Board's staff in 1998 as a senior community affairs analyst and was promoted to manager in 1999. Before joining the Board, Ms. Johnsen was manager of the consumer compliance examination function at the Federal Reserve Bank of Kansas City. Ms. Johnsen has a BA in English and an MPA, both from the University of Kansas. She is also a graduate of the Stonier Graduate School of Banking.

Suzanne Killian was appointed assistant director for Consumer Compliance Supervision Oversight. Ms. Killian joined the Board in 1993 and was employed in the Board's Office of Inspector General before moving to DCCA as a manager in 1998. Ms. Killian has a BS in accounting from Bloomsburg University.

Adrienne D. Hurt assumed the position of associate counsel and adviser and has responsibility for projects in the consumer protection area and provides technical assistance and expertise to other Board and

Systemwide functions. She reports to the director. Ms. Hurt joined the Board in 1983. She was appointed to the official staff as assistant director in 1998 and promoted to associate director in 2002. Ms. Hurt has a law degree from the American University.

Irene (Shawn) McNulty assumed the position of senior adviser and has responsibility for a variety of supervision projects. She reports to the deputy director. Ms. McNulty joined the Board in 1980 and was employed in DCCA as a consumer examination analyst. Before joining the Board, she worked at the Federal Reserve Bank of Dallas as a consumer examination analyst. Ms. McNulty has a BBA from Southern Methodist University. She is also a graduate of the Stonier Graduate School of Banking.

The Division of Consumer and Community Affairs announced a new structure on January 31, 2005. The division has three branches reflecting the major functions performed by staff. These branches are: Regulations, Consumer Compliance Supervision, and Analysis and Communications.

The Board of Governors approved on January 31, 2005, the following officer actions in the Division of Reserve Bank Operations and Payment Systems (RBOPS).

Jeffrey Marquardt was promoted to deputy director, with continuing responsibility for the division's Cash, Retail Payments, Wholesale Payments, Fiscal Agency, Clearance and Settlement Systems, and Payments System Studies programs, and new responsibility for the Payment System Risk program. Mr. Marquardt joined the Board in 1981 as an economist in the Division of International Finance. He was appointed as assistant director in RBOPS in 1991 and was promoted to associate director in 2001. Mr. Marquardt received a BA from Michigan State University and an MA and PhD in economics from the University of Wisconsin. He also has a JD from the University of Wisconsin.

Paul Bettge was promoted to senior associate director with responsibility for Federal Reserve Bank Financial Accounting, Planning and Control, Human Resources, Oversight Coordination, and Audit Review programs. Mr. Bettge joined the Board in 1982. He became the manager of the Financial Accounting program in 1989 and the manager of the division's Payment System Risk program in 1993. Mr. Bettge was appointed assistant director in 1997 and associate director in 2000. Mr. Bettge has a BBA in accounting and an MBA in finance from the College of William and Mary. He is also a certified public accountant.

Ken Buckley was promoted to associate director to reflect the range of his responsibilities for the division's Information Technology, Building Planning, and Protection programs. Mr. Buckley joined the Board in 1988 as manager of the division's Communications program. He was appointed assistant director in 1999. Mr. Buckley received a BA in mathematics from William Preston College, an MS in biometry from the Medical College of Virginia, and an MS in computer science from Virginia Polytechnic Institute.

Jack Walton was promoted to associate director with new responsibility for the Fiscal Agency program, as well as continuing responsibility for the division's Retail Payments and Wholesale Payments programs. Mr. Walton joined the Board in 1977 as an economist in the Division of Research and Statistics and worked in RBOPS and the Division of Monetary Affairs before returning to RBOPS in 1992 as the manager of the ACH section. He was appointed assistant director in 2001. Mr. Walton received a BA in economics from Rockhurst College and an MA in economics from the University of Maryland.

Dorothy LaChapelle was promoted to deputy associate director with continuing responsibility for the division's Federal Reserve Bank Financial Accounting and Planning and Control programs. Ms. LaChapelle joined the Board in the Division of Information Technology in 1977. She became manager of RBOPS's Planning and Control section in 1999. Ms. LaChapelle was appointed assistant director in 2003. She has a BS in business administration from George Mason University.

Gregory Evans was appointed assistant director with responsibility for the division's Federal Reserve Bank Financial Accounting program. Mr. Evans joined the Board in 1988. He became manager of the division's Federal Reserve Bank Financial Accounting program in 1994. Before joining the Board, Mr. Evans was an internal auditor with the Detroit Branch of the Federal Reserve Bank of Chicago and a staff accountant with the public accounting firm Arthur Anderson. He received his BA in accounting from Michigan State University.

Michael Lambert was appointed assistant director with responsibility for the division's Cash program. Mr. Lambert joined the Board in 1984 and worked in the Division of Personnel, the Division of International Finance, and the Division of Banking Supervision and Regulation before joining RBOPS in 1999. He was appointed manager of the division's Cash section in 2002. Mr. Lambert holds a BA in biology from Western Maryland College and an MA in economics from George Mason University.

The Board of Governors approved on February 1, 2005, the following officer actions in the Legal Division in conjunction with a reorganization of the division:

Richard M. Ashton was promoted to deputy general counsel, Litigation and System Operations. He supervises the Litigation and Legal Services, Enforcement, and Monetary and Consumer Affairs sections of the Legal Division. Mr. Ashton joined the Board in 1976 as a staff attorney. He was appointed assistant general counsel in 1982, and associate general counsel responsible for the Litigation and Enforcement section in 1985. Mr. Ashton holds a JD from the Catholic University Law School.

Kathleen O'Day was promoted to deputy general counsel, Banking Regulation and Policy. She supervises the Banking Regulation and Policy group, which handles all domestic and international bank regulatory applications and policy matters as well as international trade matters. Ms. O'Day joined the Board in 1978 as an attorney in the Legal Division. She was appointed assistant general counsel over the division's International section in 1991, and was promoted to associate general counsel in 1992. Ms. O'Day received her JD from the Boston College Law School.

Stephanie Martin was named associate general counsel, Monetary and Consumer Affairs to recognize her expanded responsibilities in the area of consumer affairs. Ms. Martin joined the Legal Division in 1987 as a staff attorney. She was appointed to the official staff in 2001 as assistant general counsel for the Monetary and Reserve Bank Affairs section and was promoted to associate general counsel in 2003. Ms. Martin received her JD from the Harvard University Law School.

Ann E. Misback was promoted to associate general counsel, International Banking Regulation, Trade, and Policy. Ms. Misback joined the Board in 1992 as a senior attorney in the Legal Division, and was appointed to the official staff in 2000 as assistant general counsel in the International Banking section. Ms. Misback earned her JD from the Georgetown University Law Center.

Katherine H. Wheatley was promoted to associate general counsel, Litigation and Legal Services. Ms. Wheatley joined the Board in 1989 as an attorney in the Legal Division's Litigation and Enforcement section. She was appointed to the official staff as assistant general counsel in 1994. Ms. Wheatley received her JD from the Harvard University Law School.

Kieran Fallon was appointed assistant general counsel, Legislation and Special Projects. Mr. Fallon joined the Legal Division in 1995 as an attorney in the Banking Structure section. He was promoted to senior attorney in 1998 and to counsel later that year. Mr. Fallon was promoted to senior counsel in 1999, and to managing senior counsel in 2003. Before joining the Board, Mr. Fallon worked for the law firm of Morrison and Foerster. He received his JD from the New York University Law School.

Stephen Meyer was appointed assistant general counsel, Enforcement. Mr. Meyer joined the Legal Division in 1992 as a senior attorney in the Litigation and Enforcement section. He was promoted to senior counsel in 1998 and to managing senior counsel in 1999. Before joining the Board, Mr. Meyer was assistant director of the Manipulation and Trade Practices Unit at the Commodity Futures Trading Commission, and worked as an attorney at the Federal Trade Commission. Mr. Meyer received his JD from the New York University Law School.

Patricia Robinson was appointed assistant general counsel, Domestic Banking Regulation and Policy. Ms. Robinson joined the Legal Division in 1993 as an attorney in the Banking Structure section. She was promoted to senior attorney in 1995 and to senior counsel in 1998. Ms. Robinson was promoted to managing senior counsel in 2003. Before joining the Board, Ms. Robinson was an associate with the law firm of Sidley and Austin, and the law firm of McKenna, Conner, and Cuneo, where she handled a variety of bank regulatory matters. She earned her JD from the Georgetown University Law Center.

The Board of Governors approved on February 1, 2005, the appointment of Steven M. Roberts as an adviser in the Division of Banking Supervision and Regulation. Mr. Roberts reports to Herbert A. Biern, senior associate director, Enforcement, and will develop an enhanced, comprehensive, compliance risk program for the Federal Reserve's supervision function.

Until recently, Mr. Roberts served as the partner in charge of the financial services regulatory practice for KPMG, LLP, Washington, D.C. Before that, he was assistant to the Chairman of the Board of Governors, under Former Chairman Paul Volcker, and earlier was senior economist in the Division of Research and Statistics. Mr. Roberts was also chief economist for the U.S. Senate Committee on Banking, Housing, and Urban Affairs. Mr. Roberts holds a PhD and

Master of economics from Purdue University and a BS in economics from Rutgers University.

The Board of Governors approved on February 7, 2005, the appointment of Robert M. Pribble as special assistant to the Board in the Congressional Liaison Program.

Mr. Pribble joined the Office of Board Members as a congressional liaison assistant in 2003. Before joining the Board, he worked for the law firm of Wilmer, Cutler, and Pickering as a senior legislative analyst and for KPMG Peat Marwick as a manager. Mr. Pribble holds a BA in political science from Indiana University.

The Board of Governors approved on February 15, 2005, the promotion of Margaret M. Shanks to associate secretary of the Board and her appointment as the Board's ombudsman under the Riegle Community Development and Regulatory Improvement Act of 1994.

Ms. Shanks is responsible for overseeing the Records Management Program, Freedom of Information Office, and Federal Reserve Directors Program. As ombudsman, she is responsible for acting as a facilitator and mediator to ensure that complaints about Board or Reserve Bank regulatory actions are addressed in a fair and timely manner.

Ms. Shanks joined the Board in 1991 as a senior attorney in the Legal Divison and was appointed assistant secretary of the Board in 2001. She received her undergraduate degree from DePaul University and her JD degree from Loyola University–Chicago.

Revision to the Money Stock Data

Measures of the money stock and components were revised in February 2005 to incorporate the results of the annual seasonal factor review. Data in tables 1.10 and 1.21 in the *Statistical Supplement to the Federal Reserve Bulletin* reflect these changes beginning with the February 2005 issue.

Seasonally adjusted measures of the monetary stock and components incorporate revised seasonal factors produced from not-seasonally-adjusted data through December 2004. Monthly seasonal factors were estimated using the X-12-ARIMA procedure. The revisions to seasonal factors lowered M2 and M3 growth rates in the first two quarters of 2004, and raised them in the third and fourth quarters.

Historical data, updated each week, are available through the Federal Reserve Board's web site at www.federalreserve.gov/releases/ with the H.6 statistical release. Current and historical data are also on the Economic Bulletin Board of the U.S. Department of Commerce. For paid electronic access to the Economic Bulletin Board, call STAT-USA at 1-800-782-8872 or 202-482-1986.

1. Monthly seasonal factors used to construct M1, January 2004–March 2006

Year and month	Currency	Nonbank travelers checks	Demand deposits	Other checkable deposits[1]	
				Total	At banks
2004—January	.9971	.9960	.9993	1.0040	1.0347
February	.9991	.9998	.9717	.9838	.9954
March	.9988	.9968	1.0006	1.0125	1.0172
April	.9992	.9889	1.0083	1.0273	1.0267
May	.9998	.9921	.9882	.9975	.9879
June	.9999	1.0122	1.0014	1.0092	1.0008
July	1.0020	1.0299	1.0019	.9974	.9883
August	.9996	1.0207	.9944	.9981	.9855
September	.9975	1.0031	.9898	.9870	.9797
October	.9993	.9925	.9898	.9848	.9819
November	1.0008	.9825	.9988	.9851	.9785
December	1.0078	.9865	1.0532	1.0134	1.0222
2005—January	.9967	.9968	.9990	1.0035	1.0335
February	.9987	1.0004	.9710	.9833	.9963
March	.9983	.9973	1.0021	1.0134	1.0197
April	.9995	.9889	1.0091	1.0257	1.0255
May	.9990	.9910	.9904	.9987	.9866
June	.9995	1.0098	1.0023	1.0091	1.0028
July	1.0029	1.0290	1.0032	.9981	.9876
August	.9996	1.0188	.9938	.9987	.9874
September	.9980	1.0027	.9899	.9866	.9803
October	.9988	.9924	.9875	.9848	.9805
November	1.0018	.9831	.9980	.9856	.9783
December	1.0082	.9877	1.0512	1.0122	1.0204
2006—January	.9962	.9966	.9999	1.0039	1.0329
February	.9985	.9993	.9712	.9833	.9968
March	.9988	.9976	1.0022	1.0130	1.0213

1. Seasonally adjusted other checkable deposits at thrift institutions are derived as the difference between total other checkable deposits, seasonally adjusted, and seasonally adjusted other checkable deposits at commercial banks.

2. Monthly seasonal factors used to construct M2 and M3, January 2004–March 2006

Year and month	Savings and MMDA deposits[1]	Small-denomination time deposits[1]	Large-denomination time deposits[1]	Money market mutual funds		RPs	Eurodollars
				In M2	In M3 only		
2004—January	.9900	1.0013	.9919	1.0051	1.0261	.9922	1.0028
February	.9910	1.0011	.9898	1.0073	1.0215	1.0139	1.0189
March	.9968	1.0008	.9955	1.0120	1.0117	1.0173	1.0260
April	1.0067	1.0004	1.0019	1.0047	.9910	.9983	1.0269
May	1.0009	.9993	1.0164	.9901	.9852	1.0166	1.0227
June	1.0023	.9982	1.0107	.9917	.9903	1.0267	.9844
July	1.0033	.9984	1.0046	.9939	.9871	.9917	.9785
August	1.0024	.9987	1.0010	1.0022	.9945	.9960	.9837
September	1.0042	.9994	.9995	.9983	.9854	.9910	.9856
October	1.0018	1.0000	.9942	.9949	.9868	.9779	.9946
November	1.0033	1.0009	.9938	.9980	1.0029	.9896	.9939
December	.9979	1.0009	.9999	1.0036	1.0160	.9914	.9852
2005—January	.9894	1.0012	.9922	1.0040	1.0241	.9894	1.0029
February	.9892	1.0012	.9898	1.0061	1.0222	1.0127	1.0169
March	.9952	1.0012	.9958	1.0103	1.0113	1.0162	1.0244
April	1.0087	1.0008	1.0024	1.0043	.9916	.9976	1.0258
May	1.0001	.9996	1.0161	.9909	.9871	1.0145	1.0223
June	1.0029	.9984	1.0103	.9929	.9905	1.0272	.9834
July	1.0055	.9984	1.0048	.9942	.9887	.9944	.9780
August	1.0029	.9985	1.0016	1.0031	.9952	.9968	.9853
September	1.0045	.9990	.9990	.9995	.9860	.9945	.9875
October	1.0016	.9997	.9944	.9948	.9878	.9823	.9974
November	1.0038	1.0006	.9933	.9974	1.0012	.9880	.9932
December	.9982	1.0009	.9997	1.0030	1.0135	.9885	.9849
2006—January	.9867	1.0013	.9926	1.0035	1.0223	.9877	1.0029
February	.9884	1.0014	.9898	1.0054	1.0229	1.0115	1.0157
March	.9955	1.0014	.9961	1.0098	1.0113	1.0155	1.0233

1. Seasonal factors are applied to deposit data at both commercial banks and thrift institutions.

3. Weekly seasonal factors used to construct M1, December 6, 2004–April 3, 2006

Week ending	Currency	Nonbank travelers checks	Demand deposits	Other checkable deposits[1]	
				Total	At banks
2004—December 6	1.0025	.9788	.9677	.9950	.9779
13	1.0048	.9829	.9444	.9732	.9660
20	1.0081	.9871	1.0633	1.0059	1.0181
27	1.0155	.9912	1.1530	1.0438	1.0777
2005—January 3	1.0067	.9954	1.1345	1.0611	1.0745
10	1.0014	.9960	.9802	.9951	1.0235
17	.9970	.9967	.9861	.9862	1.0193
24	.9925	.9973	.9690	.9958	1.0355
31	.9900	.9979	1.0050	1.0129	1.0420
February 7	.9981	.9989	.8952	.9762	.9943
14	.9999	.9999	.9554	.9627	.9742
21	.9995	1.0008	.9931	.9843	.9978
28	.9971	1.0018	1.0406	1.0099	1.0189
March 7	1.0020	1.0002	.9345	1.0048	.9987
14	.9991	.9985	.9664	.9916	.9915
21	.9979	.9968	1.0039	1.0068	1.0188
28	.9959	.9952	1.0752	1.0372	1.0583
April 4	1.0001	.9935	1.0223	1.0334	1.0267
11	1.0031	.9913	.9356	1.0026	.9925
18	.9993	.9891	1.0033	1.0245	1.0238
25	.9963	.9868	1.0464	1.0388	1.0584
May 2	.9963	.9846	1.0773	1.0382	1.0332
9	1.0015	.9872	.9057	.9818	.9641
16	.9983	.9899	.9813	.9810	.9648
23	.9975	.9925	1.0120	.9973	.9921
30	.9993	.9951	1.0433	1.0214	1.0121
June 6	1.0010	.9978	.9370	1.0057	.9880
13	1.0002	1.0044	.9601	.9872	.9726
20	.9985	1.0111	1.0018	1.0078	1.0036
27	.9979	1.0178	1.0798	1.0312	1.0388
July 4	1.0046	1.0245	1.0239	1.0154	1.0056
11	1.0059	1.0266	.9275	.9761	.9590
18	1.0026	1.0287	.9949	.9828	.9764
25	1.0002	1.0308	1.0402	1.0036	1.0028

3.—Continued

Week ending	Currency	Nonbank travelers checks	Demand deposits	Other checkable deposits[1] Total	Other checkable deposits[1] At banks
August 1	.9994	1.0330	1.0615	1.0278	1.0117
8	1.0048	1.0275	.9086	.9926	.9655
15	1.0011	1.0220	.9625	.9782	.9603
22	.9981	1.0165	1.0072	.9945	.9895
29	.9950	1.0110	1.0792	1.0201	1.0246
September 5	1.0021	1.0055	.9653	.9982	.9901
12	.9987	1.0041	.9299	.9646	.9560
19	.9973	1.0026	.9928	.9768	.9742
26	.9957	1.0011	1.0627	1.0011	1.0013
October 3	.9967	.9996	1.0213	1.0095	.9892
10	1.0028	.9965	.9050	.9567	.9470
17	.9991	.9933	.9582	.9666	.9652
24	.9971	.9900	1.0133	.9933	.9966
31	.9954	.9868	1.0636	1.0135	1.0138
November 7	1.0023	.9854	.9190	.9782	.9615
14	1.0021	.9840	.9374	.9565	.9459
21	1.0006	.9827	.9843	.9840	.9817
28	1.0036	.9813	1.1265	1.0138	1.0143
December 5	1.0027	.9799	1.0093	1.0001	.9885
12	1.0052	.9838	.9427	.9733	.9703
19	1.0080	.9877	1.0533	1.0021	1.0127
26	1.0152	.9916	1.1409	1.0386	1.0652
2006—January 2	1.0070	.9955	1.1383	1.0611	1.0748
9	1.0019	.9960	.9915	.9935	1.0235
16	.9966	.9964	.9938	.9901	1.0189
23	.9928	.9969	.9822	1.0003	1.0382
30	.9902	.9974	1.0060	1.0174	1.0440
February 6	.9971	.9978	.8952	.9830	1.0007
13	.9998	.9987	.9552	.9605	.9730
20	1.0001	.9996	.9913	.9801	.9936
27	.9964	1.0005	1.0374	1.0063	1.0194
March 6	1.0011	1.0014	.9333	1.0061	1.0045
13	.9995	.9994	.9653	.9909	.9958
20	.9985	.9974	1.0050	1.0065	1.0188
27	.9971	.9953	1.0750	1.0354	1.0555
April 3	.9989	.9933	1.0431	1.0368	1.0332

1. Seasonally adjusted other checkable deposits at thrift institutions are derived as the difference between total other checkable deposits, seasonally adjusted, and seasonally adjusted other checkable deposits at commercial banks.

4. Weekly seasonal factors used to construct M2 and M3, December 6, 2004–April 3, 2006

Week ending	Savings and MMDA deposits[1]	Small-denomination time deposits[1]	Large-denomination time deposits[1]	Money market mutual funds In M2	Money market mutual funds In M3 only	RPs	Eurodollars
2004—December 6	1.0106	1.0012	.9962	1.0029	1.0095	.9943	.9814
13	1.0122	1.0009	1.0023	1.0081	1.0281	1.0012	.9814
20	.9977	1.0005	1.0024	1.0068	1.0176	.9885	.9772
27	.9801	1.0008	1.0014	1.0020	1.0173	1.0001	.9893
2005—January 3	.9899	1.0021	.9955	.9941	1.0003	.9595	1.0039
10	1.0096	1.0017	.9955	1.0024	1.0154	.9736	1.0056
17	.9989	1.0012	.9941	1.0072	1.0287	.9902	1.0017
24	.9779	1.0007	.9893	1.0074	1.0359	.9972	1.0022
31	.9642	1.0006	.9886	1.0031	1.0268	1.0097	1.0015
February 7	.9947	1.0011	.9914	1.0046	1.0195	1.0143	1.0023
14	.9964	1.0013	.9915	1.0048	1.0227	1.0212	1.0138
21	.9860	1.0013	.9891	1.0072	1.0246	1.0052	1.0247
28	.9798	1.0011	.9872	1.0078	1.0219	1.0102	1.0266
March 7	1.0066	1.0013	.9907	1.0099	1.0135	1.0123	1.0159
14	1.0088	1.0013	.9953	1.0106	1.0185	1.0183	1.0206
21	.9950	1.0010	.9979	1.0121	1.0115	1.0206	1.0210
28	.9783	1.0011	.9959	1.0106	1.0107	1.0256	1.0378
April 4	1.0108	1.0013	1.0037	1.0057	.9901	.9880	1.0296
11	1.0268	1.0014	1.0023	1.0128	1.0017	.9958	1.0146
18	1.0164	1.0010	1.0001	1.0088	.9928	.9920	1.0212
25	.9899	1.0003	.9990	1.0013	.9890	1.0022	1.0328

4.—Continued

Week ending		Savings and MMDA deposits[1]	Small-denomination time deposits[1]	Large-denomination time deposits[1]	Money market mutual funds		RPs	Eurodollars
					In M2	In M3 only		
May	2	.9841	1.0002	1.0095	.9891	.9808	1.0094	1.0348
	9	1.0139	1.0001	1.0157	.9876	.9816	1.0197	1.0290
	16	1.0111	.9997	1.0186	.9883	.9864	1.0163	1.0194
	23	.9916	.9992	1.0173	.9938	.9942	1.0064	1.0185
	30	.9855	.9992	1.0151	.9939	.9877	1.0156	1.0211
June	6	1.0146	.9990	1.0147	.9937	.9884	1.0242	1.0058
	13	1.0197	.9986	1.0127	.9959	.9967	1.0292	.9896
	20	1.0056	.9980	1.0108	.9940	.9897	1.0310	.9724
	27	.9824	.9978	1.0083	.9910	.9919	1.0336	.9725
July	4	1.0055	.9984	1.0000	.9857	.9783	1.0045	.9753
	11	1.0222	.9988	1.0016	.9938	.9884	.9868	.9754
	18	1.0067	.9985	1.0037	.9946	.9906	.9898	.9756
	25	.9895	.9981	1.0068	.9972	.9951	.9951	.9816
August	1	.9908	.9982	1.0107	.9962	.9864	1.0008	.9814
	8	1.0205	.9985	1.0076	1.0006	.9901	1.0098	.9818
	15	1.0159	.9985	1.0009	1.0018	.9945	1.0044	.9740
	22	.9977	.9984	.9966	1.0067	1.0000	.9835	.9854
	29	.9828	.9986	.9997	1.0051	1.0003	.9915	.9995
September	5	1.0138	.9990	1.0024	1.0004	.9861	.9887	.9882
	12	1.0234	.9991	1.0023	1.0039	.9912	.9950	.9855
	19	1.0055	.9989	.9971	1.0016	.9880	.9981	.9858
	26	.9819	.9989	.9950	.9970	.9852	1.0000	.9917
October	3	.9927	.9995	.9995	.9916	.9743	.9847	.9860
	10	1.0168	1.0000	1.0012	.9948	.9839	.9774	.9912
	17	1.0119	.9999	.9958	.9961	.9893	.9783	.9916
	24	.9903	.9994	.9902	.9963	.9935	.9822	1.0053
	31	.9839	.9994	.9885	.9936	.9901	.9904	1.0061
November	7	1.0142	1.0001	.9926	.9933	.9898	.9962	.9954
	14	1.0202	1.0005	.9945	.9943	.9969	.9927	.9921
	21	1.0053	1.0007	.9921	.9995	1.0064	.9817	.9931
	28	.9850	1.0008	.9935	1.0011	1.0098	.9810	.9957
December	5	1.0071	1.0010	.9950	1.0024	1.0072	.9886	.9817
	12	1.0134	1.0009	1.0017	1.0072	1.0231	.9989	.9817
	19	.9992	1.0006	1.0026	1.0064	1.0173	.9875	.9774
	26	.9811	1.0008	1.0013	1.0019	1.0147	.9978	.9861
2006—January	2	.9835	1.0017	.9951	.9948	.9995	.9624	1.0011
	9	1.0065	1.0019	.9963	.9999	1.0073	.9677	1.0062
	16	.9977	1.0014	.9959	1.0068	1.0252	.9864	1.0021
	23	.9781	1.0009	.9901	1.0068	1.0327	.9944	1.0031
	30	.9638	1.0007	.9875	1.0029	1.0306	1.0062	1.0011
February	6	.9925	1.0011	.9917	1.0039	1.0218	1.0098	1.0012
	13	.9951	1.0015	.9917	1.0041	1.0224	1.0180	1.0117
	20	.9864	1.0015	.9895	1.0061	1.0257	1.0065	1.0218
	27	.9781	1.0013	.9867	1.0068	1.0229	1.0113	1.0261
March	6	1.0033	1.0015	.9898	1.0089	1.0142	1.0132	1.0132
	13	1.0066	1.0015	.9946	1.0101	1.0185	1.0192	1.0183
	20	.9945	1.0013	.9976	1.0116	1.0116	1.0194	1.0194
	27	.9795	1.0013	.9964	1.0106	1.0115	1.0240	1.0359
April	3	.9996	1.0016	1.0047	1.0064	.9932	.9906	1.0318

1. Seasonal factors are applied to deposit data at both commercial banks and thrift institutions.

Legal Developments

ORDERS ISSUED UNDER BANK HOLDING COMPANY ACT

Orders Issued Under Section 3 of the Bank Holding Company Act

Banco Bilbao Vizcaya Argentaria, S.A.
Bilbao, Spain

Order Approving the Acquisition of a Bank Holding Company

Banco Bilbao Vizcaya Argentaria, S.A. ("BBVA"), a bank holding company within the meaning of the Bank Holding Company Act ("BHC Act"), has requested the Board's approval under section 3 of the BHC Act[1] to acquire Laredo National Bancshares, Inc. ("Laredo"), Laredo, Texas; Laredo National Bancshares of Delaware, Inc., Wilmington, Delaware; and The Laredo National Bank ("LNB") and South Texas National Bank of Laredo ("STNB"), both of Laredo.

Notice of the proposal, affording interested persons an opportunity to comment, has been published (69 *Federal Register* 65,196 (2004)). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3 of the BHC Act.

BBVA, with total consolidated assets of approximately $363 billion, is the 34th largest banking organization in the world. BBVA is the 110th largest depository organization in the United States, with total assets in the United States of $5.5 billion.[2] It controls approximately $2.7 billion in deposits, which represents less than 1 percent of the total amount of deposits of insured depository institutions in the United States. BBVA's U.S. subsidiary banks include Banco Bilbao Vizcaya Argentaria Puerto Rico ("BBVA Puerto Rico"), San Juan, Puerto Rico, a bank chartered in Puerto Rico; and Valley Bank, Moreno Valley, California, a state-chartered bank. BBVA also operates a branch in New York, New York, and an agency in Miami, Florida. BBVA's subsidiary bank in Mexico, BBVA Bancomer, S.A., operates a state-licensed agency in Houston, Texas. BBVA has no retail depository institution offices in Texas.

Laredo, with total consolidated assets of approximately $3.4 billion, is the 17th largest depository organization in Texas. It controls deposits of approximately $2.8 billion, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state.[3] Laredo's subsidiary banks have branches only in Texas.

On consummation of this proposal, BBVA would become the 82nd largest depository organization in the United States, with total consolidated U.S. assets of $8.9 billion. BBVA would control deposits of $5.4 billion, representing less than 1 percent of the total amount of deposits of insured depository institutions in the United States.[4]

Interstate Analysis

Section 3(d) of the BHC Act allows the Board to approve an application by a bank holding company to acquire control of a bank located in a state other than the home state of the bank holding company if certain conditions are met. For purposes of the BHC Act, the home state of BBVA is Puerto Rico and Laredo is located in Texas. Based on a review of all the facts of record, including a review of the relevant state statutes, the Board finds that all the conditions for an interstate acquisition enumerated in section 3(d) of the BHC Act are met in this case.[5] The Board is therefore permitted to approve the proposal under section 3(d) of the BHC Act.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of an attempt to monopolize the business

1. 12 U.S.C. § 1842

2. Worldwide asset data are as of December 31, 2003, and worldwide ranking is as of November 12, 2004. United States asset and deposit data are as of September 30, 2004, and national ranking is as of June 30, 2004. The data and rankings are adjusted to reflect mergers and acquisitions completed as of June 30, 2004.

3. Asset data for Laredo are as of September 30, 2004. Deposit and ranking data are as of June 30, 2004, and are adjusted to reflect mergers and acquisitions completed as of that date.

4. In this context, the term "insured depository institutions" includes insured commercial banks, savings banks, and savings associations.

5. 12 U.S.C. §§ 1842(d)(1)(A) & (B), 1842(d)(2)(A) & (B). BBVA is currently adequately capitalized and adequately managed, as defined by applicable law, and would remain so on consummation of this proposal. BBVA and its affiliates would control less than 10 percent of the total amount of deposits of insured depository institutions in the United States. All other requirements of section 3(d) would also be met on consummation of the proposal.

of banking. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[6]

Applicant does not currently compete with Laredo in any relevant banking market. Accordingly, the Board concludes, based on all the facts of record, that consummation of the proposal would not have a significant adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive considerations are consistent with approval.

Financial, Managerial, and Supervisory Considerations

The BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and depository institutions involved in the proposal and certain other supervisory factors. The Board has carefully considered these factors in light of all the facts of record, including information provided by BBVA, confidential reports of examination and other supervisory information received from the federal and state banking supervisors of the organizations involved, publicly reported and other financial information, and public comments received on the proposal.[7] The Board also has consulted with the Bank of Spain, which is responsible for the supervision and regulation of Spanish financial institutions.

In evaluating financial factors in expansion proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary banks and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the effect of the transaction on the financial condition of the combined organization on consummation, including its capital position, asset quality, and earnings prospects and the impact of the proposed funding of the transaction.

Based on its review of these factors, the Board believes financial factors are consistent with approval of this proposal. Laredo currently is well capitalized, and the capital levels of BBVA would continue to exceed the minimum levels that would be required under the Basel Capital Accord. Furthermore, BBVA's capital levels are considered equivalent to the capital levels that would be required of a U.S. banking organization and would remain so after consummation of this proposal. In addition, BBVA has sufficient financial resources to effect the proposal. The proposed transaction is structured as a share purchase, and the consideration to be received by Laredo's shareholders would be provided from BBVA's available funds.

The Board also has considered the managerial resources of BBVA, Laredo, and their subsidiary banks, particularly the supervisory experience of the other relevant banking supervisory agencies with the organizations and their records of compliance with applicable banking laws. The Board has reviewed the assessments of the organizations' management and risk management systems by the relevant federal and state banking supervisory agencies. In addition, the Board has considered the anti-money laundering programs at BBVA and the assessment of these programs by the relevant federal supervisory agencies, state banking agencies, and the Bank of Spain.[8] The Board also has considered BBVA's plans to implement the proposal, including its proposed management after consummation and the proposed integration of Laredo and its subsidiaries into BBVA.[9] Based on these and all other facts of record, the Board concludes that the managerial resources and future prospects of the organizations involved in the proposal are consistent with approval.

Section 3 of the BHC Act also provides that the Board may not approve an application involving a foreign bank unless the bank is subject to comprehensive supervision or regulation on a consolidated basis by the appropriate authorities in the bank's home country.[10] As previously

6. 12 U.S.C. § 1842(c)(1).

7. A commenter quoted a Spanish newspaper article that suggested that a construction group in Spain intended to acquire less than 5 percent of the voting stock of BBVA. The commenter provided no information, and no other information is in the record, that indicates that this potential future acquisition is in any way related to the proposal currently under review.

8. The commenter made general allegations about BBVA's ability to comply with U.S. anti-money laundering laws. In addition, the commenter expressed concern, citing media reports in 2002, that BBVA might be under investigation in Mexico, Columbia, and Peru in connection with its acquisitions of financial institutions in those countries. BBVA has provided information to the Board, the Bank of Spain, and other appropriate governmental authorities relating to these allegations and has publicly disclosed information on these matters in filings with the U.S. Securities and Exchange Commission. As part of its review of banking organizations, the Board seeks information on enforcement actions by government authorities in other countries. The Board notes that no enforcement action has been initiated against BBVA by government authorities in the countries mentioned in the media reports.

9. The commenter criticized LNB's and STNB's lending relationships with unaffiliated pawn shops and Valley Bank's lending to a rent-to-own business, stating that BBVA was enabling high-cost, nontraditional providers of financial services. These businesses are licensed by the states where they operate and are subject to applicable state law. BBVA stated that neither Laredo nor any of its affiliates engages in the activities conducted by payday lenders, check cashers, or rent-to-own businesses. The only dealings that Laredo or any of its affiliates have with such businesses are in the ordinary course of extending credit and cashing checks for existing customers, to the extent consistent with regulations of the Office of the Comptroller of the Currency ("OCC"). BBVA further stated that neither Laredo nor any of its affiliates plays any role, formal or otherwise, in the lending practices or credit review processes of any unaffiliated subprime lender or provider of nontraditional financing products.

10. 12 U.S.C. § 1842(c)(3)(B). Under Regulation Y, the Board uses the standards enumerated in Regulation K to determine whether a foreign bank is subject to consolidated home country supervision. *See* 12 CFR 225.13(a)(4). Regulation K provides that a foreign bank will be considered subject to comprehensive supervision or regulation

noted, the home country supervisor of BBVA is the Bank of Spain.

In approving an application under the International Banking Act ("IBA"),[11] the Board previously determined that BBVA was subject to home country supervision on a consolidated basis by the Bank of Spain.[12] Based on all the facts of record, the Board has concluded that BBVA continues to be subject to comprehensive supervision on a consolidated basis by its home country supervisor.

In addition, section 3 of the BHC Act requires the Board to determine that an applicant has provided adequate assurances that it will make available to the Board such information on its operations and activities and those of its affiliates that the Board deems appropriate to determine and enforce compliance with the BHC Act.[13] The Board has reviewed the restrictions on disclosure in the relevant jurisdictions in which BBVA operates and has communicated with relevant government authorities concerning access to information. In addition, BBVA has previously committed to make available to the Board such information on the operations of BBVA and its affiliates that the Board deems necessary to determine and enforce compliance with the BHC Act, the IBA, and other applicable federal law. BBVA has also committed to cooperate with the Board to obtain any waivers or exemptions that may be necessary to enable BBVA and its affiliates to make such information available to the Board. In light of the Board's review of the restrictions on disclosure and these commitments, the Board concludes that BBVA has provided adequate assurances of access to any appropriate information the Board may request. Based on these and all other facts of record, the Board has concluded that the supervisory factors it is required to consider are consistent with approval.

Convenience and Needs Considerations

In acting on this proposal, the Board is required to consider the effects of the transaction on the convenience and needs of the communities to be served and to take into account the records of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[14] The CRA requires the federal financial supervisory agencies to encourage financial institutions to help meet the credit needs of local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account an institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank expansionary proposals.

The Board has considered carefully the convenience and needs factor and the CRA performance records of the subsidiary banks of BBVA and Laredo in light of all the facts of record, including public comment on the proposal.[15] As provided in the CRA, the Board has evaluated the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the CRA performance records of the relevant insured depository institutions. An institution's most recent CRA performance evaluation is a particularly important consideration in the application process because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisor.[16]

All the subsidiary insured depository institutions of BBVA and Laredo received "satisfactory" ratings at the most recent evaluations of their CRA performance. BBVA Puerto Rico received a "satisfactory" CRA performance rating by the Federal Deposit Insurance Corporation ("FDIC"), as of October 29, 2002, and Valley Bank received a "satisfactory" CRA performance rating by the FDIC, as of August 26, 2002.[17] The OCC gave a "satisfactory" rating to LNB, as of February 5, 2001, and to STNB, as of September 3, 2003.

BBVA represented that it is committed to maintaining the existing CRA programs at LNB and STNB and enhancing their CRA performance. In addition, BBVA represented that consummation of this proposal would further its goal of becoming a leading financial services provider to the Hispanic community in the United States.

In BBVA Puerto Rico's most recent CRA performance evaluation, examiners reported that the bank's lending

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on a consolidated basis if the Board determines that the bank is supervised or regulated in such a manner that its home country supervisor receives sufficient information on the worldwide operations of the bank, including its relationship with any affiliates, to assess the bank's overall financial condition and its compliance with laws and regulations. *See* 12 CFR 211.24(c)(1).

11. 12 U.S.C. §3101 *et seq.*

12. *See BBVA Bancomer, S.A.*, 89 *Federal Reserve Bulletin* 146 (2003).

13. *See* 12 U.S.C. §1842(c)(3)(A).

14. 12 U.S.C. §2901 *et seq.*

15. The commenter asserted, based on data reported under the Home Mortgage Disclosure Act ("HMDA") (12 U.S.C. §2801 *et seq.*), that Homeowners Loan Corporation ("HLC"), a subprime lending subsidiary of LNB, originated a disproportionately large percentage of subprime loans to African Americans in possible violation of fair lending laws. Using 2003 HMDA data reported by HLC in several MSAs, the commenter compared the number of HLC's loan originations to white applicants with the number of its loan originations to African-American applicants. Based on these comparisons, the commenter asserted that HLC's ratio of originations to African-American applicants compared to white applicants significantly exceeded the ratio of aggregate lenders in those markets. The commenter alleged that HLC's disproportionately high ratio of originations to African-American applicants compared to white applicants was a possible indication of fair lending law violations. The Board has considered the limited HMDA data presented by the commenter; confidential supervisory information received from the OCC, the primary federal supervisor of HLC; and information provided by the applicant. BBVA has stated that HLC selects prospects for direct marketing using objective criteria, specifically, home ownership, home equity, and credit score, and uses no racial demographic or geographic criteria in any modeling for marketing purposes. The Board also has consulted with the OCC about HLC's subprime lending operations and its programs for compliance with fair lending laws and other consumer protection laws.

16. *See Interagency Questions and Answers Regarding Community Reinvestment*, 66 *Federal Register* 36,620 and 36,639 (2001).

17. The FDIC evaluated the CRA performance of Valley Bank before BBVA acquired it in early 2004.

levels reflected a "good responsiveness" to the credit needs of its assessment areas during the evaluation period.[18] Examiners noted that BBVA Puerto Rico maintained a "reasonable standard of lending" in its assessment areas by aggressively offering a variety of loan products at competitive rates. They commended BBVA Puerto Rico's distribution of small business loans and its efforts to meet the needs of businesses within its assessment areas.[19] In addition, examiners commended BBVA Puerto Rico for having a high level of community development lending directed towards areas where traditional bank products did not meet the needs of LMI families. They also noted that BBVA Puerto Rico had developed the "Global Commercial Package," a special product designed to satisfy the needs of small business owners in Puerto Rico by offering commercial accounts, credit facilities, and merchant services.

In LNB's most recent evaluation, the bank received "high satisfactory" ratings under both the lending and investment tests and an "outstanding" rating under the service test.[20] In particular, examiners described LNB's home mortgage lending, small loans to businesses, branch distribution, and community development services as "excellent."

Examiners commended LNB's record of making home purchase loans to borrowers of different income levels, including LMI individuals. They reported that the bank's market share of home purchase loans to LMI borrowers was almost twice its overall market share in the Laredo MSA.[21] In addition, examiners commended Laredo for its distribution of home purchase loans to LMI borrowers in the Houston MSA. Examiners noted that LNB offered a special affordable housing product with flexible underwriting criteria for LMI borrowers. LNB offered this product directly to customers and indirectly through special programs of Neighborhood Housing Services, Inc., an organization that provides home-buyer education classes and offers grants for down payments and closing-cost assistance.

Examiners also commended LNB's participation in the Bank Enterprise Award program of the U.S. Department of the Treasury for loans in low-income, high-unemployment neighborhoods designated as "Distressed Communities." They noted that LNB had 13 full-service branches in Distressed Communities, representing 62 percent of its total branches. In addition, examiners commended LNB for providing affordable checking account products to LMI customers and offering check-cashing services to noncustomers with a fee structure that was more affordable than most check-cashing operations offered in the bank's assessment areas.

The Board has carefully considered all the facts of record, including reports of examination of the CRA performance records of the institutions involved, information provided by BBVA, comments on the proposal, confidential supervisory information, and BBVA's plans to enhance the CRA performance of STNB and LNB. The Board notes that the proposal would provide Laredo's customers with expanded banking opportunities and resources, including access to BBVA's expertise in and knowledge of Latin American banking markets. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that considerations relating to the convenience and needs factor, including the CRA performance records of the relevant depository institutions, are consistent with approval.

Conclusion

Based on the foregoing and all facts of record, the Board has determined that the application should be, and hereby is, approved. In reaching its conclusion, the Board has considered all the facts of record, including commitments and conditions imposed in this order, in light of the factors that it is required to consider under the BHC Act and other applicable statutes.[22]

The Board's approval is specifically conditioned on BBVA's compliance with the conditions imposed in this order, including receipt by BBVA of all appropriate regulatory approvals, and with the commitments made to the Board in connection with the application. For purposes of

18. The evaluation period was from January 2000 through September 2002.

19. For purposes of this order, a "small business loan" or a "small loan to business" is a loan in an original amount of $1 million or less that either is secured by nonfarm, nonresidential properties or is classified as a commercial and industrial loan.

20. The evaluation period was January 1998 through February 2001. Full-scope reviews were performed on the following LNB assessment areas: the Laredo Metropolitan Statistical Area ("MSA"), the Harris County portion of the Houston MSA, and the Bexar County portion of the San Antonio MSA. More than 90 percent of LNB's small business, home purchase, home improvement, and refinance loans were originated or purchased within these assessment areas. LNB assessment areas receiving limited-scope reviews included the Brownsville, McAllen, and Corpus Christi MSAs and Willacy County.

21. Examiners noted that the Laredo MSA was one of the least affordable areas in the country for home ownership because home prices were relatively high while a large percentage of the population lived below the poverty level.

22. The commenter requested that the Board hold a public hearing or meeting on the proposal. Section 3 of the BHC Act does not require the Board to hold a public hearing on an application unless the appropriate supervisory authority for the bank to be acquired makes a timely written recommendation of denial of the application. The Board has not received such a recommendation from the appropriate supervisory authority. Under its regulations, the Board also may, in its discretion, hold a public meeting or hearing on an application to acquire a bank if a meeting or hearing is necessary or appropriate to clarify factual issues related to the application and to provide an opportunity for testimony. 12 CFR 225.16(e). The Board has considered carefully the commenter's request in light of all the facts of record. In the Board's view, the commenter had ample opportunity to submit comments on the proposal, and, in fact, the commenter has submitted written comments that the Board has considered carefully in acting on the proposal. The commenter's request fails to demonstrate why its written comments do not adequately present its evidence and fails to identify disputed issues of fact that are material to the Board's decision that would be clarified by a public meeting or hearing. For these reasons, and based on all the facts of record, the Board has determined that a public meeting or hearing is not required or warranted in this case. Accordingly, the request for a public meeting or hearing on the proposal is denied.

this transaction, these conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

The proposed transaction may not be consummated before the fifteenth calendar day after the effective date of this order, or later than three months after the effective date of this order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of New York, acting pursuant to delegated authority.

By order of the Board of Governors, effective March 30, 2005.

Voting for this action: Chairman Greenspan and Governors Gramlich, Bies, Olson, Bernanke, and Kohn. Absent and not voting: Vice Chairman Ferguson.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

Citigroup Inc.
New York, New York

Order Approving the Acquisition of a Bank

Citigroup Inc. ("Citigroup"), a financial holding company within the meaning of the Bank Holding Company Act ("BHC Act"), has requested the Board's approval under section 3 of the BHC Act[1] to acquire First American Bank, SSB ("FAB"), Bryan, Texas. Citigroup would acquire FAB immediately after its conversion to a national bank.[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published in the *Federal Register* (69 *Federal Register* 58,173 (2004)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 3 of the BHC Act.

Citigroup, with total consolidated assets of approximately $1.48 trillion, is the largest depository organization in the United States.[3] Citigroup's subsidiary depository institutions control deposits of approximately $192.5 billion, which represent approximately 3 percent of the total deposits of insured depository institutions in the United States.[4] Citigroup operates insured depository institutions in fourteen states, the District of Columbia, Puerto Rico, and two U.S. territories.[5] Citigroup currently operates one retail depository institution branch in Texas, primarily for employees at a sales and service center in San Antonio, and several nonbanking companies in Texas. Citigroup has no other retail depository institution offices in the state.

FAB, with total consolidated assets of approximately $3.5 billion, is the 18th largest insured depository institution in Texas, controlling deposits of approximately $2.7 billion. Currently, FAB is an indirect subsidiary of The Adam Corporation/Group ("TACG"), a Texas corporation that is subject to the supervision and regulation of the Office of Thrift Supervision ("OTS").[6]

On consummation of the proposal, Citigroup would become the 18th largest depository organization in Texas, controlling deposits of approximately $2.7 billion, which represent less than 1 percent of the total amount of insured deposits in the state.

Interstate Analysis

Section 3(d) of the BHC Act allows the Board to approve an application by a bank holding company to acquire control of a bank located in a state other than the home state of such bank holding company if certain conditions are met.[7] For purposes of the BHC Act, the home state of Citigroup is New York. Depository institutions controlled by Citigroup operate in California, Connecticut, Delaware, Florida, Georgia, Illinois, Maryland, Nevada, New Jersey, New York, South Dakota, Texas, Utah, Virginia, the District of Columbia, Puerto Rico, Guam, and the U.S. Virgin Islands. Citigroup proposes to acquire a bank located in Texas.[8]

Based on a review of all the facts of record, including a review of relevant state statutes, the Board finds that all conditions for an interstate acquisition enumerated in sec-

1. 12 U.S.C. § 1842.

2. FAB would relocate the bank's main office to Dallas and change its name to Citibank Texas, National Association ("Citibank Texas") before the proposed acquisition by Citigroup. FAB's application to convert to a national charter was approved by the Office of the Comptroller of the Currency ("OCC") on February 15, 2005. The Board consulted with the OCC and the Federal Deposit Insurance Corporation ("FDIC"), the primary supervisor of FAB, regarding their reviews of the proposal.

3. Asset data and nationwide ranking data for Citigroup are as of December 31, 2004.

4. Deposit data are as of June 30, 2004, and reflect the unadjusted total of deposits reported by each organization's insured depository institutions in the Summary of Deposits. In this context, insured depository institutions include commercial banks, savings banks, and savings associations.

5. Citigroup's subsidiary insured depository institutions include Citibank, N.A., New York, New York ("Citibank"); Citibank (West), FSB, San Francisco, California; Citibank, Federal Savings Bank, Reston, Virginia; Citibank (South Dakota), National Association, Sioux Falls, South Dakota; California Commerce Bank, Century City, California; Citicorp Trust Bank, FSB, Newark, Delaware; Citibank (Nevada), National Association, Las Vegas, Nevada; Citibank USA, National Association, Sioux Falls, South Dakota; Citibank (Delaware), New Castle, Delaware; Associates Capital Bank, Inc., Salt Lake City, Utah; and Universal Financial Corp., Salt Lake City, Utah.

6. Citigroup proposes to acquire five of FAB's twelve subsidiaries, including FAB Holdings GP, LLC; FAB Holdings LP, LLC; FAB Financial, LP; SALSCO Inc.; and SB Plano Corporation. Each is currently a subsidiary of FAB and will become a subsidiary of Citibank Texas. All activities conducted by these subsidiaries are permissible for subsidiaries of a national bank. All other FAB subsidiaries will be transferred to TACG before the acquisition.

7. *See* 12 U.S.C. § 1842(d). A bank holding company's home state is the state in which the total deposits of all subsidiary banks of the company were the largest on the later of July 1, 1966, or the date on which the company became a bank holding company. 12 U.S.C. § 1841(o)(4)(C).

8. For purposes of section 3(d), the Board considers a bank to be located in the states in which the bank is chartered or headquartered or operates a branch. *See* 12 U.S.C. §§ 1841(o)(4)–(7), 1842(d)(1)(A) & (B).

tion 3(d) of the BHC Act are met in this case.[9] In light of all the facts of record, the Board is permitted to approve the proposal under section 3(d) of the BHC Act.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or that would be in furtherance of an attempt to monopolize the business of banking. The BHC Act also prohibits the Board from approving a bank acquisition that would substantially lessen competition in any relevant banking market, unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[10]

Citigroup and FAB do not compete directly in any relevant banking market. Based on all the facts of record, the Board has concluded that consummation of the proposed transaction would have no significantly adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive factors are consistent with approval.

Financial, Managerial, and Other Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and depository institutions involved in the proposal and certain other supervisory factors. In reviewing these factors, the Board has considered, among other things, confidential reports of examination and other supervisory information received from the primary federal supervisors of the organizations involved, including the Federal Reserve System's confidential supervisory information. In addition, the Board has consulted with the relevant supervisory agencies, including the OCC, OTS, FDIC, Securities and Exchange Commission ("SEC"), and Texas Savings and Loan Department. The Board also has considered publicly available financial and other information on the organizations and their subsidiaries, all the information submitted on the financial and managerial aspects of the proposal by Citigroup, and public comments received by the Board about the financial and managerial resources of Citigroup.

In evaluating financial factors in expansion proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary banks and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the effect of the transaction on the financial condition of the applicant and the target, including their capital positions, asset quality, and earnings prospects and the impact of the proposed funding of the transaction.

The Board has reviewed these factors carefully in this case and believes financial factors are consistent with approval of this application. The Board notes that Citigroup and its subsidiary depository institutions are well capitalized and would remain so on consummation of the proposal. The Board also finds that Citigroup has sufficient financial resources to effect the proposal. The proposed transaction is structured as a cash purchase of the outstanding shares of FAB, and Citigroup would not directly incur any debt to finance the proposed transaction.

In addition, the Board has considered the managerial resources of Citigroup and FAB, particularly the supervisory experience and assessments of management by the various bank supervisory agencies and the organizations' records of compliance with applicable banking laws.[11] In reviewing this proposal, the Board has assembled and considered a broad and detailed record, including substantial confidential and public information about Citigroup. The Board has carefully reviewed the examination records of Citigroup, FAB, and their subsidiaries, including assessments of their risk-management systems. The Board also considered information from ongoing examinations, the publicly disclosed investigations that are underway, and consultations with other federal and state banking authori-

9. 12 U.S.C. §§1842(d)(1)(A) & (B), 1842(d)(2)(A) & (B). Citigroup is adequately capitalized and adequately managed, as defined by applicable law. FAB has been in existence and operated for the minimum period of time required by applicable law. On consummation of the proposal, Citigroup would control less than 10 percent of the total amount of deposits of insured depository institutions in the United States and less than 30 percent of the total amount of deposits of insured depository institutions in Texas. All other requirements under section 3(d) of the BHC Act also would be met on consummation of the proposal.

10. *See* 12 U.S.C. § 1842(c)(1).

11. A commenter asserted that management of Citigroup is inadequate because it indirectly supports allegedly abusive lending practices through warehouse lending and securitization activities of its subsidiary, Citigroup Global Markets, Inc. ("CGMI"), that support unaffiliated third parties engaged in subprime lending, check cashing, auto-title lending, and operating pawnshops. The commenter also contended that FAB has relationships with these nontraditional providers of financial services that allegedly harm consumers. Citigroup indicated that CGMI engages in underwriting securities backed by subprime mortgage loans and provides warehouse loans to some mortgage banking customers for which it underwrites securities. Citigroup stated that CGMI does not control the origination of subprime loans made by unaffiliated mortgage banking customers or participate in the credit decisions of these customers. Citigroup also stated that CGMI reviews each lender's policies and procedures and sets eligibility criteria for the loans it will finance through its warehouse lending and securitization arrangements. CGMI, or an outside firm hired and supervised by CGMI, reviews a sample of any loan pool to be securitized for compliance with consumer protection laws and its loan eligibility criteria before making any warehouse loan advance. With regard to its business relationships with unaffiliated subprime lenders and nontraditional providers of financial services, Citigroup plays no role in the credit review or other lending or service practices of these entities. The nontraditional providers of financial services are licensed by the states where they operate and are subject to applicable state law.

ties, foreign financial supervisory authorities, the SEC, and other relevant regulators. The Board also reviewed confidential supervisory information on the policies, procedures, and practices of Citigroup to comply with the Bank Secrecy Act and other anti-money-laundering laws and consulted with the OCC, the appropriate federal financial supervisory agency of Citibank, concerning its record of compliance with anti-money-laundering laws.[12]

In evaluating the managerial resources of a banking organization in an expansion proposal, the Board considers assessments of an organization's risk management—the ability of the organization's board of directors and senior management to identify, measure, monitor, and control risk—to be especially important.[13] In evaluating Citigroup's and other banking organizations' risk management, the Board considers a variety of areas, including the following matters: (1) board and senior management oversight of the organization's inherent risks, as well as the general capabilities of management; (2) the adequacy of the organization's policies, procedures, and limits, including the organization's accounting and risk-disclosure policies and procedures; (3) the risk-monitoring and management-information systems used by an organization to measure risk, and the consistency of these tools with the level of complexity of the organization's activities; and (4) the adequacy of the organization's internal controls and audit procedures, including the accuracy of financial reporting and disclosure, the independence of control areas from management, and the consistency of the scope of coverage of the internal audit team with the complexity of the organization.[14] The Board has also taken into account that an organization as large and varied as Citigroup has a particular need to adopt risk-management practices that can appropriately address the scope, complexity, and geographic diversity of its operations.

In assessing these matters, the Board has also taken into account recent publicly disclosed deficiencies and investigations involving Citigroup's activities in Japan, in Europe, and in its mutual fund relationships in the United States. The Board continues to monitor the investigations of Citigroup's securities-related activities that are being conducted by its functional regulators, including the SEC, and is consulting with these authorities. In addition, the Board continues to monitor the investigations regarding Citigroup's bond trades in Europe and its private banking and other activities in Japan. The Board is consulting with the relevant foreign authorities on these matters. The Federal Reserve Bank of New York and the OCC also have conducted targeted examinations of Citigroup's Japanese operations.[15]

Citigroup has acknowledged that it has some deficiencies in its compliance and internal controls in these areas and has developed plans that it has already begun to implement to address the weaknesses. The Board has given careful attention to the measures that Citigroup and its subsidiaries have taken to address these matters and the steps it is continuing to take to resolve these matters and strengthen the company's compliance risk-management structure and practices.[16] Importantly, Citigroup has demonstrated a willingness and ability to take actions to address concerns raised in these investigations and in the examination process. The Board notes that Citigroup recently has significantly increased its funding of compliance risk-management programs and technology, and is in the process of implementing various initiatives designed to strengthen compliance risk management, increase ethics awareness and encourage compliance, and enhance the oversight of its international operations.

As part of Citigroup's plan to enhance its existing compliance risk management and to address compliance issues, Citigroup has strengthened the independence of its compliance structure. The reporting relationship between compliance personnel and business-line management has been changed so that all compliance personnel now have a direct reporting line to the independent compliance function. In addition, Citigroup is in the process of implementing enhanced compliance policies and procedures; management information and reporting systems; monitoring and surveillance programs; and firm-wide and business-specific compliance training for its employees and compliance personnel. Finally, Citigroup is in the process of expanding its audit coverage of the compliance function.

Citigroup has also reviewed and standardized its performance appraisal process to incorporate increased incen-

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12. A commenter criticized the managerial resources of Citigroup and its subsidiaries based on press reports alleging that Citibank and other subsidiaries of Citigroup held accounts for certain international leaders the commenter believed were associated with terrorism. The commenter asserted, based only on information in press reports, that Citigroup lacks sufficient policies and procedures and other resources to prevent money laundering.

13. *See* Revisions to Bank Holding Company Rating System, 69 *Federal Register* 70,444 (2004).

14. *Id.* at 70,447.

15. As a matter of practice and policy, the Board generally has not tied consideration of an application or notice to the scheduling or completion of an examination or investigation if the applicant has an overall satisfactory record of performance and the issues being reviewed may be resolved in the examination and supervisory process. *See* 62 *Federal Register* 9290 (1997) (Preamble to the Board's Regulation Y). As the Board has indicated previously, it has broad supervisory authority under the banking laws to address matters that are found in the examination and supervisory process. Moreover, many issues are more appropriately and adequately addressed in the supervisory process, where particular matters and violations of law may be identified and addressed specifically, rather than in the application process, which requires a weighing of the overall record of the companies involved.

16. The commenter also asserted that Citigroup's management had not implemented effective policies and programs to address alleged abusive sales and lending practices of Citigroup's subsidiaries, including those engaged in subprime lending and related insurance activities, and that the Board's enforcement action against Citigroup and its subsidiary subprime lender, CitiFinancial Credit Company ("CitiFinancial"), Baltimore, Maryland, indicated that Citigroup's managerial resources are inadequate. *See Enforcement Actions,* 90 *Federal Reserve Bulletin* 348–349 (2004) ("Consent Order"). The Board has taken into account the Consent Order and the progress that Citigroup and CitiFinancial currently are making to comply with the Consent Order.

tives for compliance. It has introduced an enhanced corporate-wide ethics awareness program with an expanded orientation program and annual training sessions. Top corporate officials are taking an active role in this ethics program by spearheading regional meetings, conference calls, and site visits.

To ensure that the shortcomings associated with its oversight and the management structure of its Japanese operations are not prevalent in its international operations, Citigroup conducted reviews of its franchise in key global markets and met with regulators to identify any concerns that may exist with regard to corporate governance and compliance. As a result of this review, Citigroup has taken steps designed to clarify accountability and responsibility and to enhance oversight of its international operations.

In addition, the Board has considered the nature of the proposal in this case. This transaction is small relative to Citigroup's U.S. retail banking operations. The Board has also considered the strength and success of Citigroup's managerial resources in operating its retail banking business in the U.S.

Based on these and all the facts of record, including a careful review of public comments, Citigroup's management record, its risk-management programs, the actions taken by Citigroup to address compliance concerns, and the nature of the transaction at hand, the Board concludes that considerations relating to the managerial resources of Citigroup, FAB, and their subsidiaries are consistent with approval of the proposal, as are the other supervisory factors that the Board must consider under section 3 of the BHC Act.[17] The Board expects Citigroup management to continue its efforts to implement fully the improvements it has developed to enhance all aspects of its oversight of the organization's operations. The Board will continue to monitor closely Citigroup's implementation of its plan for enhancing its compliance programs and its progress in meeting the schedule it has set out for implementing that plan.

Given the size, scope, and complexity of Citigroup's global operations, successfully addressing the deficiencies in compliance risk management that have given rise to a series of adverse compliance events in recent years will require significant attention over a period of time by Citigroup's senior management and board of directors. The Board expects that management at all levels will devote the necessary attention to implementing its plan fully and effectively and will not undertake significant expansion during the implementation period. The Board believes it important that management's attention not be diverted from these efforts by the demands that mergers and acquisitions place on management resources. In this application, the Board has determined that demands on managerial resources from this proposal would not be so significant as to divert management from implementing its improvement programs.

Based on all the facts of record, the Board has concluded that the financial and managerial resources and future prospects of the organizations and the other supervisory factors involved are consistent with approval of the proposal.

Convenience and Needs Considerations

In acting on a proposal under section 3 of the BHC Act, the Board is required to consider the effects of the proposal on the convenience and needs of the communities to be served and to take into account the records of the relevant insured depository institution under the Community Reinvestment Act ("CRA").[18] The CRA requires the federal financial supervisory agencies to encourage financial institutions to help meet the credit needs of local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account an institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank expansionary proposals.

A. CRA Performance Evaluations

As provided in the CRA, the Board has evaluated the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the CRA performance records of the relevant insured depository institutions. An institution's most recent CRA performance evaluation is a particularly important consideration in the application process because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisor.[19]

Citigroup's subsidiary depository institutions received either "outstanding" or "satisfactory" ratings at their most recent CRA performance evaluations.[20] Citibank, the lead subsidiary depository institution of Citigroup, received an "outstanding" rating from the OCC, as of June 9, 2003 ("2003 Evaluation"). FAB received a "satisfactory" rating at its most recent CRA performance evaluation by the FDIC, as of June 3, 2002. Citigroup has indicated that it would continue its CRA-related loan, investment, grant, and service programs and fair lending policies at the combined entity after consummation.

17. The commenter expressed concern that Citigroup has helped to finance various activities and projects worldwide that might damage the environment or cause other social harm. These contentions contain no allegations of illegality or action that would affect the safety and soundness of the institutions involved in the proposal and are outside the limited statutory factors that the Board is authorized to consider when reviewing an application under the BHC Act. *See Western Bancshares, Inc. v. Board of Governors*, 480 F.2d 749 (10th Cir. 1973).

18. 12 U.S.C. §2901 *et seq.*

19. *See Interagency Questions and Answers Regarding Community Reinvestment*, 66 *Federal Register* 36,620 and 36,639 (2001).

20. The CRA ratings of all Citigroup's subsidiary depository institutions are provided in the Appendix.

B. CRA Performance of Citibank

Citibank received an "outstanding" rating under the lending, investment, and service tests in the 2003 Evaluation.[21] The examination stated that Citibank had good lending activity in its primary assessment areas, good geographic distribution of loans, and excellent distribution of loans by borrower income. Examiners commended Citibank's use of innovative and flexible mortgage loan products. Citibank, in connection with Fannie Mae, state banking agencies, and nonprofit organizations, such as ACORN, developed several programs for first-time homebuyers and LMI borrowers. Many of these programs, including CRA Portfolio Sub-Allocation and the Enhanced Fannie Neighbors with Community Homebuyers Program, allow for more flexible underwriting standards and reduced down payments. The examiners commended Citibank's small business lending and noted that Citibank was the leading small business lender in the New York City assessment area, with 23 percent of the market share of small business loans.[22]

In addition, the examiners reported that Citibank's community development lending in the New York City assessment area was excellent. They found that Citibank originated a high number and dollar amount of community development loans and that these loans exhibited complexity and innovativeness. Examiners noted that Citibank offered a wide range of financing alternatives to nonprofit and for-profit entities that supported community development initiatives, including the acquisition and rehabilitation of affordable housing units.

Additionally, examiners found that Citibank had an excellent level of community development investments during the evaluation period. For example, in the New York City assessment area, Citibank made or purchased approximately $165 million in qualified investments during the evaluation period. These investments supported affordable housing initiatives for LMI individuals and families, projects that benefited specific LMI populations, and projects that improved deteriorating or mismanaged occupied buildings. Further, the examiners stated that Citibank was a leader in providing community development services that were responsive to the needs of the bank's assessment areas.

C. HMDA and Fair Lending Record

The Board has carefully considered the lending record of Citigroup in light of public comment received on the proposal. A commenter alleged that Citigroup engages in discriminatory lending by directing minority customers to CitiFinancial or other Citigroup subsidiaries that originate subprime loans, rather than to Citigroup's subsidiary banks and other prime lending channels.[23] The commenter also alleged, based on a review of 2003 HMDA data, that the denial disparity ratios of some of the Citigroup Prime Lenders in certain markets indicated that these lenders disproportionately denied African-American or Hispanic applicants for home mortgage loans.[24] Citigroup stated that it does not direct customers to any specific subsidiary based on race or ethnicity criteria and that it provides subprime loans through certain subsidiaries as part of a group of products designed to meet a broad range of credit needs.

The Board reviewed HMDA data reported by the Citigroup Prime Lenders and the Citigroup Subprime Lenders in the primary assessment areas of the Citigroup Prime Lenders and in the other MSAs identified by the commenter.[25] An analysis of 2003 HMDA data does not support the contention that the Citigroup Prime Lenders have disproportionately denied applications of minority or LMI customers, or directed minority or LMI borrowers to its subprime lenders. The HMDA data for the Citigroup Prime Lenders indicate that their denial disparity ratios for African-American and Hispanic applicants were generally higher than the ratios for the aggregate of all lenders ("aggregate lenders") in the MSAs reviewed.[26] However, the origination rates for total HMDA-reportable loans to African-American and Hispanic borrowers by the

21. The evaluation period was from October 18, 2000, to June 9, 2003.

22. The small business lending performance reviewed by examiners included data from the following affiliates of Citibank: Citibank, Federal Savings Bank; Citibank (South Dakota), National Association; Associates Capital Bank, Inc.; Citibank (Nevada), National Association.; Citibank USA, National Association; and Universal Financial Corp. For purposes of this analysis, small business loans included business loans with an original amount of $1 million or less.

23. Specifically, the commenter's allegations were based on 2003 data reported pursuant to the Home Mortgage Disclosure Act, 12 U.S.C. §2801 *et seq.* ("HMDA"), by certain Citigroup subsidiaries engaged in conventional mortgage lending in the New York, New York; Nassau/Suffolk, New York; Chicago, Illinois; Los Angeles, California; Washington, D.C., and Newark, New Jersey Metropolitan Statistical Areas ("MSAs"). In addition, the commenter criticized Citigroup's lending record in the Houston and Dallas MSAs, where Citigroup's subsidiary depository institutions have no branches. The commenter also asserted, without analysis, that CitiFinancial originated a higher volume and larger percentage of its HMDA-reportable loans to African-American or Hispanic borrowers than Citigroup's conventional mortgage lending subsidiaries originated in the MSAs noted by the commenter. For purposes of this application, the Board analyzed 2002 and 2003 HMDA data in Citigroup's CRA assessment areas in these MSAs, the San Francisco–San Mateo–Redwood City, California MSA, and the State of New York that was reported by Citibank; CitiMortgage, Inc., St. Louis, Missouri; Citibank, Federal Savings Bank; and Citibank (West), FSB (collectively, "Citigroup Prime Lenders"). Citibank (West), FSB is the successor to California Federal Bank, San Francisco, California. For purposes of this review, information relating to Citibank (West), FSB included California Federal Bank's data. The Board also reviewed 2003 HMDA data reported by CitiFinancial; Citicorp Trust Bank, FSB; and CitiFinancial Mortgage Company, Inc., Irving, Texas (collectively, "Citigroup Subprime Lenders").

24. The denial disparity ratio equals the denial rate for a particular racial category (*e.g.*, African-American) divided by the denial rate for whites.

25. In the MSAs reviewed, the Board compared the 2003 HMDA data reported by the Citigroup Prime Lenders with the HMDA data reported by the Citigroup Subprime Lenders.

26. The lending data of the aggregate lenders represent the cumulative lending for all financial institutions that have reported HMDA data in a particular area.

Citigroup Prime Lenders in all but one of the MSAs reviewed were comparable to or higher than the rates for the aggregate lenders.[27] The 2003 HMDA data also show that the Citigroup Prime Lenders extended more total HMDA-reportable loans to African-American and Hispanic borrowers than the Citigroup Subprime Lenders in most of the MSAs reviewed.

Although the HMDA data may reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial groups in certain local areas, the HMDA data do not demonstrate that the Citigroup Prime Lenders are excluding any racial group on a prohibited basis. The Board is concerned when HMDA data for an institution indicate disparities in lending and believes that all banks are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending, but also equal access to credit by creditworthy applicants regardless of their race. The Board recognizes, however, that HMDA data alone provide an incomplete measure of an institution's lending in its community because these data cover only a few categories of housing-related lending. HMDA data, moreover, provide only limited information about the covered loans.[28] HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has not assisted adequately in meeting its community's credit needs or has engaged in illegal lending discrimination. Moreover, HMDA data indicating that one affiliate is lending to minorities more than another affiliate do not, without more information, indicate that either affiliate has engaged in illegal discriminatory lending activities.

Because of the limitations of HMDA data, the Board has considered these data carefully and taken into account other information, including examination reports that provide an on-site evaluation of compliance by Citigroup and its subsidiaries with fair lending laws. Importantly, examiners noted no fair lending issues or concerns in the performance evaluations of Citigroup's subsidiary depository institutions or FAB.

The record also indicates that Citigroup has taken steps to help ensure compliance with fair lending laws and other consumer protection laws. Citigroup has implemented corporate-wide fair lending policies, procedures, and training programs, and it regularly conducts internal reviews for compliance with policies and procedures, including reviews of individual loans and reviews of its subsidiary lenders' overall lending data. Citigroup's subsidiary depository institutions have established detailed fair lending procedures in addition to Citigroup's corporate policies and procedures, including extensive fair lending training programs for employees and fair lending self-assessments using matched-pair testing and statistical analyses. In addition, all declined applications are independently reviewed by two underwriters, the second of whom must be a senior underwriter or risk-management expert. Declined applications go through a third level of review if the applicant is a LMI borrower, is applying for a community lending product, or lives in an LMI or minority census tract.

In addition, Citigroup has taken actions to address deficiencies in CitiFinancial's management of its compliance with consumer protection laws and currently is making progress in complying with the Consent Order.[29] Citigroup is in the process of implementing the restitution plan and changes to its compliance risk-management systems, including audit and training functions, in accordance with the Consent Order's terms. The Board is continuing to monitor Citigroup's compliance with the Consent Order and enhancements to its various real estate lending initiatives to help ensure compliance with consumer protection laws and prevent abusive lending practices by CitiFinancial ("Initiatives"). Citigroup has enhanced these Initiatives by, among other things, implementing new insurance sales practices and introducing mortgage loan products at CitiFinancial that provide qualifying applicants with access to lower-cost mortgage loans. These new loan products offer interest rates that are close to the rates on the conventional mortgage loan products offered by the Citigroup Prime Lenders.

The Board also has considered the HMDA data in light of other information, including the programs described above and the overall performance records of Citigroup's subsidiary depository institutions under the CRA. These established efforts demonstrate that the institutions are active in helping to meet the credit needs of their entire communities.

Conclusion on Convenience and Needs and CRA Performance

The Board has carefully considered all the facts of record, including reports of examination of the CRA performance records of the institutions involved, information provided by Citigroup, comments on the proposal, and confidential supervisory information. The Board notes that the proposal would provide the combined entity's customers with access

27. The origination rate equals the total number of loans originated to applicants of a particular racial category divided by the total number of applications received from members of that racial category.

28. The data, for example, do not account for the possibility that an institution's outreach efforts may attract a larger proportion of marginally qualified applicants than other institutions attract and do not provide a basis for an independent assessment of whether an applicant who was denied credit was, in fact, creditworthy. Credit history problems and excessive debt levels relative to income (reasons most frequently cited for a credit denial) are not available from HMDA data.

29. As the Board previously has noted, subprime lending is a permissible activity that provides needed credit to consumers who have difficulty meeting conventional underwriting criteria. The Board continues to expect all bank holding companies and their affiliates to conduct their subprime lending operations without any abusive lending practices. *See, e.g., Royal Bank of Canada*, 88 *Federal Reserve Bulletin* 385, 388 n.18 (2002). The commenter reiterated concerns raised in previous Citigroup applications and asserted that CitiFinancial engaged in various lending practices that the commenter argued were abusive, unfair, or deceptive. The commenter also contended that the Board should deny this application or impose conditions requested by the commenter in light of the Consent Order entered into by Citigroup in May 2004.

to a broader array of products and services in an expanded service area, including access to an expanded branch and ATM network. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that considerations relating to the convenience and needs factor and the CRA performance records of the relevant depository institutions are consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the application should be, and hereby is, approved.[30] In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act and other applicable statutes.[31] The Board's approval is specifically conditioned on compliance by Citigroup with the conditions imposed in this order and the commitments made to the Board in connection with the application. For purposes of this action, these commitments and conditions are deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

The acquisition of FAB shall not be consummated before the fifteenth calendar day after the effective date of this order or later than three months after the effective date of this order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of New York, acting pursuant to delegated authority.

By order of the Board of Governors, effective March 16, 2005.

Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Bies, Olson, Bernanke, and Kohn. Absent and not voting: Governor Gramlich.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

30. The commenter requested that the Board hold a public meeting or hearing on the proposal. Section 3(b) of the BHC Act does not require the Board to hold a public hearing on an application unless the appropriate supervisory authority for the bank to be acquired makes a timely written recommendation of denial of the application. The Board has not received such a recommendation from the appropriate supervisory authorities. Under its regulations, the Board also may, in its discretion, hold a public meeting or hearing on an application to acquire a bank if a meeting or hearing is necessary or appropriate to clarify factual issues related to the application and to provide an opportunity for testimony. 12 CFR 225.16(e). The Board has considered carefully the commenter's request in light of all the facts of record. In the Board's view, the commenter has had ample opportunity to submit its views and has submitted written comments that have been considered carefully by the Board in acting on the proposal. The commenter's requests fail to demonstrate why written comments do not present its evidence adequately and fail to identify disputed issues of fact that are material to the Board's decision that would be clarified by a public meeting or hearing. For these reasons, and based on all the facts of record, the Board has determined that a public meeting or hearing is not required or warranted in this case. Accordingly, the request for a public meeting or hearing on the proposal is denied.

31. The commenter also requested that the Board delay action or extend the comment period on the proposal. As previously noted, the Board has accumulated a significant record in this case, including reports of examination, confidential supervisory information, public reports and information, and considerable public comment. In the Board's view, for the reasons discussed above, the commenter has had ample opportunity to submit its views and, in fact, has provided substantial written submissions that the Board has considered carefully in acting on the proposal. Moreover, the BHC Act and Regulation Y require the Board to act on proposals submitted under those provisions within certain time periods. Based on a review of all the facts of record, the Board has concluded that the record in this case is sufficient to warrant action at this time, and that further delay in considering the proposal, extension of the comment period, or denial of the proposal on the grounds discussed above or on the basis of informational insufficiency is not warranted.

Appendix

CRA Performance Evaluations of Citigroup

Subsidiary Depository Institution	CRA Rating	Date of Evaluation	Agency
Citibank, N.A., New York, New York	Outstanding	June 9, 2003	OCC
Citibank (West), FSB, San Francisco, California[1]	Outstanding	July 30, 2001	OTS
Citibank, Federal Savings Bank, Reston, Virginia	Outstanding	September 8, 2003	OTS
Citibank (South Dakota), National Association, Sioux Falls, South Dakota	Outstanding	May 5, 2003	OCC
California Commerce Bank, Century City, California	Outstanding	October 1, 2002	FDIC
Citicorp Trust Bank, FSB, Newark, Delaware	Outstanding	February 5, 2001	OTS
Citibank (Nevada), National Association, Las Vegas, Nevada	Outstanding	March 31, 2003	OCC
Citibank USA, National Association, Sioux Falls, South Dakota	Satisfactory	May 5, 2003	OCC
Citibank (Delaware), New Castle, Delaware	Outstanding	December 1, 2003	FDIC
Associates Capital Bank, Inc., Salt Lake City, Utah	Outstanding	March 1, 2000	FDIC
Universal Financial Corp., Salt Lake City, Utah	Outstanding	November 1, 2002	FDIC

1. As noted above, Citibank (West), FSB is the successor to California Federal Bank. The rating shown was received by California Federal Bank.

The Colonial BancGroup, Inc.
Montgomery, Alabama

Order Approving the Acquisition of a Bank

The Colonial BancGroup, Inc. ("BancGroup"), a financial holding company within the meaning of the Bank Holding Company Act ("BHC Act"), has requested the Board's approval under section 3 of the BHC Act[1] to acquire Union Bank of Florida, Lauderhill, Florida ("Union Bank").

Notice of the proposal, affording interested persons an opportunity to comment, has been published in the *Federal Register* (69 *Federal Register* 69,369 (2004)).[2] The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3 of the BHC Act.

BancGroup, with total consolidated assets of approximately $18.2 billion, is the 56th largest depository organization in the United States. BancGroup operates one subsidiary insured depository institution, Colonial Bank, National Association, also in Montgomery ("Colonial Bank"), with branches in Alabama, Florida, Georgia, Nevada, Tennessee, and Texas. BancGroup is the eighth largest depository organization in Florida, controlling deposits of approximately $5.6 billion, which represent approximately 1.9 percent of the total amount of deposits of insured depository institutions in the state ("state deposits").

Union Bank, with total consolidated assets of approximately $1.0 billion, is the 43rd largest insured depository institution in Florida, controlling deposits of approximately $686.7 million. On consummation of the proposal, BancGroup would remain the eighth largest depository organization in Florida, controlling deposits of approximately $6.3 billion, which represent approximately 2.1 percent of state deposits.[3]

Interstate Analysis

Section 3(d) of the BHC Act allows the Board to approve an application by a bank holding company to acquire control of a bank located in a state other than the home state of the bank holding company if certain conditions are met. For purposes of the BHC Act, the home state of

1. 12 U.S.C. § 1842.
2. 12 CFR 262.3(b).

3. Asset data are as of September 30, 2004, and national rankings are as of June 30, 2004. Deposit data and state rankings are as of June 30, 2004, and are adjusted to reflect mergers and acquisitions completed through December 1, 2004.

BancGroup is Alabama.[4] BancGroup proposes to acquire a bank located in Florida.[5]

Based on a review of all the facts of record, including a review of relevant state statutes, the Board finds that all conditions for an interstate acquisition enumerated in section 3(d) of the BHC Act are met in this case.[6] In light of all the facts of record, the Board is permitted to approve the proposal under section 3(d) of the BHC Act.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of an attempt to monopolize the business of banking. The BHC Act also prohibits the Board from approving a bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by its probable effect in meeting the convenience and needs of the community to be served.[7]

BancGroup and Union Bank compete directly in the Miami-Fort Lauderdale and West Palm Beach Area banking markets in Florida.[8] The Board has reviewed carefully the competitive effects of the proposal in each of these banking markets in light of all the facts of record. In particular, the Board has considered the number of competitors that would remain in the markets, the relative shares of total deposits of depository institutions in the markets ("market deposits") controlled by BancGroup and Union Bank,[9] the concentration level of market deposits and the increase in this level as measured by the Herfindahl–Hirschman Index ("HHI") under the Department of Justice Merger Guidelines ("DOJ Guidelines"),[10] and other characteristics of the market.

Consummation of the proposal would be consistent with Board precedent and the DOJ Guidelines in both of these banking markets. After consummation, the Miami–Fort Lauderdale and West Palm Beach Area banking markets would remain moderately concentrated as measured by the HHI. In both markets, the increases in concentration would be small and numerous competitors would remain.[11]

The Department of Justice also has reviewed the anticipated competitive effects of the proposal and advised the Board that consummation of the proposal would not likely have a significant adverse effect on competition in any relevant banking market. In addition, the appropriate banking agencies were afforded an opportunity to comment and have not objected to the proposal.

Based on all the facts of record, the Board concludes that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of resources in either of the two banking markets in which BancGroup and Union Bank directly compete or in any other relevant banking market. Accordingly, based on all the facts of record, the Board has determined that competitive considerations are consistent with approval.

Financial and Managerial Resources and Future Prospects

The Board is also required under section 3(c) of the BHC Act to consider the financial and managerial resources and future prospects of the companies and banks involved in the proposal and to consider certain other supervisory factors. The Board has carefully considered these factors in light of all the facts of record including, among other things, information provided by BancGroup, confidential reports of examination and other supervisory information received from the federal and state banking supervisors of the organizations involved, publicly reported and other financial information, and public comments received on the proposal.

In evaluating financial factors in expansion proposals by banking organizations, the Board reviews the finan-

4. 12 U.S.C. § 1842(d). Under section 3(d) of the BHC Act, a bank holding company's home state is the state in which the total deposits of all banking subsidiaries of such company were the largest on July 1, 1966, or the date on which the company became a bank holding company, whichever is later. 12 U.S.C. § 1841(o)(4)(C).

5. For purposes of section 3(d), the Board considers a bank to be located in states in which the bank is chartered or headquartered or operates a branch. *See* 12 U.S.C. §§ 1841(o)(4)–(7) and 1842(d)(1)(A) & (d)(2)(B).

6. 12 U.S.C. § 1842(d)(1)(A) & (B), 1842(d)(2)(A) & (B). BancGroup is well capitalized and well managed, as defined by applicable law. Union Bank has been in existence and operated for the minimum period of time required by Florida law. On consummation of the proposal, BancGroup would control less than 10 percent of the total amount of deposits of insured depository institutions in the United States and less than 30 percent of the total amount deposits of insured depository institutions in Florida. *See* Fla. Stat. Ch. 658.295(8)(b) (2004). All other requirements under section 3(d) of the BHC Act would be met on consummation of the proposal.

7. 12 U.S.C. § 1842(c)(1).

8. The Miami–Fort Lauderdale market is defined as Broward and Dade Counties. The West Palm Beach Area market is defined as Palm Beach County east of the town of Loxahatchee and the towns of Indiantown and Hobe Sound in Martin County.

9. Deposit and market share data are as of June 30, 2004, adjusted to reflect subsequent mergers and acquisitions through December 1, 2004, and are based on calculations in which the deposits of thrift institutions are included at 50 percent. The Board previously has indicated that thrift institutions have become, or have the potential to become, significant competitors of commercial banks. *See, e.g., Midwest Financial Group*, 75 *Federal Reserve Bulletin* 386 (1989); *National City Corporation*, 70 *Federal Reserve Bulletin* 743 (1984). Thus, the Board regularly has included thrift deposits in the market share calculation on a 50 percent weighted basis. *See, e.g., First Hawaiian, Inc.*, 77 *Federal Reserve Bulletin* 52 (1991).

10. Under the DOJ Guidelines, a market is considered unconcentrated if the post-merger HHI is less than 1000 and moderately concentrated if the post-merger HHI is between 1000 and 1800. The Department of Justice has informed the Board that a bank merger or acquisition generally will not be challenged (in the absence of other factors indicating anticompetitive effects) unless the post-merger HHI is at least 1800 and the merger increases the HHI by more than 200 points. The Department of Justice has stated that the higher than normal HHI thresholds for screening bank mergers for anticompetitive effects implicitly recognize the competitive effects of limited-purpose lenders and other nondepository financial institutions.

11. The effects of the proposal on the concentration of banking resources in these banking markets are described in the Appendix.

cial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary banks and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the effect of the transaction on the financial condition of the applicant and the target, including their capital positions, asset quality, and earnings prospects and the impact of the proposed funding of the transaction.

Based on its review of these factors, the Board finds that BancGroup has sufficient financial resources to effect the proposal. BancGroup and its subsidiary bank are well capitalized and would remain so on consummation of this proposal. BancGroup will acquire all the shares of Union Bank from UB Financial Corporation, Sunrise, Florida, the parent company of Union Bank. The transaction will be funded through a combination of BancGroup common stock and cash raised by BancGroup through a stock issuance.

The Board also has evaluated the managerial resources of the organizations involved, including the proposed combined organization. The Board has reviewed the examination records of BancGroup, Colonial Bank, and Union Bank, including assessments of their management, risk management systems, and operations. In addition, the Board has considered its supervisory experience and that of the other relevant banking supervisory agencies with the organizations and their records of compliance with applicable banking law. BancGroup, Colonial Bank, and Union Bank are considered well managed. The Board also has considered BancGroup's plans to integrate Union Bank and the proposed management, including the risk management systems, of the resulting organization.

Based on all the facts of record, the Board has concluded that the financial and managerial resources and future prospects of the organizations and the other supervisory factors involved are consistent with approval of the proposal.

Convenience and Needs Considerations

In acting on this proposal, the Board is required to consider the effects of the proposal on the convenience and needs of the communities to be served and to take into account the records of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[12] The CRA requires the federal financial supervisory agencies to encourage financial institutions to help meet the credit needs of local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account an institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank expansionary proposals. The Board has considered carefully the convenience and needs factor and the CRA performance records of Colonial Bank and Union Bank in light of all the facts of record.

A. CRA Performance Evaluations

As provided in the CRA, the Board has evaluated the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the CRA performance records of the relevant insured depository institutions. An institution's most recent CRA performance evaluation is a particularly important consideration in the applications process because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisor.[13]

BancGroup's subsidiary depository institution, Colonial Bank, received a "satisfactory" rating at its most recent CRA performance evaluation, as of February 25, 2002, by the Federal Reserve Bank of Atlanta.[14] Union Bank received a "satisfactory" rating at its most recent CRA performance evaluation by the Federal Deposit Insurance Corporation, as of December 2, 2002.

BancGroup has indicated that it would continue Colonial Bank's CRA-related loan, investment, grant, and service programs and fair lending policies at the combined entity after consummation.

B. CRA Performance of Colonial Bank and Union Bank

Colonial Bank. Colonial Bank received an overall rating of "high satisfactory" under the lending test at its most recent CRA performance evaluation. Examiners reported that the bank's lending levels reflected good responsiveness to its assessment areas' credit needs, including a good level of loans reportable under the Home Mortgage Disclosure Act ("HMDA")[15] and loans to businesses with gross annual revenues of $1 million or less. They commended Colonial Bank's level of HMDA-reportable and small business lending in LMI census tracts and the bank's use of innovative and flexible loan programs in serving its assessment areas' credit needs, including several affordable housing loan programs. The evaluation also found that Colonial Bank made a relatively high level of community development loans, totaling $38.2 million, in its assessment areas during the evaluation period.[16] Colonial Bank represented

12. 12 U.S.C. § 2901 *et seq.*

13. *See Interagency Questions and Answers Regarding Community Reinvestment,* 66 *Federal Register* 36,620 and 36,639 (2001).

14. At that time, Colonial Bank was a state-chartered member bank of the Federal Reserve System. Colonial Bank converted to a national bank charter in 2003.

15. 12 U.S.C. § 2801 *et seq.*

16. The evaluation period was from January 1, 2000, to December 31, 2001.

that since the examination, it has originated approximately $263 million in qualified community development loans in its assessment areas.

Colonial Bank also received overall ratings of "high satisfactory" under the investment and service tests. Examiners reported that the bank made a significant level of qualified community development investments and grants, and found that Colonial Bank's systems for delivering retail banking services were accessible essentially to all segments of the bank's assessment areas. Examiners also found that the bank provided a relatively high level of community development services throughout its assessment areas and specifically noted that these services were highly responsive to affordable housing needs.

Union Bank. As previously noted, Union Bank received a "satisfactory" rating at its most recent CRA performance evaluation. Examiners found that Union Bank's overall lending activity demonstrated an adequate responsiveness to the credit needs of its assessment areas, and that the geographic distribution of the bank's loans and its community development lending activity were also adequate.[17] They reported that the bank's level of qualified community development investments within its assessment areas was very good. Examiners also favorably noted that Union Bank's retail banking delivery systems were reasonably accessible to essentially all portions of its assessment areas.

C. HMDA and Fair Lending Record

The Board's review of the record in this case included a review of HMDA data reported by Colonial Bank. Although the HMDA data may reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial groups in certain local areas, the HMDA data generally do not indicate that Colonial Bank is excluding any racial group or geographic area on a prohibited basis.[18]

Because of the limitations of HMDA data, the Board has considered these data carefully in light of other information, including examination reports that provide an on-site evaluation of compliance by Colonial Bank with fair lending laws and the CRA performance records of Colonial Bank and Union Bank that are detailed above. Importantly, examiners noted no fair lending issues or concerns in the performance evaluations of Colonial Bank or Union Bank. These established efforts demonstrate that, on balance, the records of performance of Colonial Bank and Union Bank in meeting the convenience and needs of their communities are consistent with approval of this proposal. The record in this case also reflects an opportunity for Colonial Bank to improve its mortgage lending to African-American borrowers in its communities. Colonial Bank has recognized the need to improve its lending in this regard and is in the process of establishing objectives and strategies for improved performance, particularly for lending to minorities and in predominantly minority census tracts. The Board expects that Colonial Bank will continue to take steps to improve its mortgage lending performance to African-American borrowers.

D. Conclusion on Convenience and Needs and CRA Performance

The Board has carefully considered all the facts of record, including reports of examination of the CRA performance records of the institutions involved, information provided by BancGroup, and confidential supervisory information. The Board notes that the proposal would provide the combined entity's customers with access to a broader array of products and services in expanded service areas, including access to expanded branch and automated teller machine networks. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that considerations relating to the convenience and needs factor and the CRA performance records of the relevant depository institutions are consistent with approval.

Conclusion

Based on the foregoing and all facts of record, the Board has determined that the application should be, and hereby is, approved. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act. The Board's approval is specifically conditioned on compliance by BancGroup with the condition imposed in this order and the commitments made to the Board in connection with the application. For purposes of this transaction, the condition and these commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

The proposed transaction may not be consummated before the fifteenth calendar day after the effective date of this order, or later than three months after the effective date of this order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of Atlanta, acting pursuant to delegated authority.

By order of the Board of Governors, effective January 25, 2005.

Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Gramlich, Bies, Olson, Bernanke, and Kohn.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

17. The evaluation period was from January 1, 2001, to October 31, 2002.

18. The Board recognizes, however, that HMDA data alone provide an incomplete measure of an institution's lending in its community because these data cover only a few categories of housing-related lending and provide only limited information about the covered loans. HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has not assisted adequately in meeting its community's credit needs or has engaged in illegal lending discrimination.

Appendix

Banking Market Data

Miami–Fort Lauderdale, Florida

BancGroup is the 11th largest depository institution in the Miami–Fort Lauderdale market, controlling $1.5 billion in deposits, which represents approximately 1.8 percent of market deposits. Union Bank is the 21st largest depository institution in the market, controlling $627.1 million in deposits, which represents less than 1 percent of market deposits. On consummation of the proposal, BancGroup would be the ninth largest depository institution in the Miami–Fort Lauderdale market, controlling approximately $2.1 billion in deposits, which would represent approximately 2.5 percent of market deposits. The HHI for the Miami–Fort Lauderdale market would increase 2 points to 1029, and 99 other bank and thrift competitors would remain in the market.

West Palm Beach Area, Florida

BancGroup is the 11th largest depository institution in the West Palm Beach Area market, controlling $452.0 million in deposits, which represents approximately 1.8 percent of market deposits. Union Bank is the 36th largest depository institution in the market, controlling $59.6 million in deposits, which represents less than 1 percent of market deposits. On consummation of the proposal, BancGroup would be the ninth largest depository institution in the West Palm Beach Area market, controlling approximately $511.6 million in deposits, which would represent approximately 2.1 percent of market deposits. The HHI for the West Palm Beach Area market would increase 1 point to 1422, and 59 other bank and thrift competitors would remain in the market.

Synovus Financial Corp.
Columbus, Georgia

Order Approving the Acquisition of a Bank

Synovus Financial Corp. ("Synovus"), a bank holding company within the meaning of the Bank Holding Company Act ("BHC Act"), has requested the Board's approval under section 3 of the BHC Act[1] to acquire all the voting shares of Cohutta Banking Company of Tennessee, Chattanooga, Tennessee ("CBCT"), a de novo state chartered bank.[2] After consummation of the proposal, Synovus will operate CBCT as a separate subsidiary bank.

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (69 *Federal Register* 59,229 (2004)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 3 of the BHC Act.

Synovus, with total consolidated assets of $23.6 billion, is the 47th largest depository organization in the United States, controlling $17.5 billion of deposits, which represents less than 1 percent of the total deposits in insured depository institutions in the United States.[3] In Tennessee, Synovus is the 16th largest depository organization, and its subsidiary depository institutions have approximately $1.1 billion in combined assets and $720.3 million in combined deposits. Synovus operates 40 subsidiary insured depository institutions in Alabama, Florida, Georgia, South Carolina, and Tennessee, as well as a nondepository trust company in Georgia.

Interstate Analysis

Section 3(d) of the BHC Act allows the Board to approve an application by a bank holding company to acquire control of a bank located in a state other than the bank holding company's home state if certain conditions are met. For purposes of the BHC Act, the home state of Synovus is Georgia,[4] and CBCT is located in Tennessee.[5]

Based on a review of all the facts of record, including relevant state statutes, the Board finds that all conditions for an interstate acquisition enumerated in section 3(d) are met in this case.[6] In light of all the facts of record, the Board is permitted to approve the proposal under section 3(d) of the BHC Act.

1. 12 U.S.C. § 1842.

2. Under Tennessee branching law, one of Synovus's Tennessee-chartered subsidiary banks established a phantom branch in Chattanooga, and the organizers and proposed management of CBCT filed an application to charter the branch as a de novo institution (CBCT). The Tennessee Department of Financial Institutions ("TDFI") approved CBCT's charter on October 20, 2004, and the Federal Deposit Insurance Corporation ("FDIC") granted CBCT deposit insurance on October 22. Synovus also has filed applications to acquire CBCT that must be approved by the FDIC, TDFI, and the Georgia Department of Banking and Finance.

3. Asset, deposit, nationwide, and statewide ranking data are as of June 30, 2004. In this context, depository institutions include commercial banks, savings banks, and savings associations.

4. *See* 12 U.S.C. § 1842(d). A bank holding company's home state is the state in which the total deposits of all banking subsidiaries of such company were the largest in July 1, 1966, or the date on which the company became a bank holding company, whichever is later.

5. For purposes of section 3(d), the Board considers a bank to be located in states in which the bank is chartered or headquartered or operates a branch. *See* 12 U.S.C. §§ 1841(o)(4)–(7) and 1842(d)(1)(A) and (d)(2)(B).

6. *See* 12 U.S.C. §§ 1842(d)(1)(A)–(B) and 1842(d)(2)(A)–(B). Synovus is adequately capitalized and adequately managed, as defined by applicable law. Although Tennessee law generally prohibits the acquisition of a bank that has been in operation less than five years, the state's provisions on branch banking provide an exception to this prohibition for transactions structured like Synovus's proposal. *See* TENN. CODE ANN. §§ 45-2-1403 and 45-2-614(c) (2000). On consummation of the proposal, Synovus and its affiliates would control less than 10 percent of the total amount of deposits in insured depository institutions in the United States and less than 30 percent of the total amount of deposits of insured depository institutions in Tennessee. *See* TENN. CODE ANN. § 45-2-1404. All other requirements under section 3(d) of the BHC Act also would be met on consummation of the proposal.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking. The BHC Act also prohibits the Board from approving a bank acquisition that would substantially lessen competition in any relevant banking market, unless the Board finds that the anticompetitive effects are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[7]

The proposal involves the formation and acquisition of a de novo bank in the Chattanooga Area banking market,[8] which would expand Synovus's operations in the market[9] and increase its ability to offer products and services to customers in that market. The Board previously has noted that the establishment of a de novo bank enhances competition in the relevant banking market and is a positive consideration in an application under section 3 of the BHC Act.[10] There is no evidence that the proposal would create or further a monopoly or lessen competition in any relevant market. Accordingly, the Board concludes, based on all the facts of record, that consummation of the proposal would not result in any significantly adverse effects on competition or on the concentration of banking resources in any relevant banking market and that competitive considerations are consistent with approval.

Financial, Managerial, and Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and banks involved in the proposal and certain other supervisory factors. The Board has considered carefully these factors in light of all the facts of record, including confidential reports of examination, other confidential supervisory information from the primary federal supervisors of the organizations involved in the proposal and certain other agencies, publicly reported information and other financial information, information provided by Synovus, and public comment on the proposal.[11]

In evaluating the financial factors in expansion proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis and the financial condition of the subsidiary banks and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the financial condition of the combined organization on consummation, including its capital position, asset quality, earnings prospects, and the impact of the proposed funding of the transaction.

Based on its review of these factors, the Board finds that Synovus has sufficient financial resources to effect the proposal. Synovus will use existing cash resources to purchase CBCT's shares and capitalize the bank. Synovus is well capitalized and will remain so on consummation of the proposal, and CBCT will be well capitalized.

The Board has considered the managerial resources of Synovus in light of its supervisory experiences and those of the other relevant federal and state banking supervisors with the organization and its subsidiary banks and their records of compliance with applicable banking laws. The Board has reviewed the examination records of the Synovus organization, including assessments of its management, risk management systems, and operations. Synovus and its subsidiary depository institutions are considered well managed. The Board also has reviewed the proposed management, risk management systems, and operations of CBCT and consulted with the FDIC and TDFI.

Based on all the facts of record, the Board has concluded that considerations relating to the financial and managerial resources and future prospects of Synovus and CBCT are consistent with approval, as are the other supervisory factors under section 3 of the BHC Act.

Convenience and Needs Considerations

In acting on this proposal, the Board also must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[12] The CRA requires the federal financial supervisory agencies to encourage financial institutions to help meet the credit needs of the local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account a depository institution's record of meeting

7. 12 U.S.C. § 1842(c)(1).

8. The Chattanooga Area banking market is defined as Hamilton and Marion Counties, excluding the portion of the town of Monteagle that is outside Marion County, all in Tennessee; and Catoosa, Dade, and Walker Counties in Georgia.

9. Synovus, through The Cohutta Banking Company, Chatsworth, Georgia, has two branches in the Chattanooga Area banking market with $60.4 million in total deposits. Synovus ranks 17th in the market with less than 1 percent of the total deposits in depository institutions in the market.

10. *See Canadian Imperial Bank of Commerce*, 85 *Federal Reserve Bulletin* 733 (1999); *Wilson Bank Holding Company*, 82 *Federal Reserve Bulletin* 568 (1996).

11. A commenter expressed concern over press reports about an investigation of Synovus's credit-card processing company subsidiary and one of its clients for possible violations of federal law in connection with mailings on behalf of that client. The investigation concerns compliance with U.S. Postal Service ("USPS") regulations that authorize discounted postal rates subject to certain mailing list requirements. This matter is not within the Board's jurisdiction to adjudicate. The Board has consulted with the USPS and the Department of Justice about the matter.

12. 12 U.S.C. § 2901 *et seq.*; 12 U.S.C. § 1842(c)(2).

the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank expansionary proposals.

The Board has carefully considered the convenience and needs factor and the CRA performance records of Synovus's subsidiary banks in light of all the facts of record, including public comment on the proposal. A commenter opposing the proposal alleged, based on data reported under the Home Mortgage Disclosure Act ("HMDA"),[13] that Synovus Mortgage Corp., Birmingham, Alabama ("SMC"), Synovus's indirect subsidiary mortgage lending company,[14] engaged in disparate treatment of African Americans in home mortgage lending in certain markets.[15]

As previously noted, CBCT is in formation and has not begun operations. CBCT was required to submit a comprehensive CRA plan to the FDIC in connection with its charter application, and the FDIC considered the CRA plan in granting preliminary approval of the bank's state charter. CBCT's plan indicates that the bank intends to lend to small- and medium-sized businesses, including those in LMI census tracts; engage in mortgage and other consumer lending activities; and provide a variety of banking, trust, brokerage, and insurance services. Synovus represented that CBCT will implement Synovus's centralized CRA policies and procedures to help ensure that the existing and anticipated credit needs of CBCT's community are met. The FDIC will evaluate the implementation of CBCT's CRA plan in future CRA performance evaluations of the bank.

A. CRA Performance Evaluations

As provided in the CRA, the Board has evaluated the convenience and needs factor in light of examinations of the CRA performance records of Synovus's subsidiary insured depository institutions by the appropriate federal supervisors.[16] Each of Synovus's subsidiary depository institutions received "outstanding" or "satisfactory" ratings at their most recent performance examinations. CB&T, Synovus's lead bank, received an overall "satisfactory" rating at its most recent CRA performance evaluation by the FDIC, as of January 14, 2002.

CB&T received a "high satisfactory" rating under the lending, investment, and service tests.[17] Examiners noted that although CB&T considered itself to be primarily a commercial lender, it offered a full range of products and services to individuals in its assessment areas. They found that CB&T's lending activity demonstrated a good responsiveness to community credit needs. Examiners noted that the bank offered innovative and flexible lending programs, including various products designed to meet the needs of small businesses owned by minorities or women; different loan products sponsored by the Small Business Administration; and alternative home mortgage loan products through its affiliate, SMC, for borrowers who did not qualify for its conventional mortgage loans.

Examiners reported that CB&T was the leading lender in 2000, by number and dollar volume of small business loans and small farm loans in the bank's assessment area.[18] CB&T originated small business loans totaling approximately $153 million and small farm loans totaling approximately $6.9 million in its assessment area. Examiners noted the bank's geographic distribution of all its loans reflected adequate penetration and that its distribution of loans based on borrower income was good. More than 80 percent of its small business loan originations by number and dollar volume were to businesses with gross annual revenues of $1 million or less, and more than 96 percent of its small farm loan originations were to farms with gross annual revenues of $1 million or less. In addition, the bank originated more than 19 percent of its home mortgage loans to LMI borrowers.

Examiners noted that CB&T's level of community development lending was adequate and reflected the bank's limited opportunities to participate in community development projects in its assessment area. During the evaluation

13. 12 U.S.C. § 2801 *et seq.*

14. SMC is a subsidiary of First Commercial Bank, also in Birmingham and an indirect subsidiary bank of Synovus.

15. The commenter also asserted that Synovus's lead subsidiary bank, Columbus Bank and Trust ("CB&T"), Columbus, controls the operations of CompuCredit Corporation ("CompuCredit"), Atlanta, both in Georgia, a third-party organization that engages in subprime credit-card and payday lending. CB&T and CompuCredit offer a co-branded credit card program ("credit card affinity program") under a contractual arrangement. Under the contract, CB&T reviews, modifies, and approves the credit terms and underwriting criteria proposed by CompuCredit for the credit card program and issues the credit cards, and CompuCredit buys the credit card receivables and provides certain marketing and other services for the issued cards. Synovus represented that CB&T reviews the terms and underwriting criteria proposed by CompuCredit to ensure that all aspects of the credit card affinity program comply with applicable consumer protection laws and regulations. Synovus also stated that a Senior Regulatory Risk Analyst manages all aspects of the CB&T/CompuCredit relationship, which includes reviewing policies and procedures with internal and external counsel, reviewing customer complaints, and initiating audits. The Board consulted with the FDIC and reviewed supervisory and other confidential information about this credit card affinity program. Synovus is not involved in any other business conducted by CompuCredit and does not own or control CompuCredit within the meaning of the BHC Act.

16. The Interagency Questions and Answers Regarding Community Reinvestment provides that an institution's most recent CRA performance evaluation is an important and often controlling factor in the consideration of an institution's CRA record because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisory agency. 66 *Federal Register* 36,620 and 36,639 (2001).

17. The evaluation period of the examination was January 1, 2001, through January 14, 2002, and included a review of HMDA-reportable mortgage loans by SMC in the bank's assessment area from January 1, 2000, through September 30, 2001. CB&T's assessment area is the Columbus, Georgia Metropolitan Statistical Area ("Columbus MSA").

18. In this context, small business loans are loans with original amounts of $1 million or less that are either secured by nonfarm nonresidential properties or are classified as commercial and industrial loans. Small farm loans are loans with original amounts of $500,000 or less that are either secured by farmland, including farm residential improvements, or are classified as loans to finance agricultural production and other loans to farmers.

period, CB&T extended community development loans totaling more than $14 million.

Examiners reported that the bank's level of qualified investments and grants was good, despite the limited investment opportunities in its assessment area. CB&T made 45 community development investments and grants totaling more than $2.25 million during the evaluation period.

In addition, examiners found that CB&T provided a relatively high level and variety of financial and retail services to meet the needs of its assessment area. CB&T's community development activities included a school savings program for children from LMI families, financial training and special financing packages for businesses owned by women or minorities, and assistance in establishing a credit union focused on serving LMI communities.

B. HMDA and Fair Lending Records

The Board also has carefully considered the lending record of SMC in light of the comments received on the HMDA data. Based on 2003 HMDA data, the commenter alleged that SMC disproportionately denied African-American applicants for home mortgage purchase or refinance loans in three MSAs in Alabama and Georgia.[19]

In most of the markets reviewed, SMC's denial disparity ratios[20] with respect to African-American applicants for all HMDA-reportable loans on a combined basis were either below or slightly above the denial disparity ratios for the aggregate of all lenders in the market ("aggregate lenders").[21] SMC's denial rate[22] for African-American applicants was lower than the denial rate for the aggregate lenders in the markets reviewed.

Although the HMDA data may reflect certain disparities in the rates of applications, originations, or denials among members of different racial groups in certain local areas, the HMDA data generally do not demonstrate that SMC excluded any racial group on a prohibited basis. The Board nevertheless is concerned when HMDA data for an institution indicate disparities in lending and believes that all banks are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending, but also equal access to credit by creditworthy applicants regardless of their race. The Board recognizes, however, that HMDA data alone provide an incomplete measure of an institution's lending in its community because these data cover only a few categories of housing-related lending. HMDA data, moreover, provide only limited information about the covered loans.[23] HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has not assisted adequately in meeting its community's credit needs or has engaged in illegal lending discrimination.

Because of the limitations of HMDA data, the Board has considered these data carefully in light of other information, including information on Synovus's programs for compliance with fair lending and other consumer protection laws. The Board also consulted with the FDIC, the primary regulator of First Commercial Bank, SMC, and CB&T, and considered examination reports on the compliance with fair lending laws of these and other subsidiary depository and lending institutions of Synovus. Examiners noted no evidence of discriminatory lending practices on a prohibited basis in the CRA performance evaluations of Synovus's subsidiary depository institutions.

The record also indicates that Synovus has taken steps to ensure compliance with fair lending laws. Synovus has a Corporate Compliance Department ("CCD"), managed and staffed by individuals with extensive compliance experience, which develops and maintains comprehensive compliance programs for all laws and regulations applicable to Synovus's consumer lending activities. The CCD consults with internal and external counsel to ensure the adequacy of these programs and requires Synovus lending personnel to receive annual fair-lending training.

In addition, Synovus stated that the CCD reviews the consumer lending programs of each subsidiary by examining lending overrides on a monthly basis and conducting full-file compliance reviews on an annual basis. The CCD also monitors the subsidiaries' compliance with the HMDA and the CRA on a quarterly basis. Compliance officers at each Synovus subsidiary forward complaints as appropriate to the CCD for review and action. Synovus represented that it will implement similar compliance programs at CBCT.

Synovus's CCD performs oversight of SMC's lending activities in a manner similar to its oversight of other Synovus subsidiary institutions. Internal reviews by both SMC's Quality Control Group and Synovus's CCD are conducted at various stages of the mortgage process,

19. The Board analyzed the 2003 HMDA data for SMC in the Columbus MSA and the Birmingham and Montgomery, Alabama MSAs, which the commenter identified, and in the Atlanta, Georgia; Huntsville, Alabama; and Pensacola, Florida MSAs, where SMC also conducts much of its lending. SMC serves as the primary mortgage lender for most of Synovus's subsidiary banks. Synovus stated that if an applicant seeks a conventional home purchase or refinance loan, the application, with the applicant's consent, is referred to SMC for processing. The Board also reviewed confidential supervisory information, information provided by Synovus, and consulted with the FDIC on SMC's HMDA-reportable lending.

20. The denial disparity ratio equals the denial rate for a particular racial category (*e.g.*, African-American) divided by the denial rate for whites.

21. The lending data of the aggregate lenders represent the cumulative lending for all financial institutions that have reported HMDA data in a particular area.

22. The denial rate represents the percentage of a lender's HMDA loan applications that were denied.

23. The data, for example, do not account for the possibility that an institution's outreach efforts may attract a larger proportion of marginally qualified applicants than other institutions attract and do not provide a basis for an independent assessment of whether an applicant who was denied credit was, in fact, creditworthy. Credit history problems and excessive debt levels relative to income (reasons most frequently cited for a credit denial) are not available from HMDA data.

including the underwriting, prefunding, and postfunding periods. Independent third-party review of SMC's lending is conducted on a monthly basis, and Synovus conducts an internal audit of SMC annually.

The Board also has considered the HMDA data in light of the CRA performance records of Synovus's subsidiary depository institutions. These records demonstrate that Synovus is active in helping to meet the credit needs of its entire community.

C. Conclusion on the Convenience and Needs Factor

The Board has carefully considered all the facts of record, including reports of examination of the CRA records of the institutions involved, information provided by Synovus, public comment on the proposal, and supervisory and other confidential information. The Board notes that the proposal would expand the availability of financial products and services to customers by increasing the geographic scope of Synovus's banking operations. Based on a review of the entire record, and for reasons discussed above, the Board concludes that considerations related to the convenience and needs factor, including the CRA performance records of the relevant depository institutions, are consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the application should be, and hereby is, approved. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act and other applicable statutes. The Board's approval is specifically conditioned on compliance by Synovus with the conditions imposed in this order, the commitments made to the Board in connection with the application, and receipt of all other regulatory approvals. The conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

The acquisition of CBCT's voting shares may not be consummated before the fifteenth calendar day after the effective date of this order, or later than three months after the effective date of this order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of Atlanta, acting pursuant to delegated authority.

By order of the Board of Governors, effective February 23, 2005.

Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Gramlich, Bies, Olson, Bernanke, and Kohn.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

The Toronto-Dominion Bank
Toronto, Canada

Order Approving the Acquisition of a Bank Holding Company

The Toronto-Dominion Bank ("TD"), a financial holding company within the meaning of the Bank Holding Company Act ("BHC Act"), has requested the Board's approval under section 3 of the BHC Act[1] to acquire 51 percent of the voting shares of Banknorth Group, Inc. ("Banknorth") and its wholly owned subsidiary, Banknorth, National Association ("Banknorth Bank"), both in Portland, Maine.[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (69 *Federal Register* 68,147 (2004)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 3 of the BHC Act.

TD, with total consolidated assets of approximately $202 billion, is the fifth largest banking organization in Canada.[3] TD is the 82nd largest depository organization in the United States, controlling $8.5 billion of deposits through its only U.S. subsidiary insured depository institution, TD Waterhouse Bank, National Association, Jersey City, New Jersey ("TDW Bank"). TD also operates a branch in New York City and an agency in Houston. Banknorth, with total consolidated assets of approximately $29 billion, is the 47th largest depository organization in the United States, controlling deposits of $19.6 billion, representing less than 1 percent of total deposits of insured depository institutions in the United States.[4] On consummation of this proposal, TD would become the 29th largest depository organization in the United States, controlling deposits of approximately $28.1 billion, which represent less than 1 percent of total deposits of insured depository institutions in the United States.[5]

Interstate Analysis

Section 3(d) of the BHC Act allows the Board to approve an application by a bank holding company to acquire control of a bank located in a state other than the home state of the bank holding company if certain conditions are met.[6] For purposes of the BHC Act, the home state

1. 12 U.S.C. § 1842.

2. Applicants propose to acquire the nonbanking subsidiaries of Banknorth in accordance with section 4(k) of the BHC Act and the post-transaction notice procedures in section 225.87 of Regulation Y. 12 U.S.C. § 1843(k); 12 CFR 225.87.

3. Asset data are as of October 31, 2004, and rankings are as of June 30, 2004. Both are based on the exchange rate then available.

4. Asset data and rankings are as of June 30, 2004.

5. On consummation of the proposal, Banknorth will be renamed TD Banknorth, Inc.

6. Under section 3(d) of the BHC Act, a bank holding company's home state is the state in which the total deposits of all subsidiary banks of the company were the largest on the later of July 1, 1966, or the date on which the company became a bank holding company,

of TD is New York, and Banknorth Bank is located in Connecticut, Maine, Massachusetts, New Hampshire, New York, and Vermont.[7]

Based on a review of the facts of record, including a review of relevant state statutes, the Board finds that all conditions for an interstate acquisition enumerated in section 3(d) of the BHC Act are met in this case.[8] In light of all the facts of record, the Board is permitted to approve the proposal under section 3(d) of the BHC Act.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal clearly are outweighed in the public interest by its probable effect in meeting the convenience and needs of the community to be served.[9]

TD and Banknorth compete directly in the Metro New York banking market.[10] The Board has reviewed carefully the competitive effects of the proposal in this banking market in light of all the facts of record. In particular, the Board has considered the number of competitors that would remain in the markets, the relative shares of total deposits in depository institutions in the markets ("market deposits") controlled by TD and Banknorth,[11] the concentration level of market deposits and the increase in this level as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Merger Guidelines ("DOJ Guidelines"),[12] and other characteristics of the markets.

Consummation of the proposal would be consistent with Board precedent and the DOJ Guidelines in this banking market.[13] After consummation, the Metro New York banking market would remain moderately concentrated as measured by the HHI. The increase in concentration would be small and numerous competitors would remain.

The Department of Justice also has reviewed the anticipated competitive effects of the proposal and has advised the Board that consummation of the proposal would not have a significantly adverse effect on competition in this market or in any other relevant banking market. In addition, the appropriate banking agencies have been afforded an opportunity to comment and have not objected to the proposal.

Based on these and all other facts of record, the Board concludes that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive considerations are consistent with approval.

Financial, Managerial, and Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and banks involved in the proposal and certain other supervisory factors. The Board has carefully considered these factors in light of all the facts of record, including confidential supervisory and examination information from the various U.S. banking supervisors of the

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whichever is later. 12 U.S.C. § 1841(o)(4)(C). New York is the home state of TD for purposes of the International Banking Act and Regulation K. 12 U.S.C. § 3103; 12 CFR 211.22.

7. For purposes of section 3(d), the Board considers a bank to be located in the states in which the bank is chartered or headquartered or operates a branch. *See* 12 U.S.C. §§ 1841(o)(4)–(7) and 1842(d)(1)(A) and (d)(2)(B).

8. *See* 12 U.S.C. §§ 1842(d)(1)(A) & (B), 1842(d)(2)(A) & (B). TD is well capitalized and well managed, as defined by applicable law. Banknorth Bank has been in existence and operated for the minimum period of time required by applicable state law. *See* Conn. Gen. Stats. Ann. Ch. 666 § 36a-411 (five years); Mass. Gen. Laws Ann. Ch. 167A § 2 (three years). On consummation of the proposal, TD would control less than 10 percent of the total amount of deposits of insured depository institutions in the United States and less than 30 percent, or the appropriate percentage established by applicable state law, of deposits in Connecticut, Maine, Massachusetts, and New Hampshire. *See* Conn. Gen. Stats. Ann. Ch. 666 § 36a-411; Maine Rev. Stat. Ann. Tit. 9-B § 1013(3)(C); Mass. Gen. Laws Ann. Ch. 167A § 2; N.H. Rev. Stat. Ann. § 384-B3. All other requirements under section 3(d) of the BHC Act also would be met on consummation of the proposal.

9. 12 U.S.C. § 1842(c)(1).

10. The Metro New York banking market is defined as the counties of Bronx, Dutchess, Kings, Nassau, New York, Orange, Putnam, Queens, Richmond, Rockland, Suffolk, Sullivan, Ulster, and Westchester in New York; the counties of Bergen, Essex, Hudson, Hunterdon, Middlesex, Monmouth, Morris, Ocean, Passaic, Somerset, Sussex, Union, and Warren and portions of Mercer County in New Jersey; Pike County in Pennsylvania; and Fairfield County and portions of Litchfield and New Haven Counties in Connecticut.

11. Market share data are based on Summary of Deposits reports filed as of June 30, 2004, and on calculations in which the deposits of thrift institutions are included at 50 percent. The Board previously has indicated that thrift institutions have become, or have the potential to become, significant competitors of commercial banks. *See, e.g., Midwest Financial Group, 75 Federal Reserve Bulletin* 386 (1989); *National City Corporation, 70 Federal Reserve Board* 743 (1984). Thus, the Board regularly has included thrift deposits in the market share calculation on a 50 percent weighted basis. *See, e.g., First Hawaiian, Inc., 77 Federal Reserve Bulletin* 52 (1991).

12. Under the DOJ Guidelines, 49 *Federal Register* 26,823 (1984), a market is considered moderately concentrated if the post-merger HHI is between 1000 and 1800. The Department of Justice has informed the Board that a bank merger or acquisition generally will not be challenged (in the absence of other factors indicating anticompetitive effects) unless the post-merger HHI is at least 1800 and the merger increases the HHI by more than 200 points. The Department of Justice has stated that the higher than normal HHI thresholds for screening bank mergers for anticompetitive effects implicitly recognize the competitive effects of limited-purpose lenders and other nondepository financial institutions.

13. TD operates the 15th largest depository institution in the Metro New York banking market, controlling \$5.7 billion in deposits, which represents less than 1 percent of market deposits. Banknorth operates the 224th largest depository institution in the market, controlling \$38.4 million in deposits. On consummation of the proposal, TD would remain the 15th largest depository institution in the market, controlling deposits of approximately of \$5.7 billion. The HHI would remain at 1017, and 257 bank and thrift competitors would remain in the market.

institutions involved, publicly reported and other financial information, information provided by the applicant, and public comment on the proposal.[14] The Board also has consulted with the Office of the Superintendent of Financial Institutions ("OSFI"), which is responsible for the supervision and regulation of Canadian banks.

In evaluating financial factors in expansion proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of subsidiary depository institutions and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the financial condition of the combined organization on consummation, including its capital position, asset quality, and earnings prospects, and the impact of the proposed funding of the transaction.

Based on its review of these factors, the Board finds that TD has sufficient financial resources to effect the proposal. The capital levels of TD would continue to exceed the minimum levels that would be required under the Basel Capital Accord and its capital levels are considered equivalent to the capital levels that would be required of a U.S. banking organization. Furthermore, the subsidiary depository institutions of TD and Banknorth are well capitalized and would remain so on consummation of the proposal. The proposed transaction is structured in part as a share purchase, and TD has indicated that it would fund the cash portion of the consideration to be received by Banknorth shareholders from general corporate sources.

The Board also has evaluated the managerial resources of the organizations involved, including the proposed combined organization. The Board has reviewed the examination records of TD's U.S. operations, Banknorth, and Banknorth Bank, including assessments of their management, risk management systems, and operations. In addition, the Board has considered its supervisory experience and that of the other relevant banking supervisory agencies with the organizations and their records of compliance with applicable banking laws. TD, Banknorth, and their U.S. subsidiary banks are considered well managed. The Board also has considered TD's plans to consummate the proposal.

Based on these and all other facts of record, the Board concludes that the financial and managerial resources and future prospects of the organizations involved in the proposal are consistent with approval.[15]

Section 3 of the BHC Act also provides that the Board may not approve an application involving a foreign bank unless the bank is subject to comprehensive supervision or regulation on a consolidated basis by the appropriate authorities in the bank's home country.[16] The home country supervisor of TD is the OSFI.

In approving applications under the BHC Act and the International Banking Act ("IBA"),[17] the Board previously has determined that various Canadian banks, including TD, were subject to home country supervision on a consolidated basis by the OSFI.[18] In this case, the Board has determined that the OSFI continues to supervise TD in substantially the same manner as it supervised Canadian banks at the time of those determinations. Based on this finding and all the facts of record, the Board has concluded that TD continues to be subject to comprehensive supervision on a consolidated basis by its home country supervisor.

In addition, section 3 of the BHC Act requires the Board to determine that an applicant has provided adequate assurances that it will make available to the Board such information on its operations and activities and those of its affiliates that the Board deems appropriate to determine and enforce compliance with the BHC Act.[19] The Board has reviewed the restrictions on disclosure in relevant jurisdictions in which TD operates and has communicated with relevant government authorities concerning access to information. In addition, TD previously has committed to make available to the Board such information on the operations of it and its affiliates that the Board deems necessary to

14. A commenter expressed concerns about:

(1) the amount of consideration Banknorth shareholders might receive in the future if TD seeks to acquire the remaining Banknorth shares;
(2) projects financed by TD in North and South America that the commenter asserted are having negative environmental consequences; and
(3) press reports about a dispute in Canada between TD and one of its retail customers.

These matters are not within the Board's jurisdiction to adjudicate or within the limited statutory factors that the Board is authorized to consider when reviewing an application under the BHC Act. *See, e.g., Western Bancshares, Inc. v. Board of Governors*, 480 F.2d 749 (10th Cir. 1973).

15. A commenter expressed concern about a press report of anomalies with respect to trading of Banknorth shares before the proposal was publicly announced. The Securities and Exchange Commission ("SEC"), and self-regulatory organizations ("SROs") acting under authority delegated by the SEC, have the authority to investigate trading activity and to take action if there are violations of the federal securities laws or SRO rules. The commenter also expressed concern about allegations that TD assisted Enron in preparing false financial statements. The SEC has the authority to investigate and adjudicate if any violations of federal securities laws have occurred. The Board has consulted with the SEC and the relevant SRO about these matters.

16. 12 U.S.C. § 1842(c)(3)(B). Under Regulation Y, the Board uses the standards enumerated in Regulation K to determine whether a foreign bank is subject to consolidated home country supervision. *See* 12 CFR 225.13(a)(4). Regulation K provides that a foreign bank will be considered subject to comprehensive supervision or regulation on a consolidated basis if the Board determines that the bank is supervised or regulated in such a manner that its home country supervisor receives sufficient information on the worldwide operations of the bank, including its relationship to any affiliates, to assess the bank's overall financial condition and its compliance with laws and regulations. *See* 12 CFR 211.24(c)(1).

17. 12 U.S.C. § 3101 *et seq.*

18. *See, e.g., The Toronto-Dominion Bank*, 82 *Federal Reserve Bulletin* 1052 (1996); *see also Royal Bank of Canada*, 89 *Federal Reserve Bulletin* 139 (2003); *Canadian Imperial Bank of Commerce*, 87 *Federal Reserve Bulletin* 678 (2001).

19. *See* 12 U.S.C. § 1842(c)(3)(A).

determine and enforce compliance with the BHC Act, the IBA, and other applicable federal laws. TD also previously has committed to cooperate with the Board to obtain any waivers or exemptions that may be necessary to enable TD and its affiliates to make such information available to the Board. In light of these commitments, the Board concludes that TD has provided adequate assurances of access to any appropriate information the Board may request. Based on these and all other facts of record, the Board has concluded that the supervisory factors it is required to consider are consistent with approval.

Convenience and Needs Considerations

In acting on this proposal, the Board is required to consider the effects of the proposal on the convenience and needs of the communities to be served and to take into account the records of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[20] The CRA requires the federal financial supervisory agencies to encourage financial institutions to help meet the credit needs of local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account an institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank expansionary proposals.

The Board has considered carefully the convenience and needs factor and the CRA performance records of TD's subsidiary insured depository institutions and Banknorth Bank in light of all the facts of record, including public comment on the proposal. Two commenters opposed the proposal and alleged, based on data reported under the Home Mortgage Disclosure Act ("HMDA"),[21] that Banknorth Bank provided a low level of home mortgage lending to LMI borrowers or in LMI communities and engaged in disparate treatment of minority individuals in home mortgage lending in the banks' assessment areas.[22]

A. CRA Performance Evaluations

As provided in the CRA, the Board has evaluated the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the CRA performance records of the relevant insured depository institutions. An institution's most recent CRA performance evaluation is a particularly important consideration in the applications process because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisor.[23]

TDW Bank received a "satisfactory" rating at its most recent CRA performance evaluation by the Office of the Comptroller of the Currency ("OCC"), as of March 10, 2003.[24] Banknorth Bank was formed on January 1, 2002, by the consolidation of nine subsidiary banks of Banknorth (the "Consolidation"), all of which had "satisfactory" or "outstanding" CRA performance ratings at that time.[25] Peoples Heritage Bank, NA, Portland, Maine ("Peoples Heritage"), the surviving bank of the Consolidation, received an "outstanding" CRA performance rating by the OCC as of July 2001, and First Massachusetts Bank, N.A., Worcester, Massachusetts ("First Massachusetts"), Banknorth's largest subsidiary bank immediately before the Consolidation, received a "satisfactory" CRA performance rating by the OCC as of April 2001.[26] TD has indicated that Banknorth's management team would remain intact after consummation of the proposal and that no new products or services are expected to be offered by Banknorth Bank as a result of the proposal.

B. CRA Performance of TDW Bank

As noted, TDW Bank received a "satisfactory" rating in its March 2003 evaluation.[27] Examiners reported that the

20. 12 U.S.C. § 1842(c)(2); 12 U.S.C. § 2901 *et seq.*

21. 12 U.S.C. § 2801 *et seq.*

22. One commenter also expressed concern about Banknorth Bank's relationships with unaffiliated retail check cashers, pawn shops, and other unaffiliated nontraditional providers of financial services. TD has indicated that Banknorth had reviewed its relationships with these types of businesses and has opted to continue relationships with those firms willing to meet certain conditions. These conditions include provisions in each loan agreement with Banknorth Bank of representations and warranties that the firm will comply with all applicable laws, including any applicable fair lending and consumer protections laws, and follow the bank's program requirements to ensure compliance with anti-money-laundering laws and regulations. TD has represented that neither Banknorth Bank nor any of its affiliates play any role in the lending practices, credit review, or other business practices of these firms, nor does the bank or any of its affiliates purchase any loans originated by these firms.

23. *See Interagency Questions and Answers Regarding Community Reinvestment*, 66 *Federal Register* 36,620 and 36,639 (2001).

24. TD dissolved its other U.S. subsidiary insured depository institution, TD Bank USA, FSB, Jersey City, New Jersey ("FSB"), as of December 31, 2004. When dissolved, FSB was rated "satisfactory" for CRA performance by the Office of Thrift Supervision in its most recent examination as of October 1999.

25. The banks that were parties to the Consolidation and their CRA ratings at that time are listed in Appendix A. Banknorth Investment Management Group, N.A., Burlington, Vermont, a nondeposit trust company, was also part of the Consolidation. Since the Consolidation, Banknorth has acquired eight additional banks and has merged them into Banknorth Bank. These banks, the date on which they were merged into Banknorth Bank, and their CRA ratings at the time of their mergers are listed in Appendix B. In addition, Banknorth Bank's acquisition of a savings association has been approved by the OCC, but the acquisition has not been consummated.

26. On consummation of the Consolidation, Peoples Heritage changed its name to Banknorth, National Association.

27. TDW Bank has elected to be evaluated for CRA performance under the strategic plan alternative. Under this alternative, the bank submits a plan, subject to the OCC's approval, specifying measurable goals for meeting the lending, investment, and service needs of the bank's assessment area, and the OCC evaluates the bank on its fulfillment of the goals in the approved plan. *See* 12 CFR 25.27. The March 2003 evaluation covered the evaluation period beginning January 1, 2000, through December 31, 2003, and reviewed the bank's CRA performance under strategic plans approved by the OCC in March 1998 (with respect to the year 2000) and November 2000 (with

bank originated or purchased almost $16.8 million in community development loans during the evaluation period and had met its annual goals for community development lending each year. These loans funded affordable housing for LMI individuals in the bank's assessment areas.

The bank's community development investments totaled almost $77 million at the end of the evaluation period and included investments in community development financial institutions, low-income housing tax credit projects, and affordable housing bonds issued by the New Jersey and New York state housing authorities. The bank met its goals for community development investments in 2000 and 2002 and substantially met its goal for 2001. Examiners also reported that TDW Bank made $1.04 million in qualified community development grants during the evaluation period and met its annual grants goals in each of the three years. The bank also met its goals for each year in the evaluation period for membership in community development organizations, including organizations involved in providing affordable LMI housing and supporting community development corporations.

C. CRA Performance of Banknorth Bank

1. *Peoples Heritage.* As noted, Peoples Heritage received an overall "outstanding" rating in its July 2001 evaluation.[28] The bank received a rating of "outstanding" under the lending test in this evaluation. Examiners reported that the bank's overall distribution of home mortgage loans to LMI geographies and borrowers was excellent during the evaluation period. Examiners also noted that Peoples Heritage participated in mortgage programs sponsored by the State of Maine that offer flexible underwriting and documentation standards, below-market interest rates, and low down payments.

Examiners stated that Peoples Heritage's record of making small loans to businesses in LMI census tracts was excellent.[29] The bank also made more than $16 million in community development loans during the evaluation period, including $11 million in loans to create more than 160 units of housing for LMI individuals and families.

Peoples Heritage received ratings of "high satisfactory" and "outstanding" on the investment and service tests respectively, in the July 2001 evaluation. During the evaluation period, Peoples Heritage made 80 qualified investments totaling $3.6 million, a level examiners described as good. Examiners noted that the percentage of the bank's branches in LMI census tracts generally equaled or exceeded the percentage of the population living in LMI census tracts in the bank's assessment areas. They also reported that Peoples Heritage provided an excellent level of community development services.

2. *First Massachusetts.* As noted, First Massachusetts received an overall "satisfactory" rating in its April 2001 CRA evaluation. The bank received a rating of "high satisfactory" under the lending test in this evaluation. Examiners stated that the bank's distribution of home mortgage loans to LMI geographies and borrowers was adequate or better in each of the bank's assessment areas. They also noted that the bank participated in a number of state and federal affordable housing programs with flexible underwriting criteria and other features designed to promote homeownership among LMI individuals.

Examiners reported that First Massachusetts's record of making small loans to businesses in LMI census tracts was adequate or better in each of the bank's assessment areas. The bank also made more than $23 million in community development loans during the period covered by the April 2001 evaluation, including two loans to the Massachusetts Housing Partnership Fund, which promotes affordable housing and neighborhood development throughout Massachusetts.[30]

First Massachusetts received ratings of "low satisfactory" and "high satisfactory" on the investment and the services tests, respectively, in the April 2001 evaluation. During the evaluation period, the bank made almost $11.3 million in qualified investments, a level examiners described as adequate. Examiners characterized the bank's distribution of branches as good or excellent in its assessment areas and stated that it provided an adequate level of community development services.

3. *Recent CRA Activities of Banknorth Bank.* During 2002 and 2003, Banknorth Bank originated or purchased more than 16,900 HMDA-reportable loans totaling approximately $2.2 billion in Maine, Massachusetts, New Hampshire, and Vermont.[31] In each of these states, Banknorth Bank made higher percentages of its HMDA-reportable loans to LMI borrowers and in LMI census tracts than did lenders in the aggregate ("aggregate lenders") in 2002 and 2003.[32]

To assist first-time and LMI homebuyers, Banknorth Bank also offers loans insured by the Federal Housing Authority and loans guaranteed by the Department of Veteran Affairs and participates in state housing finance agency programs that offer below-market interest rates and lower down-payment requirements. In 2002 and 2003, the

respect to the years 2001 and 2002). In February 2004, the OCC approved the bank's strategic plan for the years 2004 through 2006.

28. The evaluation period was from July 1, 1998, through December 31, 2000, except for community development loans, which were evaluated for the period beginning September 1, 1998, through July 9, 2001.

29. In this context, "small loans to businesses" refers to loans with original amounts of $1 million or less that are either secured by nonfarm or residential real estate or are classified as commercial and industrial loans.

30. The evaluation period was from July 1, 1997, through December 31, 2000, except for community development loans, which were evaluated for the period beginning August 1, 1997, through April 20, 2001.

31. Together, these four states accounted for more than 81 percent of Banknorth Bank's deposit base, as of June 30, 2004.

32. The lending data of the aggregate lenders represent the cumulative lending for all financial institutions that have reported HMDA data in a given market.

bank originated more than 1,700 loans totaling more than $150 million through these programs.

In 2002 and 2003, Banknorth Bank's percentages of small business loans in LMI census tracts were higher than or comparable to the percentages for aggregate lenders in each of the following states: Maine, Massachusetts, New Hampshire, and Vermont. In all its assessment areas across six states, the bank continues to participate in Small Business Administration and state programs focused on lending to small businesses unable to secure conventional financing. From January 2001 through October 2004, the bank made more than 1,500 of these loans totaling more than $152 million.

During 2001 through 2003, Banknorth Bank made 227 community development loans totaling more than $164 million. Community development lending included loan commitments of $13.6 million to finance the construction, rehabilitation, or preservation of more than 180 units of affordable housing in New Hampshire and a $7 million loan to a state housing fund to create and preserve affordable housing throughout Vermont. During this same period, the bank made loan commitments totaling almost $3.2 million to three community mental health facilities in Massachusetts.

Banknorth Bank's community development investments from January 2001 through June 2004 totaled more than $66 million. These investments included commitments of more than $18 million to fund low-income housing tax credit projects in Maine, Massachusetts, New Hampshire, and New York. Banknorth Bank has indicated that its community development donations during the same period have totaled more than $4 million, and recipients have included a wide range of community organizations throughout the bank's assessment area.

D. HMDA Data and Fair Lending Record

The Board has carefully considered Banknorth Bank's lending record in light of comments on the bank's HMDA data. Based on 2003 HMDA data, two commenters alleged that Banknorth Bank disproportionately excluded or denied African-American or Hispanic applicants for home mortgage loans in various Metropolitan Statistical Areas ("MSAs").[33] The Board reviewed HMDA data for 2002 and 2003 reported by the bank in the six states in its assessment areas, in the MSAs identified by the commenter, and in certain other MSAs.[34]

The 2002 and 2003 HMDA data reported by BankNorth Bank indicate that its denial disparity ratios[35] for African-American and Hispanic applicants for total HMDA-reportable loans in Maine, Massachusetts, and New Hampshire, which together accounted for 80 percent of the bank's HMDA-reportable loans in 2002 and 2003, were not as favorable as those ratios for the aggregate lenders in those states. The data also indicate, however, that the bank's percentages of its total-HMDA-reportable loans to African Americans or Hispanics in each of these states in 2002 and 2003 were generally comparable to or more favorable than those ratios for the aggregate lenders.[36] Similarly, the bank's percentages of total HMDA-reportable loans to borrowers in predominantly minority census tracts in Massachusetts during 2002 and 2003 were more favorable than the percentages for the aggregate lenders in those areas.[37]

Although the HMDA data might reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial groups, these data generally do not indicate that Banknorth Bank is excluding any race segment of the population or geographic area on a prohibited basis. The Board nevertheless is concerned when HMDA data for an institution indicate disparities in lending and believes that all banks are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending, but also equal access to credit by creditworthy applicants regardless of their race or income level. The Board recognizes, however, that HMDA data alone provide an incomplete measure of an institution's lending in its community because these data cover only a few categories of housing-related lending and provide only limited information about covered loans.[38] HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has not assisted adequately in meeting its community's credit needs or has engaged in illegal lending discrimination.

Because of the limitations of HMDA data, the Board has considered these data carefully in light of other information, including examination reports that provide an on-site evaluation of compliance with fair lending laws by the subsidiary banks of TD and Banknorth. Examiners noted no fair lending law issues or concerns in the March 2003 TDW Bank evaluation or in any of the most recent CRA evaluations of the banks that have been merged into Banknorth Bank. The Board also consulted with the OCC, which has responsibility for enforcing compliance with fair

33. Specifically, the commenter cited HMDA data on Banknorth Bank's lending to African Americans or Hispanics in the Hartford and New Haven MSAs in Connecticut, in the Lowell and Springfield MSAs in Massachusetts, in the Boston MSA in Massachusetts and New Hampshire, and in the Albany MSA in New York.

34. The Board also reviewed HMDA data for the Portland, Maine, MSA, which is Banknorth Bank's home market, and the Glens Falls MSA in New York.

35. The denial disparity ratio equals the denial rate of a particular racial category (*e.g.* African-American) divided by the denial rate for whites.

36. The percentage of the bank's loans to Hispanics in New Hampshire in 2002 and 2003 were modestly less favorable than those ratios for lenders in the aggregate.

37. For purposes of this HMDA analysis, a predominantly minority census tract means a census tract with a minority population of 80 percent or more.

38. The data, for example, do not account for the possibility that an institution's outreach efforts may attract a larger proportion of marginally qualified applicants than other institutions attract and do not provide a basis for an independent assessment of whether an applicant who was denied credit was, in fact, creditworthy. Credit history problems and excessive debt levels relative to income (reasons most frequently cited for a credit denial) are not available from HMDA data.

lending laws by TDW Bank and Banknorth Bank, about this proposal and the record of performance of these banks since their most recent CRA evaluations.

The record also indicates that Banknorth Bank has taken steps to ensure compliance with fair lending laws and other consumer protection laws. Among other things, the bank has implemented an annual compliance monitoring program that includes comparative file analysis and review of HMDA data, and it has developed a system for addressing fair lending complaints.

The Board has also considered the HMDA data in light of the programs described above and the overall performance records of the subsidiary banks of TDW Bank and Banknorth Bank under the CRA. These established efforts demonstrate that the banks are actively helping to meet the credit needs of their entire communities.

E. Conclusion on Convenience and Needs Factor

The Board has carefully considered all the facts of record,[39] including reports of examination of the CRA records of the institutions involved, information provided by the applicant, public comments on the proposal, and confidential supervisory information. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that considerations relating to the convenience and needs factor, including the CRA performance records of the relevant depository institutions, are consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the application should be, and hereby is, approved. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act and other applicable statutes.[40] The Board's approval is specifically conditioned on compliance by TD with the condition imposed in this order, the commitments made to the Board in connection with the application, and the prior commitments to the Board referenced in this order. For purposes of this transaction, these commitments and conditions are deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

The proposal may not be consummated before the fifteenth calendar day after the effective date of this order, or later than three months after the effective date of this order unless such period is extended for good cause by the Board or the Federal Reserve Bank of New York, acting pursuant to delegated authority.

By order of the Board of Governors, effective January 18, 2005.

Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Gramlich, Bies, Olson, Bernanke, and Kohn.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

39. One commenter requested that the Board condition its approval of the proposal on TD's making certain community reinvestment and other commitments. As the Board previously has explained, an applicant must demonstrate a satisfactory record of performance under the CRA without reliance on plans or commitments for future actions. The Board has consistently stated that neither the CRA nor the federal banking agencies' CRA regulations require depository institutions to make pledges or enter into commitments or agreements with any organization. *See, e.g., J.P. Morgan Chase & Co.*, 90 *Federal Reserve Bulletin* 352 (2004); *Wachovia Corporation*, 91 *Federal Reserve Bulletin* 77 (2005). In this case, as in past cases, the Board instead has focused on the demonstrated CRA performance record of the applicant and the programs that the applicant has in place to serve the credit needs of its CRA assessment areas when the Board reviews the proposal under the convenience and needs factor. In reviewing future applications by TD under this factor, the Board similarly will review TD's actual CRA performance record and the programs it has in place to meet the credit needs of its communities at that time.

40. Two commenters also requested that the Board hold a public meeting or hearing on the proposal. Section 3 of the BHC Act does not require the Board to hold a public hearing on an application unless the appropriate supervisory authority for the bank to be acquired makes a timely written recommendation of denial of the application. The Board has not received such a recommendation from the appropriate supervisory authorities.

Under its rules, the Board also may, in its discretion, hold a public meeting or hearing on an application to acquire a bank if a meeting or hearing is necessary or appropriate to clarify factual issues related to the application and to provide an opportunity for testimony. 12 CFR 225.16(e). The Board has considered carefully the commenter's requests in light of all the facts of record. In the Board's view, the commenters had ample opportunity to submit their views, and in fact, the commenters have submitted written comments that the Board has considered carefully in acting on the proposal. The commenter's requests fail to demonstrate why the written comments do not present their views adequately and fail to identify disputed issues of fact that are material to the Board's decision that would be clarified by a public meeting or hearing. For these reasons, and based on all the facts of record, the Board has determined that a public meeting or hearing is not required or warranted in this case. Accordingly, the requests for a public meeting or hearing on the proposal are denied.

Appendix A

Banks Consolidated to Form Banknorth Bank on January 1, 2002

Bank	CRA Rating	Date	Supervisor
Andover Bank, Andover, Massachusetts	Outstanding	October 1999	FDIC
Bank of New Hampshire, N.A., Farmington, New Hampshire	Satisfactory	September 2000	OCC
Evergreen Bank, National Association, Glen Falls, New York	Satisfactory	October 2000	OCC
First Massachusetts Bank, N.A., Worcester, Massachusetts	Satisfactory	April 2001	OCC
First Vermont Bank and Trust Company, Brattleboro, Vermont	Satisfactory	December 1997	FDIC
Franklin Lamoille Bank, St. Albans, Vermont	Outstanding	March 1999	OCC
Gloucester Bank & Trust Company, Gloucester, Massachusetts	Outstanding	July 1998	FDIC
The Howard Bank, N.A., Burlington, Vermont	Outstanding	December 1997	OCC
Peoples Heritage Bank, N.A., Portland, Maine	Outstanding	July 2001	OCC

Appendix B

Banks Merged Into Banknorth Bank Since January 1, 2002

Bank	Date of Acquisition	CRA Rating	Date	Supervisor
American Bank of Connecticut, Waterbury, Connecticut	01/22/2002	Satisfactory	June 2001	FDIC
Ipswich Savings Bank, Ipswich, Massachusetts	07/27/2002	Satisfactory	May 1999	FDIC
Southington Savings Bank, Southington, Connecticut	09/01/2002	Satisfactory	June 2000	FDIC
Warren Five Cents Savings Bank, Peabody, Massachusetts	01/01/2003	Satisfactory	October 2001	FDIC
American Savings Bank, New Britain, Connecticut	02/15/2003	Outstanding	January 2001	FDIC
First & Ocean National Bank, Newburyport, Massachusetts	01/01/2004	Outstanding	August 1999	OCC
Cape Cod Bank and Trust Company, Hyannis, Massachusetts	05/01/2004	Satisfactory	March 2003	OCC
Foxborough Savings Bank, Foxborough, Massachusetts	05/01/2004	Satisfactory	September 2002	FDIC
Boston Federal Savings Bank, Burlington, Massachusetts	Acquisition pending*	Outstanding	June 2001	OTS

* The OCC approved the proposed merger on November 15, 2004.

Webster Financial Corporation
Waterbury, Connecticut

Order Approving the Acquisition of a Bank Holding Company

Webster Financial Corporation ("Webster"), a financial holding company within the meaning of the Bank Holding Company Act ("BHC Act"), has requested the Board's approval pursuant to section 3 of the BHC Act[1] to acquire Eastern Wisconsin Bancshares, Inc. ("Eastern")[2] and its subsidiary bank, State Bank of Howards Grove, both in Howards Grove, Wisconsin ("State Bank").[3]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (69 *Federal Register* 63,385 (2004)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in the BHC Act.

Webster, with total consolidated assets of approximately $17.8 billion, is the 48th largest depository organization in the United States,[4] controlling deposits of approximately $10.6 billion.[5] Webster has one subsidiary depository institution, Webster Bank, with branches in Connecticut, Massachusetts, New York, and Rhode Island. Eastern, with total consolidated assets of approximately $164.9 million, is the 103rd largest depository institution in Wisconsin, controlling deposits of $138 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state. On consummation of the proposal, Webster would remain the 48th largest depository organization in the United States, with total consolidated assets of approximately $18 billion, and would control deposits of approximately $10.7 billion, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the United States.

Interstate Analysis

Section 3(d) of the BHC Act allows the Board to approve an application by a bank holding company to acquire control of a bank located in a state other than the home state of such bank holding company if certain conditions are met. For purposes of the BHC Act, the home state of Webster is Connecticut,[6] and Eastern's subsidiary bank is located in Wisconsin.[7]

Based on a review of the facts of record, including a review of relevant state statutes, the Board finds that all conditions for an interstate acquisition enumerated in section 3(d) of the BHC Act are met in this case.[8] In light of all the facts of record, the Board is permitted to approve the proposal under section 3(d) of the BHC Act.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market, unless the Board finds that the anticompetitive effects of the proposal clearly are outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[9]

Webster and Eastern do not compete directly in any relevant banking market. Based on all the facts of record, the Board has concluded that consummation of the proposal would have no significant adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive factors are consistent with approval.

1. 12 U.S.C. § 1842.

2. Webster also has requested the Board's approval under section 3 of the BHC Act to exercise an option to purchase up to 19.9 percent of Eastern's common stock on the occurrence of certain circumstances. The option would terminate on consummation of Webster's application to acquire Eastern. In addition, Webster has requested the Board's approval under section 3 of the BHC Act to purchase up to 19.9 percent of Eastern's common stock before consummation if the Board approves the proposal and the purchase is necessary to maintain State Bank as a well-capitalized institution.

3. State Bank operates one full-service branch in Howards Grove and a loan production office in Beaver Dam, Wisconsin. State Bank offers health savings accounts ("HAS") nationwide through its division, HSA Bank. HSAs, authorized by the Medicare Prescription Drug Improvement and Modernization Act of 2003, are tax-exempt savings accounts earmarked for medical expenses. After consummation of this proposal, Webster proposes to merge State Bank into its subsidiary bank, Webster Bank, National Association ("Webster Bank"), also in Waterbury; operate HSA Bank as a division of Webster Bank; and sell the remaining operations of State Bank, including its two offices in Wisconsin. Webster has represented that it intends to operate the State Bank offices until Webster sells them to another financial institution.

4. Asset and national ranking data are as of September 30, 2004, and reflect consolidations through that date.

5. Deposit data are as of June 30, 2004, and reflect the total of the deposits reported by each organization's insured depository institutions in their Consolidated Reports of Condition and Income or Thrift Financial Reports for June 30, 2004. In this context, insured depository institutions include commercial banks, savings banks, and savings associations.

6. A bank holding company's home state is the state in which the total deposits of all subsidiary banks of the company were the largest on July 1, 1966, or the date on which the company became a bank holding company, whichever is later. 12 U.S.C. § 1841(o)(4)(C).

7. For purposes of section 3(d), the Board considers a bank to be located in the states in which the bank is chartered or headquartered or operates a branch. 12 U.S.C. §§ 1841(o)(4)–(7) and 1842(d)(1)(A) and (d)(2)(B).

8. 12 U.S.C. §§ 1842(d)(1)(A)&(B), 1842(d)(2)(A)&(B). Webster is well capitalized and well managed, as defined by applicable law. State Bank has been in existence and operated for the minimum period of time required by applicable state law (five years). Wis. Stat. Ann. § 221.0901. On consummation of the proposal, Webster would control less than 10 percent of the total amount of deposits of insured depository institutions in the United States and less than 30 percent of the total amount of deposits of insured depository institutions in Wisconsin. Wis. Stat. Ann. § 221.0901. All other requirements under section 3(d) of the BHC Act also would be met on consummation of the proposal.

9. 12 U.S.C. § 1842(c)(1).

Financial, Managerial, and Supervisory Considerations

Section 3 of the BHC Act also requires the Board to consider the financial and managerial resources and future prospects of companies and depository institutions involved in the proposal and certain other supervisory factors. The Board has carefully considered these factors in light of all the facts of record, including confidential reports of examination, other confidential supervisory information from the federal and state banking supervisors of the organizations involved, publicly reported and other financial information, public comments received on the proposal,[10] and information provided by Webster.

In evaluating financial factors in expansion proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary depository institutions and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the financial condition of the combined organization on consummation, including its capital position, asset quality, and earnings prospects, and the impact of the proposed funding of the transaction.

Based on its review of these factors, the Board finds Webster to have sufficient financial resources to effect the proposal. Webster and Webster Bank currently are well capitalized and would remain so on consummation of the proposal. The proposed transaction is structured primarily as a cash transaction funded from Webster's existing resources.

The Board also has considered the managerial resources of the organizations involved, including the proposed combined organization. The Board has reviewed the examination records of Webster, Eastern, and their subsidiary depository institutions, including assessments of their management, risk management systems, and operations.[11] In addition, the Board has considered its supervisory experiences and those of the other relevant banking agencies with the organizations and their records of compliance with applicable banking law. Webster, Eastern, and their subsidiary depository institutions are considered well managed. In addition, the Board also has considered Webster's plans for implementing the proposal, including its proposed management after consummation.

Based on all the facts of record, including a review of the comments received, the Board concludes that considerations relating to the financial and managerial resources and future prospects of the organizations involved in the proposal are consistent with approval, as are the other supervisory factors under the BHC Act.

Convenience and Needs and CRA Performance Considerations

In acting on this proposal, the Board also must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[12] The CRA requires the federal financial supervisory agencies to encourage financial institutions to help meet the credit needs of the local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account a depository institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating the depository institution's expansionary proposals.[13]

The Board has considered carefully the convenience and needs factor and the CRA performance records of the subsidiary depository institutions of Webster and Eastern in light of all the facts of record, including public comments received on the proposal.[14] The commenter alleged, based on data reported under the Home Mortgage Disclosure Act ("HMDA"),[15] that Webster disproportionately denied applications for loans by minorities and that its plans to divest State Bank's offices in Wisconsin would disrupt services to retail customers.[16]

10. A commenter asserted generally that Webster's entry into the HSA business raises regulatory compliance issues and warrants an extensive compliance review. State Bank, a state member bank, operates under the supervision of the Federal Reserve System and the Wisconsin Department of Financial Institutions. Neither supervisor has found consumer compliance deficiencies related to its HSA Bank operations. Webster Bank stated that it will retain substantially all of HSA Bank's employees, including its manager, after consummation of the proposed merger with State Bank, and the HSA operations will be subject to review by the Office of the Comptroller of the Currency ("OCC"), Webster Bank's primary federal supervisor.

11. The commenter also cited a 2002 press report of a lawsuit filed against Webster Bank concerning allegations by a teller that the bank's branch employees were required to work overtime without compensation in 2000 and 2001. The press report noted that efforts would be made to certify the litigation as a class action suit. Webster Bank stated that the teller's suit was settled in March 2003 and that no class action suit was certified. Moreover, the Board does not have jurisdiction to determine compliance with state or federal employment laws.

12. 12 U.S.C. § 2901 *et seq.*

13. 12 U.S.C. § 2903.

14. The commenter asserted that Webster should be required to have a CRA plan that takes into account its proposed acquisition of State Bank's HSA Bank and that Webster should be evaluated under the CRA on a nationwide basis after consummation of the proposal. The adequacy of Webster's CRA-related efforts in the future and the scope of its CRA evaluation after consummation of this proposal are matters within the jurisdiction of the OCC, Webster Bank's primary supervisor under the CRA.

15. 12 U.S.C. § 2801 *et seq.*

16. The commenter criticized Webster's relationships with unaffiliated car-title-lending companies and other providers of nontraditional financial services. Webster Bank responded that it has entered into lending relationships with providers of nontraditional financial products, but it does not play any role in the lending or business practices or credit review processes of those providers.

A. CRA Performance Evaluations

As provided in the CRA, the Board has evaluated the convenience and needs factor in light of evaluations by the appropriate federal supervisors of the CRA performance records of the relevant insured depository institutions. An institution's most recent CRA performance evaluation is a particularly important consideration in the applications process because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisor.[17]

Webster Bank received an "outstanding" rating at the most recent evaluation of its CRA performance by the Office of Thrift Supervision ("OTS"), as of January 14, 2002 ("2002 Evaluation").[18] State Bank received a "satisfactory" rating at the most recent evaluation of its CRA performance by the Federal Reserve Bank of Chicago, as of May 12, 2003.

B. CRA Performance of Webster Bank

In the 2002 Evaluation, Webster Bank received an "outstanding"rating under the lending, investment, and service tests.[19] Examiners stated that the "outstanding" rating under the lending test was based on the bank's high volume and percentage of residential mortgage loans to LMI individuals and on its high volume of loans to small businesses.[20] They also determined that Webster Bank's community development lending performance enhanced its overall lending performance.

Examiners reported that the bank made a higher percentage of its loans reported under HMDA to LMI individuals in its assessment areas in 2000 than the percentage for the aggregate of lenders ("aggregate lenders").[21] They noted that the bank used flexible mortgage loan products and innovative deposit products to serve the assessment area's credit needs.

Since the 2002 Evaluation, Webster Bank's HMDA-reportable lending in LMI geographies continued to strengthen in 2003. The bank increased its home mortgage loans in LMI census tracts from more than 570 loan originations totaling $60.9 million in 2002, to more than 1,050 loan originations totaling $105.4 million in 2003. Webster Bank also has continued to offer a variety of affordable housing loans. Webster Bank offers Fannie Mae programs that feature no or minimal down payment requirements or that allow applicants with less than perfect credit records to receive adjustable rate loans that reward timely payments over a specified period with limited interest rate reductions. Webster Bank also offers loans sponsored by the Federal Housing Administration. In October 2004, Webster Bank announced a new affordable mortgage product, the Home Ownership Possibilities for Everyone ("HOPE") mortgage loan that features nontraditional underwriting standards, including the use of innovative credit scoring methods and minimal down-payment requirements. After attending homebuyer education classes, borrowers are eligible for reduced interest rates and are not required to purchase private mortgage insurance under the HOPE mortgage program.

Examiners reported that Webster Bank had the highest market share of small loans to businesses in its assessment areas of any of the aggregate lenders, as reported by the Small Business Loan Aggregate Report of the Federal Financial Institutions Examination Council. Moreover, examiners noted that 77 percent of Webster Bank's small loans to businesses were in amounts of $100,000 or less, which demonstrated an excellent responsiveness to assessment-area credit needs. Since the 2002 Evaluation, Webster Bank reported that it made $10.5 million in small loans to businesses in its assessment areas.

In the 2002 Evaluation, Webster Bank originated community development loans totaling almost $12 million. Examiners found that these loans assisted economic development throughout all of its assessment areas and provided more than 200 units of housing to LMI residents. Examiners also noted that Webster Bank formed a business unit dedicated to community development lending during the evaluation period.

Webster Bank stated that its community development lending has increased since the 2002 Evaluation. From January 2002 through September 2004, Webster Bank originated seven major community development loans totaling $35.1 million.

In the 2002 Evaluation, examiners noted that Webster Bank had an excellent level of qualified community development investments and grants, particularly those that were not routinely provided by private investors. They commended the bank for acting as a leader with respect to its community development investments. During the evaluation period, Webster Bank made $22 million in investments. In 2002 and 2003, Webster Bank made more than $13.7 million in community development investments and grants.

Examiners reported that Webster Bank's delivery systems were readily accessible to all portions of the assessment areas and that 20 percent of its offices were in LMI geographies. They further commended Webster Bank's senior management for its leadership in providing community development services.

17. *See Interagency Questions and Answers Regarding Community Reinvestment, 66 Federal Register* 36,620 and 36,639 (2001).

18. At the time, Webster Bank was a savings bank supervised by the OTS. It converted to a national bank charter in April 2004.

19. The evaluation period was from November 1, 1999, to December 31, 2001. During this period, Webster Bank had four assessment areas. The bank's Hartford assessment area and the assessment area for Bridgeport, New Haven, Waterbury, and Danbury, all in Connecticut, received full-scope reviews.

20. Small businesses are businesses with gross annual revenues of $1 million or less. Small loans to businesses include loans with original amounts of $1 million or less that are either secured by nonfarm, nonresidential properties or classified as commercial and industrial loans.

21. The lending data of the aggregate lenders represent the cumulative lending for all financial institutions that have reported data in a particular area.

C. HMDA Data and Fair Lending

The Board also has carefully considered the lending record of Webster in light of comments received on the HMDA data reported by Webster Bank in 2002 and 2003.[22] The commenter alleged that Webster's lending evidenced systematic disparities by disproportionately denying applications for HMDA-reportable loans to minorities. Webster Bank's denial disparity ratios[23] for African-American and Hispanic applicants in 2002 and 2003 for the markets reviewed were comparable to, or were less favorable than, the ratios for the aggregate lenders during the same time period.

Although the HMDA data may reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial groups and persons at different income levels in certain local areas, the HMDA data generally do not indicate that Webster excluded any race or income segment of the population or geographic areas on a prohibited basis. The Board nevertheless is concerned when the record of an institution indicates disparities in lending and believes that all banks are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending, but also equal access to credit by creditworthy applicants regardless of race or income level. The Board recognizes, however, that HMDA data alone provide an incomplete measure of an institution's lending in its community because these data cover only a few categories of housing-related lending and provide only limited information about covered loans.[24] HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has not assisted adequately in meeting its community credit needs or has engaged in illegal lending discrimination.

Because of the limitations of HMDA data, the Board has considered these data carefully in light of other information, including examination reports that provide on-site evaluations of compliance with fair lending laws by the subsidiary depository and lending institutions of Webster. Examiners identified no violations of the antidiscrimination laws and regulations in the 2002 Evaluation and no substantive fair lending issues or concerns in Webster Bank's consumer compliance examinations. Examiners also noted that management implemented adequate fair lending policies and procedures, training programs, and internal reviews. After reviewing Webster Bank's advertisements and application files and holding discussions with management and staff, examiners concluded that applications were solicited from all segments of the community.

The record also indicates that Webster has taken various measures to help ensure compliance with fair lending laws.[25] Webster has instituted corporate-wide policies and procedures to help ensure compliance with all fair lending and other consumer protection laws and regulations. Webster has adopted a corporate Fair Lending Policy, enhanced fair-lending compliance training at all organization levels, and initiated the process of reviewing and updating the fair lending procedures of its various business lines. Webster Bank's Compliance Unit monitors the internal controls applicable to the wholesale, retail, and consumer lending operations and verifies that the internal controls system identifies fair-lending compliance risks or exceptions. The Compliance Unit also uses quality control testing to confirm that the system of internal controls in place is functioning properly at the transactional level. Webster Bank states that the fair-lending compliance functions report to the CRA Officer, who is responsible for coordinating and reviewing fair lending compliance at the Bank. Webster Bank's Internal Audit Department regularly reviews the lending activities to assess compliance with consumer protection laws and regulations. In addition, Webster Bank reports that it provides compliance training to bank employees.

The Board also has considered the HMDA data in light of other information, including the CRA performance records of the subsidiary depository institutions of Webster. These records demonstrate that Webster is active in helping to meet the credit needs of its entire community.[26]

22. The Board analyzed 2002 and 2003 HMDA data reported by Webster Bank in specific Metropolitan Statistical Areas and statewide in Connecticut. During that period, Webster Bank operated only in Connecticut. Webster Bank acquired its Massachusetts and Rhode Island operations in May 2004 through its acquisition of First Federal Savings Bank of America, Swansea, Massachusetts, and the bank opened its New York branches in 2004.

23. The denial disparity ratio equals the denial rate for a particular racial category (for example, African-American) divided by the denial rate for whites.

24. The data, for example, do not account for the possibility that an institution's outreach efforts may attract a larger proportion of marginally qualified applicants than other institutions attract and do not provide a basis for an independent assessment of whether an applicant who was denied credit was, in fact, creditworthy. Credit history problems and excessive debt levels relative to income (reasons most frequently cited for a credit denial) are not available from HMDA data.

25. The commenter expressed general concerns about Webster Bank's safeguards against predatory lending. Webster Bank has arrangements to refer subprime applicants to two third-party subprime mortgage lenders. According to Webster, the purpose of each arrangement is to provide applicants with an array of mortgage loan options after the bank has determined that they do not qualify for a loan Webster offers. Applicants are informed of these mortgage loan alternatives only after their loan applications have been reviewed under a second-review process at Webster Bank. Under an arrangement with one subprime lender, Webster Bank refers potential candidates to the lender. Under an agreement with the other subprime lender, Webster Bank originates the loan only after the subprime lender makes a creditworthiness determination and provides Webster Bank with a written commitment to purchase the loan immediately. Webster Bank has represented that it reviews and approves the lender's underwriting criteria and the terms and features of these loans before origination to ensure that there are no predatory lending practices. The OCC, as Webster Bank's primary supervisor, will examine Webster Bank's compliance with applicable statutes and regulations. Furthermore, the Board previously has noted that subprime lending is a permissible activity that provides needed credit to consumers who have difficulty meeting conventional underwriting criteria. *See, e.g., Royal Bank of Canada*, 88 *Federal Reserve Bulletin* 385, 388 (2002).

26. The commenter also expressed concern about Webster Bank's alleged involvement in mortgage lending at high rates and the suffi-

D. Branch Issues

The commenter also expressed concern about the effect on the convenience and needs of State Bank's communities from Webster's plan to divest the acquired branch and loan production office in Wisconsin, asserting that this plan would be disruptive to retail customers of the bank. Webster represented it is taking the following steps to provide continuity in banking services to the affected communities: retaining senior management of State Bank for a period of time after Webster's acquisition of Eastern, planning to sell State Bank's local operations and facilities as a single unit, and marketing this sale primarily to local banking organizations. In addition, Webster hopes to consummate the sale of State Bank's community banking operations as soon as possible after consummating the acquisition.

E. Conclusion on Convenience and Needs and CRA Performance

The Board has carefully considered all the facts of record, including reports of examination of the CRA records of the institutions involved, information provided by Webster and Eastern, comments on the proposal, and confidential supervisory information. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that considerations relating to the convenience and needs factor and the CRA performance records of the relevant depository institutions are consistent with approval.

Conclusion

Based on the foregoing and in light of all the facts of record, the Board has determined that the application should be, and hereby is, approved. In reaching this conclusion, the Board has considered all the facts of record in light of the factors it is required to consider under the BHC Act and other applicable statutes.[27] The Board's approval is specifically conditioned on compliance by Webster with all the conditions imposed in this order and the commitments made to the Board in connection with this proposal, and receipt of all other regulatory approvals. For purposes of this action, the conditions and these commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

The acquisition shall not be consummated before the fifteenth calendar day after the effective date of this order, or later than three months after the effective date of this order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of Boston, acting pursuant to delegated authority.

By order of the Board of Governors, effective February 4, 2005.

Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Gramlich, Bies, Olson, Bernanke, and Kohn.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

ciency of the bank's safeguards against predatory lending practices. The commenter cited a 2001 press report of a lawsuit by homeowners in a moderate-income housing development in Connecticut. Webster Bank became involved in the lawsuit when it acquired another bank. In 2001, the Connecticut Attorney General's Office announced a settlement with an acknowledgement that Webster Bank played a major role in resolving the predecessor bank's litigation.

27. The commenter requested that the Board hold a public hearing or meeting on the proposal. Section 3 of the BHC Act does not require the Board to hold a public hearing on an application unless the appropriate supervisory authority for any of the banks to be acquired makes a timely written recommendation of denial of the application. The Board has not received such a recommendation from any supervisory authority. Under its rules, the Board also may, in its discretion, hold a public meeting or hearing on an application to acquire a bank if a meeting or hearing is necessary or appropriate to clarify factual issues related to the application and to provide an opportunity for testimony. 12 CFR 225.16(e). The Board has considered carefully the commenter's request in light of all the facts of record. As noted, the public has had ample opportunity to submit comments on the proposal and, in fact, the commenter has submitted written comments that the Board has considered carefully in acting on the proposal. The commenter's request fails to demonstrate why its written comments do not present its views adequately or why a meeting or hearing otherwise would be necessary or appropriate. The request also fails to identify disputed issues of fact that are material to the Board's decision that would be clarified by a public hearing or meeting. For these reasons, and based on all the facts of record, the Board has determined that a public hearing or meeting is not required or warranted in this case. Accordingly, the request for a public hearing or meeting on the proposal is denied.

Westamerica Bancorporation
San Rafael, California

Westamerica Bank
San Rafael, California

Order Approving the Merger of Bank Holding Companies, Merger of Banks, and Establishment of Branches

Westamerica Bancorporation ("Westamerica"), a bank holding company within the meaning of the Bank Holding Company Act ("BHC Act") has requested the Board's approval under section 3 of the BHC Act[1] to merge with Redwood Empire Bancorp ("Redwood"), with Westamerica as the surviving entity, and thereby indirectly acquire Redwood's wholly owned subsidiary, National Bank of the Redwoods ("Redwood Bank"), Santa Rosa, California. In addition, Westamerica's subsidiary bank, Westamerica Bank, a state member bank, has requested the Board's approval under section 18(c) of the Federal Deposit Insurance Act[2] ("Bank Merger Act") to merge with Redwood Bank, with Westamerica Bank as the surviving entity. Westamerica Bank has also applied under section 9 of the Federal Reserve Act ("FRA") to retain and

1. 12 U.S.C. § 1842.
2. 12 U.S.C. § 1828(c).

operate branches at the location of Redwood Bank's main office and branches.[3]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published in the *Federal Register* (69 *Federal Register* 71,056 (2004)) and locally in accordance with the relevant statutes and the Board's Rules of Procedure.[4] As required by the BHC Act and the Bank Merger Act, reports on the competitive effects of the mergers were requested from the United States Attorney General and the appropriate banking agencies. The time for filing comments has expired, and the Board has considered the applications and all comments received in light of the factors set forth in section 3 of the BHC Act, the Bank Merger Act, and the FRA.

Westamerica, with total consolidated assets of approximately \$4.6 billion, is the 23rd largest banking organization in California, controlling deposits of approximately \$3.5 billion.[5] Redwood, with total consolidated assets of approximately \$523 million, is the 89th largest banking organization in California, controlling deposits of approximately \$455.3 million. On consummation of the proposal and accounting for the proposed divestiture, Westamerica would become the 22nd largest depository organization in California, controlling deposits of approximately \$4.0 billion, which would represent less than 1 percent of the total amount of deposits of insured depository institutions in the state.[6]

Competitive Considerations

Section 3 of the BHC Act and the Bank Merger Act prohibit the Board from approving a proposal that would result in a monopoly or would be in furtherance of an attempt to monopolize the business of banking in any relevant banking market. The BHC Act and the Bank Merger Act also prohibit the Board from approving a bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[7]

Westamerica Bank and Redwood Bank compete directly in the Lake County, Santa Rosa, and Ukiah banking markets in California.[8] The Board has reviewed carefully the competitive effects of the proposal in each of these banking markets in light of all the facts of record, including public comment on the proposal.[9] In particular, the Board has considered the number of competitors that would remain in the markets, the relative shares of total deposits of depository institutions in the markets ("market deposits") controlled by Westamerica Bank and Redwood Bank,[10] the concentration level of market deposits and the increase in this level as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Merger Guidelines ("DOJ Guidelines"),[11] other characteristics of the markets, and commitments made by Westamerica to divest a branch.

In the Lake County banking market, Westamerica Bank is the largest depository organization, controlling approximately \$159.4 million in deposits, which represents approximately 27.3 percent of market deposits. Redwood Bank is the sixth largest depository institution in the market, controlling approximately \$50.1 million of deposits, which represents approximately 8.6 percent of market deposits. To mitigate the potentially adverse competitive effects of the proposal in the Lake County banking market, Westamerica Bank has committed to divest one branch with at least \$43.1 million in deposits in the market to a competitor that is competitively suitable to the Board.[12] On consummation of the proposal and after accounting for the proposed divestiture, Westamerica Bank would remain the largest depository organization in the market, controlling

3. 12 U.S.C. § 321. These branches are listed in Appendix A.

4. 12 CFR 262.3(b).

5. Asset data are as of September 30, 2004, and deposit data and state ranking data are as of June 30, 2004.

6. In this context, the term "insured depository institutions" includes insured commercial banks, savings banks, and savings associations.

7. *See* 12 U.S.C. § 1842(c)(1); 12 U.S.C. § 1828(c)(5).

8. The Lake County banking market is defined as Lake County. The Santa Rosa banking market is defined as the Santa Rosa Ranally Metropolitan Area and the town of Cloverdale in Sonoma County. The Ukiah banking market is defined as the towns of Ukiah, Hopland, and Redwood Valley in Mendocino County.

9. One commenter expressed general concern about the competitive effects of this proposal in the Lake County banking market.

10. Deposit and market share data are as of June 30, 2004, and are based on calculations in which the deposits of thrift institutions are included at 50 percent. The Board previously has indicated that thrift institutions have become, or have the potential to become, significant competitors of commercial banks. *See, e.g., Midwest Financial Group*, 75 *Federal Reserve Bulletin* 386 (1989); *National City Corporation*, 70 *Federal Reserve Bulletin* 743 (1984). Thus, the Board regularly has included thrift deposits in the market share calculation on a 50 percent weighted basis. *See, e.g., First Hawaiian, Inc.*, 77 *Federal Reserve Bulletin* 52 (1991).

11. Under the DOJ Guidelines, a market is considered moderately concentrated if the post-merger HHI is between 1000 and 1800, and a market is considered highly concentrated if the post-merger HHI is more than 1800. The Department of Justice ("DOJ") has informed the Board that a bank merger or acquisition generally will not be challenged (in the absence of other factors indicating anticompetitive effects) unless the post-merger HHI is at least 1800 and the merger increases the HHI by more than 200 points. The DOJ has stated that the higher than normal HHI thresholds for screening bank mergers and acquisitions for anticompetitive effects implicitly recognize the competitive effects of limited-purpose and other nondepository financial entities.

12. Westamerica has committed that, before consummating the proposed merger with Redwood, it will execute an agreement for the proposed divestiture in the Lake County banking market, consistent with this order, with a purchaser determined by the Board to be competitively suitable. Westamerica also has committed to complete the divestiture within 180 days after consummation of the proposed merger. In addition, Westamerica has committed that, if it is unsuccessful in completing the proposed divestiture within such time period, it will transfer the unsold branch to an independent trustee who will be instructed to sell the branch to an alternate purchaser or purchasers in accordance with the terms of this order and without regard to price. Both the trustee and any alternate purchaser must be deemed acceptable to the Board. *See BankAmerica Corporation*, 78 *Federal Reserve Bulletin* 338 (1992); *United New Mexico Financial Corporation*, 77 *Federal Reserve Bulletin* 484 (1991).

approximately $166.4 million of deposits, which represents approximately 27.6 percent of market deposits.[13] The HHI would increase by not more than 157 points and would not exceed 1739.

After the proposed divestiture, consummation of the proposal would be consistent with the DOJ Guidelines. At least seven other competitors would remain in the market. The second largest bank competitor in the market would control approximately 18 percent of market deposits, and two other bank competitors would each control more than 10 percent of market deposits.

Consummation of the proposal would be consistent with Board precedent and within the thresholds in the DOJ Guidelines in the Santa Rosa and Ukiah banking markets.[14] After consummation, the Santa Rosa market would remain moderately concentrated, with only a modest increase in market concentration as measured by the HHI, and numerous competitors would remain in the market. Although the Ukiah banking market would remain highly concentrated after consummation of the proposal, the increase in market concentration as measured by the HHI would be small and several other competitors would remain in the banking market.

The DOJ has reviewed the proposal and has advised the Board that consummation of the proposal would not likely have a significantly adverse effect on competition in any relevant banking market. The other federal banking agencies also have been afforded an opportunity to comment and have not objected to the proposal.

Based on all facts of record, the Board concludes that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of resources in any of the three banking markets in which Westamerica Bank and Redwood Bank directly compete or in any other relevant banking market. Accordingly, based on all the facts of record and subject to completion of the proposed divestiture, the Board has determined that competitive considerations are consistent with approval.

Financial, Managerial, and Supervisory Considerations

The BHC Act, the Bank Merger Act, and the FRA require the Board to consider the financial and managerial resources and future prospects of the companies and depository institutions involved in the proposal and certain other supervisory factors. The Board has carefully considered these factors in light of all the facts of record including, among other things, confidential reports of examination and other supervisory information received from the federal and state banking supervisors of the organizations involved, publicly reported and other financial information, information provided by the applicants, and public comments on the proposal.

In evaluating financial factors in expansion proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary banks and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the effect of the transaction on the financial condition of the applicant and target, including their capital position, asset quality, earnings prospects, and the impact of the proposed funding of the transaction.

Based on its review of these factors, the Board finds that Westamerica has sufficient financial resources to effect the proposal. Westamerica and Westamerica Bank are well capitalized and would remain so on consummation of this proposal. The proposed transaction would be funded by a cash payment and an exchange of shares, and Westamerica would not incur debt as part of this proposal.

The Board also has evaluated the managerial resources of the organizations involved, including the proposed combined organization. The Board has reviewed the examination records of Westamerica, Redwood, and their subsidiary depository institutions, including assessments of their management, risk management systems, and operations. In addition, the Board has considered its supervisory experience and that of the other relevant banking supervisory agencies with the organizations and their records of compliance with applicable banking law. The Board also has considered Westamerica's plans to integrate Redwood and Redwood Bank and the proposed management, including the risk management systems, of the resulting organization.

Based on all the facts of record, the Board has concluded that the financial and managerial resources and future prospects of the organizations and the other supervisory factors involved are consistent with approval of the proposal.

Convenience and Needs Considerations

In acting on this proposal, the Board also is required to consider the effects of the proposal on the convenience and needs of the communities to be served and to take into account the records of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[15] The CRA requires the federal financial supervisory agencies to encourage financial institutions to help meet the credit needs of local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account an institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank expansionary proposals.

13. Westamerica Bank's deposits after the divestiture reflect a decrease in branch deposits since June 30, 2004.

14. The effects of the proposal on the concentration of banking resources in these banking markets are described in Appendix B.

15. 12 U.S.C. § 2901 *et seq.*

The Board has considered carefully the convenience and needs factor and the CRA performance records of Westamerica Bank and Redwood Bank in light of all the facts of record, including public comment on the proposal. Two commenters expressed concerns about Westamerica Bank's record of meeting the banking needs of the LMI communities it serves, particularly in Lake County, California.[16] In addition, commenters expressed concern about potential branch closings and other possible reductions in service resulting from the proposed merger.[17]

A. CRA Performance Evaluations

As provided in the BHC Act and the Bank Merger Act, the Board has evaluated the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the CRA performance records of the relevant insured depository institutions. An institution's most recent CRA performance evaluation is a particularly important consideration in the applications process because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisor.[18]

Westamerica Bank received an overall "satisfactory" rating at its most recent CRA performance evaluation by the Federal Reserve Bank of San Francisco, as of April 12, 2004 ("2004 CRA Evaluation").[19] Redwood Bank also received an overall "satisfactory" rating at its most recent CRA performance evaluation by the Office of the Comptroller of the Currency, as of November 12, 2003.[20]

B. CRA Performance of Westamerica Bank

In the 2004 CRA Evaluation, Westamerica Bank received a "high satisfactory" rating under the lending test. Examiners noted that Westamerica Bank's primary business strategy was to serve the needs of small- and middle-market businesses and professionals through the creation of ongoing rather than transactionally based banking arrangements. Therefore, the lending test evaluation focused primarily on Westamerica Bank's record of small business loans[21] and loans to small businesses,[22] as well as community development loans. Examiners concluded that Westamerica Bank's level of lending reflected a good responsiveness to the credit needs of its assessment areas.[23] In the 2004 CRA Evaluation, examiners also noted that the overall distribution of loans among borrowers of different income levels and businesses of different revenue sizes was good throughout its assessment areas. Examiners characterized Westamerica Bank's geographic distribution of loans throughout its assessment areas as good and found that the bank's lending was reasonably dispersed among the assessment area's census tracts of different income levels.

The Board has also carefully considered the lending record of Westamerica Bank in light of the comments received on the bank's record. A review of the small business lending data indicates that, although Westamerica Bank's percentage of small business loans to businesses in LMI geographies in California was slightly lower than the percentages for the aggregate lenders in 2002 and 2003, the bank has improved its lending to LMI geographies during this period. In addition, Westamerica Bank increased the number of loans to small businesses in LMI census tracts by more than 20 percent in 2003. Westamerica Bank also increased its small-business-related lending in predominantly minority census tracts in 2003. Westamerica Bank made twice as many small businesses loans in predominantly minority census tracts throughout California in 2003 as it made in 2002, and tripled the number of loans to small businesses in predominantly minority census tracts during the same period.[24]

In the 2004 CRA Evaluation of the Lake County assessment area, examiners described Westamerica Bank's geographic distribution of small business loans as "excellent." Examiners found that Westamerica Bank's percentage of small business loans to businesses in moderate-income geographies in Lake County exceeded the percentage of such loans made by the aggregate lenders.[25]

Examiners praised Westamerica Bank for a relatively high level of community development loans throughout its assessment areas. During the evaluation period,

16. The commenters also criticized Westamerica Bank's lending to small businesses in LMI census tracts in Alameda County, California. Westamerica Bank had two limited-scope assessment areas in Alameda County, Alameda East and Alameda West. Alameda East consists of the cities of Dublin, Livermore, and Pleasanton, and has no LMI census tracts. Alameda West consists of the cities of Alameda, Albany, Berkeley, Emeryville, Oakland, and Piedmont. Based on 1990 census data, Westamerica Bank's percentage of small business loans to businesses in LMI geographies in Alameda West exceeded the percentage of such loans made by the aggregate of lenders ("aggregate lenders") in those geographies. The lending data of the aggregate lenders represent the cumulative lending for all financial institutions that have reported small business lending as part of their CRA data in a particular area.

17. The commenters also noted concerns about Westamerica possibly lending to an unaffiliated payday lender. Westamerica represented that it does not have any equity interest in any payday lender nor, to its knowledge, does it lend to any payday lender.

18. *See Interagency Questions and Answers Regarding Community Reinvestment*, 66 *Federal Register* 36,620 and 36,639 (2001).

19. The evaluation period for the 2004 CRA Evaluation was from January 1, 2002, through December 31, 2003.

20. The evaluation period for Redwood Bank's CRA performance evaluation was from January 1, 2000, through December 31, 2002.

21. In this context, "small business loans" are loans that have original amounts of $1 million or less and that either are secured by nonfarm nonresidential properties or are classified as commercial and industrial loans.

22. In this context, "small businesses" are businesses with gross annual revenues of $1 million or less.

23. At the time of the evaluation, Westamerica had 25 assessment areas, five of which received full-scope reviews. The full-scope assessment areas were Fresno, Kern, Lake, and Marin Counties, and the Gualala area, which is a large census tract in Mendocino County that includes the city of Point Arena.

24. See footnotes 21 and 22 for definitions of the terms "small business loans" and "small businesses."

25. The Lake County assessment area had no low-income geographies.

Westamerica Bank's community development loans totaled $82.6 million. In the Lake County assessment area, examiners described Westamerica Bank's community development loans as responsive in meeting the area's credit needs. During the evaluation period, the bank's community development loans in Lake County, which totaled $1.5 million, supported a school, a community development service provider for LMI individuals, and a tribal health consortium that had 85 percent of its patients living below the poverty level. Westamerica represented that from 2000 through 2004, it funded 11 community development loans totaling $17.1 million in Lake County, which helped provide affordable housing in moderate-income areas, and provided an additional $11.6 million in community development loans in Sonoma and Mendocino Counties.

In the 2004 CRA Evaluation, Westamerica Bank received a "high satisfactory" rating under the investment test.[26] During the evaluation period, the bank made 326 new investments totaling $45 million, including a $4.5 million investment for the creation of 675 affordable housing units. In particular, examiners praised Westamerica Bank's "good responsiveness" to community development needs with its community development investments in Lake County, despite infrequent opportunities for community equity investment. The examination noted the bank's purchase of statewide mortgage-backed securities that included loans on properties in Lake County.

Westamerica Bank also received a "high satisfactory" rating under the service test. Examiners observed that Westamerica Bank's delivery systems were readily accessible to all portions of its assessment areas.[27] Examiners noted that in Lake County, Westamerica Bank provided the only retail banking institution in the community in the Upper Lake area. Examiners noted that all the bank's branches offered a full range of products, including low-cost deposit accounts. Westamerica Bank also stated that it provides LMI customers with no-cost checking accounts. In addition, examiners noted that Westamerica Bank provided various community service programs, including a program designed to introduce LMI Spanish-speaking individuals to the bank's products and encourage them to apply for loans. The bank also provided "Basic Budgeting" seminars to teach financial literacy skills to LMI individuals and a "Senior Guard" program that helps senior citizens avoid predatory financial practices.

26. A commenter criticized Westamerica for refusing to disclose its charitable donations. The Board notes that neither the CRA nor the agencies' implementing rules require that depository institutions engage in charitable giving nor do they require depository institutions to publicly disclose their charitable giving.

27. One commenter stated that Westamerica declined to participate in the California Electronic Benefits Transfer Program (the "EBT Program") and thus denied recipients of electronic benefits transfers access to Westamerica's ATM network and opportunities to open accounts. The EBT Program is administered by California authorities. Neither the CRA nor the federal banking agencies' CRA regulations require depository institutions to offer any particular product or services overseen by state government agencies.

C. CRA Performance of Redwood Bank

As previously noted, Redwood Bank received an overall "satisfactory rating" at its most recent CRA performance evaluation. The bank received a "high satisfactory" rating under the lending test. Geographic distribution of Redwood Bank's home mortgage lending was considered good and distribution of its home mortgage loans to borrowers of different income levels was considered adequate, in light of the fact that Redwood Bank had sold its retail mortgage lending unit in 1999 and, consequently, had made fewer mortgage loans than in previous evaluations. Examiners considered Redwood Bank's geographic distribution of small business loans to be "excellent" and its distribution of loans to small businesses to be adequate. Examiners commended the bank's community development lending performance, noting that it had been "highly responsive to the affordable housing and community service needs of the area." Redwood Bank originated nine community development loans within its full-scope assessment area[28] during the evaluation period, totaling almost $6 million, to provide affordable housing and community services.

Redwood Bank received an "outstanding" rating under the investment test, reflecting its excellent volume of investments relative to its capacity to invest in its full-scope assessment area. The bank made 102 qualified investments totaling $3.5 million during the evaluation period, which examiners characterized as a significant allocation of resources in light of limited investment opportunities. A majority of the investments supported affordable housing.

Redwood Bank received a "high satisfactory" performance under the service test, based on its accessible branches and alternative delivery services and on its banking services that were tailored to the needs of its full-scope assessment area. Examiners noted that the bank's branches were accessible to essentially all of its assessment areas.

D. Branch Closures

Westamerica Bank has stated that it plans to consolidate four branches, none of which are in an LMI area, and that it will close one branch in a moderate income area. Westamerica Bank will have a branch within 2.7 miles of all the branches that will be closed or consolidated, and these remaining branches will provide accessible banking services to LMI individuals in its assessment areas.

In making the determination regarding these branches, Westamerica Bank followed its branch closing policy that requires it to consider the impact on the community, the business viability and profitability of the branch, branch usage, demographic growth or decline in the community, the impact on credit access, and the necessity of ensuring that the branch closing has no discriminatory impact. The policy requires that, before a final decision is made to close a branch, management must conduct an impact study to

28. The full-scope assessment area for Redwood Bank's CRA evaluation was the Santa Rosa Metropolitan Statistical Area.

assess the likely effects of the closure. In reviewing a branch closure in an LMI area, the impact study must include concerns and suggestions from the local community, an assessment of the closure's potential impact on customers, and other possible ways the community's credit needs might be met.[29]

The Board also has considered the fact that federal banking law provides a specific mechanism for addressing branch closings, and Westamerica Bank has stated that it will follow this policy when it closes or consolidates the branches.[30] In addition, the Board, as the appropriate federal supervisor of Westamerica Bank, will continue to review the bank's branch closing record in the course of conducting CRA performance evaluations.

E. Conclusion on Convenience and Needs and CRA Performance

The Board has carefully considered all the facts of record, including reports of examination of the CRA records of the institutions involved, information provided by Westamerica Bank, public comments on the proposal, and confidential supervisory information.[31] The proposed transaction would provide Redwood Bank's customers with a wider range of consumer retail products, such as NOW and IRA accounts, and loans subject to the larger lending limits of Westamerica Bank. The Board expects the resulting organization to continue to help serve the banking and credit needs of all its communities, including LMI areas. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that considerations relating to the convenience and needs factor and the CRA performance records of the relevant depository institutions are consistent with approval.[32]

Conclusion

Based on the foregoing and all facts of record, the Board has determined that the applications should be, and hereby are, approved. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act, the Bank Merger Act, and the FRA. The Board's approval is specifically conditioned on compliance by Westamerica with all the commitments made to the Board in connection with this proposal and the conditions imposed in this order. For purposes of this action, the commitments and conditions are deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

The proposed transactions may not be consummated before the fifteenth calendar day after the effective date of this order, or later than three months after the effective date of this order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of San Francisco, acting pursuant to delegated authority.

By order of the Board of Governors, effective January 26, 2005.

Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Gramlich, Bies, Olson, Bernanke, and Kohn.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

Appendix A

Addresses of Main Offices and Branches in California to be Acquired by Westamerica

Lakeport
650 North Main Street

Rohnert Park
6400 Redwood Drive

29. In Westamerica Bank's most recent CRA performance evaluation, examiners reviewed the bank's policy on closing branches. The examiners also noted that although Westamerica Bank closed six branches during the evaluation period, none of those closings adversely affected accessibility to the bank's services for LMI individuals, and that a large number of branches remained in LMI census tracts or readily accessible to LMI areas. They further noted that the bank opened a new branch in a moderate-income area of Fresno County and provided some alternative delivery systems targeted to LMI individuals, such as a mobile branch serving a low-income senior center in Napa County.

30. Section 42 of the Federal Deposit Insurance Act (12 U.S.C. § 1831r-1), as implemented by the Joint Policy Statement Regarding Branch Closings (64 *Federal Register* 34,844 (1999)), requires that a bank provide the public with at least 30 days' notice and the appropriate federal supervisory agency with at least 90 days' notice before the date of the proposed branch closing. The bank also is required to provide reasons and other supporting data for the closure, consistent with the institution's written policy for branch closings.

31. Two commenters expressed concern that Westamerica would not honor existing agreements between Redwood Bank and community groups. Both commenters further requested that Westamerica make certain community reinvestment commitments, meet with community representatives, or take certain other actions, and that the Board impose specific conditions on Westamerica. As the Board has previously explained, an applicant must demonstrate a satisfactory record of performance under the CRA without reliance on plans or commitments for future actions. The Board has stated consistently that neither the CRA nor the federal banking agencies' CRA regulations require depository institutions to provide commitments regarding future performance under the CRA, confer authority on the agencies to enforce commitments made to third parties, or require depository institutions to meet with, or enter into agreements with, any particular organization. The Board views the enforceability of pledges and agreements with third parties as matters outside the scope of the CRA. *See, e.g., J.P. Morgan Chase & Co.*, 90 *Federal Reserve Bulletin* 352 (2004).

32. One commenter has requested the Board to arrange an informal meeting between the commenter and Westamerica. The Board's Rules of Procedure allow a Reserve Bank to hold a private meeting to provide a forum for narrowing issues and resolving differences between an applicant and commenter, if appropriate, but does not require any person to attend an informal meeting. *See* 12 CFR 262.25(c). Westamerica declined to meet with the commenter through this process.

Santa Rosa
424 Farmers Lane
2800 Cleveland Avenue
111 Santa Rosa Avenue

Sebastopol
800 Gravenstein Highway North

Ukiah
325 East Perkins

Appendix B

Banking Market Data

Santa Rosa, California

Westamerica Bank is the eighth largest depository institution in the Santa Rosa banking market, controlling deposits of approximately $276 million, which represent approximately 5.1 percent of market deposits. Redwood Bank is the sixth largest depository institution in the market, controlling deposits of approximately $352 million, which represent approximately 6.5 percent of market deposits. On consummation of the proposal, Westamerica Bank would become the fifth largest depository institution in the market, controlling deposits of approximately $628 million, which represent approximately 11.5 percent of market deposits. Sixteen other depository institutions would remain in the banking market. The HHI would increase by 65 points to 1151.

Ukiah, California

Westamerica Bank is the seventh largest depository institution in the Ukiah banking market, controlling deposits of approximately $20.7 million, which represent approximately 3.1 percent of market deposits. Redwood Bank is the fourth largest depository institution in the market, controlling deposits of approximately $53 million, which represent approximately 8 percent of market deposits. On consummation of the proposal, Westamerica Bank would become the third largest depository institution in the market, controlling deposits of approximately $74 million, which represent approximately 11.1 percent of market deposits. Five other depository institutions would remain in the banking market. The HHI would increase by 49 points to 3666.

ORDERS ISSUED UNDER INTERNATIONAL BANKING ACT

Nacional Financiera, S.N.C.
Mexico City, Mexico

Order Approving Establishment of a Representative Office

Nacional Financiera, S.N.C. ("Bank"), Mexico City, Mexico, a foreign bank within the meaning of the International Banking Act ("IBA"), has applied under section 10(a) of the IBA (12 U.S.C. §3107(a)) to establish a representative office in Los Angeles, California. The Foreign Bank Supervision Enhancement Act of 1991, which amended the IBA, provides that a foreign bank must obtain the approval of the Board to establish a representative office in the United States.

Notice of the application, affording interested persons an opportunity to submit comments, has been published in a newspaper of general circulation in Los Angeles, California (*Los Angeles Daily Journal*, October 12, 2004). The time for filing comments has expired, and all comments have been considered.

Bank, with total consolidated assets of approximately $19.9 billion,[1] is the largest development bank in Mexico. Bank primarily funds loans by Mexican banks and other financial intermediaries to private-sector participants in financing programs established by Bank to further economic policies of the Mexican government. As financing agent for the Mexican government, Bank also disburses loan proceeds provided by multilateral agencies and foreign governments to entities in Mexico's public and private sectors. Bank is wholly owned by the Mexican government and has branches the United Kingdom and the Cayman Islands and a representative office in Japan. Bank engages in securities activities in the United States through a subsidiary.

The proposed representative office would act as a liaison with existing and potential customers of Bank and with multilateral organizations, U.S. government agencies, and other entities that provide funding for development projects in Mexico. The office would solicit new business, conduct research, and perform preliminary and servicing steps in connection with lending. It would provide information to U.S. businesses seeking investment opportunities in Mexico through programs offered by the Bank and to Mexican businesses regarding products and services offered under funding initiatives of the U.S. government.

Under the IBA and Regulation K, in acting on an application by a foreign bank to establish a representative office, the Board must consider whether the foreign bank (1) engages directly in the business of banking outside of the United States; (2) has furnished to the Board the information it needs to assess the application adequately; and (3) is subject to comprehensive supervision on a consolidated basis by its home country supervisor (12 U.S.C. §3107(a)(2); 12 CFR 211.24(d)(2)).[2] The Board also may

1. Unless otherwise indicated, data are as of September 30, 2004.

2. In assessing the supervision standard, the Board considers, among other factors, the extent to which the home country supervisors:

(i) Ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide;
(ii) Obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise;
(iii) Obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic;

consider additional standards set forth in the IBA and Regulation K (12 U.S.C. §3105(d)(3)-(4); 12 CFR 211.24(c)(2)). The Board will consider that the supervision standard has been met where it determines that the applicant bank is subject to a supervisory framework that is consistent with the activities of the proposed representative office, taking into account the nature of such activities.[3] This is a lesser standard than the comprehensive, consolidated supervision standard applicable to applications to establish branch or agency offices of a foreign bank. The Board considers the lesser standard sufficient for approval of representative office applications because representative offices may not engage in banking activities (12 CFR 211.24(d)(2)).

As noted above, Bank engages directly in the business of banking outside the United States. Bank also has provided the Board with information necessary to assess the application through submissions that address the relevant issues.

With respect to supervision by home country authorities, the Board has considered the following information. The National Banking and Securities Commission ("CNBV"), a branch of the Ministry of Finance and Public Credit, is the primary regulatory and supervisory authority for Mexican banks, including commercial and development banks, and, as such, is the home country supervisor of Bank. The Board previously has considered the supervisory regime in Mexico for commercial banks.[4] The CNBV's supervision and regulation of development banks in Mexico is substantially similar to that of commercial banks, and there is no difference with respect to capital adequacy requirements and limits on credit concentrations, large credit exposures, and foreign currency exposure. Bank is subject to on-site examinations by the CNBV at least annually, and Bank must submit annual audited financial statements and monthly unaudited financial statements.

Bank is authorized by the Bank of Mexico to participate in certain financial markets, including foreign exchange markets, and is required to file a number of financial reports with the Bank of Mexico related to its trading activity, capital position, and counterparty positions. Bank also is subject to supervision by the Secretariat of Public Function, which monitors for public corruption and governmental transparency, and the Superior Auditor of the Federation, which audits the disbursement of public funds.

Based on all the facts of record, it has been determined that Bank is subject to a supervisory framework that is consistent with the activities of the proposed representative office, taking into account the nature of such activities.

The additional standards set forth in section 7 of the IBA and Regulation K (*see* 12 U.S.C. §3105(d)(3)–(4); 12 CFR 211.24(c)(2)) have also been taken into account. The CNBV has authorized Bank to establish the proposed office.

With respect to the financial and managerial resources of Bank, taking into consideration Bank's record of operations in its home country, its overall financial resources, and its standing with its home country supervisors, financial and managerial factors are consistent with approval of the proposed representative office. Bank appears to have the experience and capacity to support the proposed representative office and has established controls and procedures for the proposed representative office to ensure compliance with U.S. law, as well as controls and procedures for its worldwide operations generally.

Mexico is a member of the Financial Action Task Force and subscribes to its recommendations regarding measures to combat money laundering and international terrorism. In accordance with these recommendations, Mexico has enacted laws and created legislative and regulatory standards to deter money laundering, terrorist financing, or other illicit activities. Money laundering is a criminal offense in Mexico, and credit institutions are required to establish internal policies, procedures, and systems for the detection and prevention of money laundering throughout their worldwide operations. Bank has policies and procedures to comply with these laws and regulations, and these are monitored by governmental entities responsible for anti-money-laundering compliance.

With respect to access to information on Bank's operations, the restrictions on disclosure in relevant jurisdictions in which Bank operates have been reviewed and relevant government authorities have been communicated with regarding access to information. Bank has committed to make available to the Board such information on the operations of Bank and any of its affiliates that the Board deems necessary to determine and enforce compliance with the IBA, the Bank Holding Company Act of 1956, as amended, and other applicable federal law. To the extent that the provision of such information to the Board may be prohibited by law or otherwise, Bank has committed to cooperate with the Board to obtain any necessary consents or waivers that might be required from third parties for disclosure of such information. In addition, subject to certain conditions, the CNBV may share information on Bank's operations with other supervisors, including the Board. In light of these commitments and other facts of record, and subject to the condition described below, it has been determined that Bank has provided adequate assurances of access to any necessary information that the Board may request.

On the basis of all the facts of record, and subject to the commitments made by Bank and the terms and conditions

(iv) Receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis;

(v) Evaluate prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis.

These are indicia of comprehensive, consolidated supervision. No single factor is essential, and other elements may inform the Board's determination.

3. *See, e.g., Jamaica National Building Society,* 88 *Federal Reserve Bulletin* 59 (2002); *RHEINHYP Rheinische Hypothekenbank AG,* 87 *Federal Reserve Bulletin* 558 (2001); *see also Promstroybank of Russia,* 82 *Federal Reserve Bulletin* 599 (1996); *Komercni Banka, a.s.,* 82 *Federal Reserve Bulletin* 597 (1996); *Commercial Bank "Ion Tiriac," S.A.,* 82 *Federal Reserve Bulletin* 592 (1996).

4. *See, e.g., BBVA Bancomer, S.A.,* 89 *Federal Reserve Bulletin* 146 (2003); *Banpais S.A.,* 81 *Federal Reserve Bulletin* 204 (1995).

set forth in this order, Bank's application to establish the representative office is hereby approved.[5] Should any restrictions on access to information on the operations or activities of Bank or any of its affiliates subsequently interfere with the Board's ability to obtain information to determine and enforce compliance by Bank or its affiliates with applicable federal statutes, the Board may require or recommend termination of any of Bank's direct and indirect activities in the United States. Approval of this application also is specifically conditioned on compliance by Bank with the commitments made in connection with this application and with the conditions in this order.[6] The commitments and conditions referred to above are conditions imposed in writing by the Board in connection with its decision and may be enforced in proceedings against Bank and its affiliates under 12 U.S.C. § 1818.

By order, approved pursuant to authority delegated by the Board, effective February 11, 2005.

ROBERT DEV. FRIERSON
Deputy Secretary of the Board

FINAL ENFORCEMENT DECISIONS ISSUED BY THE BOARD OF GOVERNORS

In the Matter of a Notice to Prohibit Further Participation Against

Kenneth L. Coleman,
Former Employee,
PNC Bank,
Pittsburgh, Pennsylvania
and
Mellon Bank, N.A.,
Pittsburgh, Pennsylvania

Docket No. OCC-AA-EC-04-43

Final Decision

This is an administrative proceeding pursuant to the Federal Deposit Insurance Act ("the FDI Act") in which the Office of the Comptroller of the Currency of the United States of America ("OCC") seeks to prohibit the Respondent, Kenneth L. Coleman ("Respondent"), from further participation in the affairs of any financial institution because of his conduct as an employee of two national banks, PNC Bank ("PNC") and Mellon Bank, N.A. ("Mellon"), both of Pittsburgh, Pennsylvania. Under the FDI Act, the OCC may initiate a prohibition proceeding against a former employee of a national bank, but the Board must make the final determination whether to issue an order of prohibition.

Upon review of the administrative record, the Board issues this Final Decision adopting the Recommended Decision of Administrative Law Judge Ann Z. Cook (the "ALJ"), and orders the issuance of the attached Order of Prohibition.

I. Statement of the Case

A. Statutory and Regulatory Framework

Under the FDI Act and the Board's regulations, the ALJ is responsible for conducting proceedings on a notice of charges. 12 U.S.C. § 1818(e)(4). The ALJ issues a recommended decision that is referred to the deciding agency together with any exceptions to those recommendations filed by the parties. The Board makes the final findings of fact, conclusions of law, and determination whether to issue an order of prohibition in the case of prohibition orders sought by the OCC. *Id.*; 12 CFR 263.40.

The FDI Act sets forth the substantive basis upon which a federal banking agency may issue against a bank official or employee an order of prohibition from further participation in banking. To issue such an order, the Board must make each of three findings: (1) that the respondent engaged in identified *misconduct*, including a violation of law or regulation, an unsafe or unsound practice or a breach of fiduciary duty; (2) that the conduct had a specified *effect*, including financial loss to the institution or gain to the respondent; and (3) that the respondent's conduct involved either personal dishonesty or a willful or continuing disregard for the safety or soundness of the institution. 12 U.S.C. § 1818(e)(1)(A)–(C).

An enforcement proceeding is initiated by filing and serving on the respondent a notice of intent to prohibit. Under the OCC's and the Board's regulations, the respondent must file an answer within 20 days of service of the notice. 12 CFR 19.19(a) and 263.19(a). Failure to file an answer constitutes a waiver of the respondent's right to contest the allegations in the notice, and a final order may be entered unless good cause is shown for failure to file a timely answer. 12 CFR 19.19(c)(1) and 263.19(c)(1).

B. Procedural History

On November 22, 2004, the OCC served upon Respondent a Notice of Intention to Prohibit Further Participation and Notice of Charges for Restitution ("Notice") that sought, *inter alia*, an order of prohibition against Respondent based on his actions of stealing funds while employed by PNC and Mellon. Specifically, the Notice alleged that while employed by PNC, Respondent stole funds on October 14, 1999, November 26, 1999, and December 1, 1999 by inflating the amount of customer deposits and subsequently depositing the surplus amount into his own account. After

5. Approved by the Director of the Division of Banking Supervision and Regulation, with the concurrence of the General Counsel, pursuant to authority delegated by the Board.

6. The Board's authority to approve the establishment of the proposed representative office parallels the continuing authority of the State of California to license offices of a foreign bank. The Board's approval of this application does not supplant the authority of the State of California or its agent, the California Department of Financial Institutions ("Department"), to license the proposed office of Bank in accordance with any terms or conditions that the Department may impose.

Respondent paid partial restitution to PNC in the amount of $979.77, PNC currently maintains an outstanding loss of $1,590.23. The Notice further alleged that while employed by Mellon, Respondent stole $810 in cash after processing a combined check and cash transaction. Mellon maintains a loss of $810 as the result of Respondent's action.

The Notice directed Respondent to file an answer within 20 days and warned that failure to do so would constitute a waiver of his right to appear and contest the allegations. The record shows that the Respondent received service of the Notice. Nonetheless, Respondent failed to file an answer within the 20-day period.

On or about January 3, 2005, Enforcement Counsel filed a Motion for Entry of an Order of Default. The motion was served on Respondent in accordance with the OCC's rules, but he did not respond to it. Finally, on or about January 4, 2005, the ALJ issued an Order to Show Cause, which was mailed to the address at which Respondent had received the Notice. The order provided Respondent until January 21, 2005 to file an answer to the Notice and show good cause for failing to do so previously. The ALJ subsequently amended that order, providing Respondent until January 28, 2005 to respond. The amended order also was sent to the address at which Respondent had received the Notice. Respondent ignored the Order to Show Cause and has never filed an answer to the Notice.

II. Discussion

The OCC's Rules of Practice and Procedure set forth the requirements of an answer and the consequences of a failure to file an answer to a Notice. Under the Rules, failure to file a timely answer "constitutes a waiver of [a respondent's] right to appear and contest the allegations in the notice." 12 CFR 19.19(c). If the ALJ finds that no good cause has been shown for the failure to file, the judge "shall file . . . a recommended decision containing the findings and the relief sought in the notice." *Id.* An order based on a failure to file a timely answer is deemed to be issued by consent. *Id.*

In this case, Respondent failed to file an answer despite notice to him of the consequences of such failure, and also failed to respond to the ALJ's Order to Show Cause. Respondent's failure to file an answer constitutes a default.

Respondent's default requires the Board to consider the allegations in the Notice as uncontested. The Notice alleges, and the Board finds, that on four separate occasions between October 14, 1999 and February 29, 2000, Respondent stole funds from PNC and Mellon, respectively, while he was processing transactions as part of his employment at each of these banks. Respondent received a total of $3,380 as a result of his actions. After Respondent partially paid restitution to PNC Bank, PNC maintains a loss of $1,590.23 and Mellon maintains a loss of $810.

This conduct by Respondent meets all the criteria for entry of an order of prohibition under 12 U.S.C. § 1818(e). It is a violation of law, breach of fiduciary duty, and an unsafe or unsound practice for a bank employee to steal funds from the bank at which he is employed. Respondent's action caused gain to himself, as well as loss to each of the banks. Finally, such actions also exhibit personal dishonesty. Accordingly, the requirements for an order of prohibition have been met and the Board hereby issues such an order.

Conclusion

For these reasons, the Board orders the issuance of the attached Order of Prohibition.

By Order of the Board of Governors, this 1st day of March 2005.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Jennifer J. Johnson
Secretary of the Board

Order of Prohibition

WHEREAS, pursuant to section 8(e) of the Federal Deposit Insurance Act, as amended, (the "FDI Act") (12 U.S.C. § 1818(e)), the Board of Governors of the Federal Reserve System ("the Board") is of the opinion, for the reasons set forth in the accompanying Final Decision, that a final Order of Prohibition should issue against KENNETH L. COLEMAN ("Coleman"), a former employee and institution-affiliated party, as defined in Section 3(u) of the FDI Act (12 U.S.C § 1813(u)), of PNC Bank, Pittsburgh, Pennsylvania and Mellon Bank, N.A., Pittsburgh, Pennsylvania.

NOW, THEREFORE, IT IS HEREBY ORDERED, pursuant to section 8(e) of the FDI Act, 12 U.S.C. § 1818(e), that:

1. In the absence of prior written approval by the Board, and by any other Federal financial institution regulatory agency where necessary pursuant to section 8(e)(7)(B) of the Act (12 U.S.C. § 1818(e)(7)(B)), Coleman is hereby prohibited:

(a) from participating in any manner in the conduct of the affairs of any institution or agency specified in section 8(e)(7)(A) of the FDI Act (12 U.S.C. § 1818(e)(7)(A)), including, but not limited to, any insured depository institution, any insured depository institution holding company or any U.S. branch or agency of a foreign banking organization;

(b) from soliciting, procuring, transferring, attempting to transfer, voting or attempting to vote any proxy, consent or authorization with respect to any voting rights in any institution described in subsection 8(e)(7)(A) of the FDI Act (12 U.S.C. § 1818(e)(7)(A));

(c) from violating any voting agreement previously approved by any Federal banking agency; or

(d) from voting for a director, or from serving or acting as an institution-affiliated party as defined in section 3(u) of the FDI Act (12 U.S.C. § 1813(u)), such as an officer, director, or employee in any institution described in section 8(e)(7)(A) of the FDI Act (12 U.S.C. § 1818(e)(7)(A)).

2. Any violation of this Order shall separately subject Coleman to appropriate civil or criminal penalties or both under section 8 of the FDI Act (12 U.S.C. § 1818).

3. This Order, and each and every provision hereof, is and shall remain fully effective and enforceable until expressly stayed, modified, terminated or suspended in writing by the Board.

This Order shall become effective at the expiration of thirty days after service is made.

By Order of the Board of Governors, this 1st day of March 2005.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM

JENNIFER J. JOHNSON
Secretary of the Board

Membership of the Board of Governors of the Federal Reserve System, 1913–2004

APPOINTED MEMBERS[1]

Name	Federal Reserve District	Date initially took oath of office	Other dates and information relating to membership[2]
Charles S. Hamlin	Boston	Aug. 10, 1914	Reappointed in 1916 and 1926. Served until Feb. 3, 1936.[3]
Paul M. Warburg	New York	Aug. 10, 1914	Term expired Aug. 9, 1918.
Frederic A. Delano	Chicago	Aug. 10, 1914	Resigned July 21, 1918.
W.P.G. Harding	Atlanta	Aug. 10, 1914	Term expired Aug. 9, 1922.
Adolph C. Miller	San Francisco	Aug. 10, 1914	Reappointed in 1924. Reappointed in 1934 from the Richmond District. Served until Feb. 3, 1936.[3]
Albert Strauss	New York	Oct. 26, 1918	Resigned Mar. 15, 1920.
Henry A. Moehlenpah	Chicago	Nov. 10, 1919	Term expired Aug. 9, 1920.
Edmund Platt	New York	June 8, 1920	Reappointed in 1928. Resigned Sept. 14, 1930.
David C. Wills	Cleveland	Sept. 29, 1920	Term expired Mar. 4, 1921.
John R. Mitchell	Minneapolis	May 12, 1921	Resigned May 12, 1923.
Milo D. Campbell	Chicago	Mar. 14, 1923	Died Mar. 22, 1923.
Daniel R. Crissinger	Cleveland	May 1, 1923	Resigned Sept. 15, 1927.
George R. James	St. Louis	May 14, 1923	Reappointed in 1931. Served until Feb. 3, 1936.[4]
Edward H. Cunningham	Chicago	May 14, 1923	Died Nov. 28, 1930.
Roy A. Young	Minneapolis	Oct. 4, 1927	Resigned Aug. 31, 1930.
Eugene Meyer	New York	Sept. 16, 1930	Resigned May 10, 1933.
Wayland W. Magee	Kansas City	May 18, 1931	Term expired Jan. 24, 1933.
Eugene R. Black	Atlanta	May 19, 1933	Resigned Aug. 15, 1934.
M.S. Szymczak	Chicago	June 14, 1933	Reappointed in 1936 and 1948. Resigned May 31, 1961.
J.J. Thomas	Kansas City	June 14, 1933	Served until Feb. 10, 1936.[3]
Marriner S. Eccles	San Francisco	Nov. 15, 1934	Reappointed in 1936, 1940, and 1944. Resigned July 14, 1951.
Joseph A. Broderick	New York	Feb. 3, 1936	Resigned Sept. 30, 1937.
John K. McKee	Cleveland	Feb. 3, 1936	Served until Apr. 4, 1946.[3]
Ronald Ransom	Atlanta	Feb. 3, 1936	Reappointed in 1942. Died Dec. 2, 1947.
Ralph W. Morrison	Dallas	Feb. 10, 1936	Resigned July 9, 1936.
Chester C. Davis	Richmond	June 25, 1936	Reappointed in 1940. Resigned Apr. 15, 1941.
Ernest G. Draper	New York	Mar. 30, 1938	Served until Sept. 1, 1950.[3]
Rudolph M. Evans	Richmond	Mar. 14, 1942	Served until Aug. 13, 1954.[3]
James K. Vardaman, Jr.	St. Louis	Apr. 4, 1946	Resigned Nov. 30, 1958.
Lawrence Clayton	Boston	Feb. 14, 1947	Died Dec. 4, 1949.
Thomas B. McCabe	Philadelphia	Apr. 15, 1948	Resigned Mar. 31, 1951.
Edward L. Norton	Atlanta	Sept. 1, 1950	Resigned Jan. 31, 1952.
Oliver S. Powell	Minneapolis	Sept. 1, 1950	Resigned June 30, 1952.
Wm. McC. Martin, Jr.	New York	April 2, 1951	Reappointed in 1956. Term expired Jan. 31, 1970.
A.L. Mills, Jr.	San Francisco	Feb. 18, 1952	Reappointed in 1958. Resigned Feb. 28, 1965.
J.L. Robertson	Kansas City	Feb. 18, 1952	Reappointed in 1964. Resigned Apr. 30, 1973.
C. Canby Balderston	Philadelphia	Aug. 12, 1954	Served through Feb. 28, 1966.
Paul E. Miller	Minneapolis	Aug. 13, 1954	Died Oct. 21, 1954.
Chas. N. Shepardson	Dallas	Mar. 17, 1955	Retired Apr. 30, 1967.
G.H. King, Jr.	Atlanta	Mar. 25, 1959	Reappointed in 1960. Resigned Sept. 18, 1963.
George W. Mitchell	Chicago	Aug. 31, 1961	Reappointed in 1962. Served until Feb. 13, 1976.[3]
J. Dewey Daane	Richmond	Nov. 29, 1963	Served until Mar. 8, 1974.[3]
Sherman J. Maisel	San Francisco	Apr. 30, 1965	Served through May 31, 1972.
Andrew F. Brimmer	Philadelphia	Mar. 9, 1966	Resigned Aug. 31, 1974.
William W. Sherrill	Dallas	May 1, 1967	Reappointed in 1968. Resigned Nov. 15, 1971.
Arthur F. Burns	New York	Jan. 31, 1970	Term began Feb. 1, 1970. Resigned Mar. 31, 1978.
John E. Sheehan	St. Louis	Jan. 4, 1972	Resigned June 1, 1975.
Jeffrey M. Bucher	San Francisco	June 5, 1972	Resigned Jan. 2, 1976.
Robert C. Holland	Kansas City	June 11, 1973	Resigned May 15, 1976.
Henry C. Wallich	Boston	Mar. 8, 1974	Resigned Dec. 15, 1986.

Name	Federal Reserve District	Date initially took oath of office	Other dates and information relating to membership[2]
Philip E. Coldwell	Dallas	Oct. 29, 1974	Served through Feb. 29, 1980.
Philip C. Jackson, Jr.	Atlanta	July 14, 1975	Resigned Nov. 17, 1978.
J. Charles Partee	Richmond	Jan. 5, 1976	Served until Feb. 7, 1986.[3]
Stephen S. Gardner	Philadelphia	Feb. 13, 1976	Died Nov. 19, 1978.
David M. Lilly	Minneapolis	June 1, 1976	Resigned Feb. 24, 1978.
G. William Miller	San Francisco	Mar. 8, 1978	Resigned Aug. 6, 1979.
Nancy H. Teeters	Chicago	Sept. 18, 1978	Served through June 27, 1984.
Emmett J. Rice	New York	June 20, 1979	Resigned Dec. 31, 1986.
Frederick H. Schultz	Atlanta	July 27, 1979	Served through Feb. 11, 1982.
Paul A. Volcker	Philadelphia	Aug. 6, 1979	Resigned August 11, 1987.
Lyle E. Gramley	Kansas City	May 28, 1980	Resigned Sept. 1, 1985.
Preston Martin	San Francisco	Mar. 31, 1982	Resigned April 30, 1986.
Martha R. Seger	Chicago	July 2, 1984	Resigned March 11, 1991.
Wayne D. Angell	Kansas City	Feb. 7, 1986	Served through Feb. 9, 1994.
Manuel H. Johnson	Richmond	Feb. 7, 1986	Resigned August 3, 1990.
H. Robert Heller	San Francisco	Aug. 19, 1986	Resigned July 31, 1989.
Edward W. Kelley, Jr.	Dallas	May 26, 1987	Reappointed in 1990; resigned Dec. 31, 2001.
Alan Greenspan	New York	Aug. 11, 1987	Reappointed in 1992.
John P. LaWare	Boston	Aug. 15, 1988	Resigned April 30, 1995.
David W. Mullins, Jr.	St. Louis	May 21, 1990	Resigned Feb. 14, 1994.
Lawrence B. Lindsey	Richmond	Nov. 26, 1991	Resigned Feb. 5, 1997.
Susan M. Phillips	Chicago	Dec. 2, 1991	Served through June 30, 1998.
Alan S. Blinder	Philadelphia	June 27, 1994	Term expired Jan. 31, 1996.
Janet L. Yellen	San Francisco	Aug. 12, 1994	Resigned Feb. 17, 1997.
Laurence H. Meyer	St. Louis	June 24, 1996	Term expired Jan. 31, 2002.
Alice M. Rivlin	Philadelphia	June 25, 1996	Resigned July 16, 1999.
Roger W. Ferguson, Jr.	Boston	Nov. 5, 1997	Reappointed in 2001.
Edward M. Gramlich	Richmond	Nov. 5, 1997	
Susan S. Bies	Chicago	Dec. 7, 2001	
Mark W. Olson	Minneapolis	Dec. 7, 2001	
Ben S. Bernanke	Atlanta	Aug. 5, 2002	Reappointed in 2003.
Donald L. Kohn	Kansas City	Aug. 5, 2002	

Chairmen[4]

Charles S. Hamlin	Aug. 10, 1914–Aug. 9, 1916
W.P.G. Harding	Aug. 10, 1916–Aug. 9, 1922
Daniel R. Crissinger	May 1, 1923–Sept. 15, 1927
Roy A. Young	Oct. 4, 1927–Aug. 31, 1930
Eugene Meyer	Sept. 16, 1930–May 10, 1933
Eugene R. Black	May 19, 1933–Aug. 15, 1934
Marriner S. Eccles	Nov. 15, 1934–Jan. 31, 1948[5]
Thomas B. McCabe	Apr. 15, 1948–Mar. 31, 1951
Wm. McC. Martin, Jr.	Apr. 2, 1951–Jan. 31, 1970
Arthur F. Burns	Feb. 1, 1970–Jan. 31, 1978
G. William Miller	Mar. 8, 1978–Aug. 6, 1979
Paul A. Volcker	Aug. 6, 1979–Aug. 11, 1987
Alan Greenspan	Aug. 11, 1987–[6]

Vice Chairmen[4]

Frederic A. Delano	Aug. 10, 1914–Aug. 9, 1916
Paul M. Warburg	Aug. 10, 1916–Aug. 9, 1918
Albert Strauss	Oct. 26, 1918–Mar. 15, 1920
Edmund Platt	July 23, 1920–Sept. 14, 1930
J.J. Thomas	Aug. 21, 1934–Feb. 10, 1936
Ronald Ransom	Aug. 6, 1936–Dec. 2, 1947
C. Canby Balderston	Mar. 11, 1955–Feb. 28, 1966
J.L. Robertson	Mar. 1, 1966–Apr. 30, 1973
George W. Mitchell	May 1, 1973–Feb. 13, 1976
Stephen S. Gardner	Feb. 13, 1976–Nov. 19, 1978
Frederick H. Schultz	July 27, 1979–Feb. 11, 1982
Preston Martin	Mar. 31, 1982–Apr. 30, 1986
Manuel H. Johnson	Aug. 4, 1986–Aug. 3, 1990
David W. Mullins, Jr.	July 24, 1991–Feb. 14, 1994
Alan S. Blinder	June 27, 1994–Jan. 31, 1996
Alice M. Rivlin	June 25, 1996–July 16, 1999
Roger W. Ferguson, Jr.	Oct. 5, 1999–

Notes and list of ex officio members appear on page 302.

EX OFFICIO MEMBERS[1]

Secretaries of the Treasury

W.G. McAdoo .... Dec. 23, 1913–Dec. 15, 1918
Carter Glass .... Dec. 16, 1918–Feb. 1, 1920
David F. Houston .... Feb. 2, 1920–Mar. 3, 1921
Andrew W. Mellon .... Mar. 4, 1921–Feb. 12, 1932
Ogden L. Mills .... Feb. 12, 1932–Mar. 4, 1933
William H. Woodin .... Mar. 4, 1933–Dec. 31, 1933
Henry Morgenthau, Jr. ...... Jan. 1, 1934–Feb. 1, 1936

Comptrollers of the Currency

John Skelton Williams ...... Feb. 2, 1914–Mar. 2, 1921
Daniel R. Crissinger .... Mar. 17, 1921–Apr. 30, 1923
Henry M. Dawes .... May 1, 1923–Dec. 17, 1924
Joseph W. McIntosh .... Dec. 20, 1924–Nov. 20, 1928
J.W. Pole .... Nov. 21, 1928–Sept. 20, 1932
J.F.T. O'Connor .... May 11, 1933–Feb. 1, 1936

1. Under the provisions of the original Federal Reserve Act, the Federal Reserve Board was composed of seven members, including five appointed members, the Secretary of the Treasury, who was ex-officio chairman of the Board, and the Comptroller of the Currency. The original term of office was ten years, and the five original appointed members had terms of two, four, six, eight, and ten years respectively. In 1922 the number of appointed members was increased to six, and in 1933 the term of office was increased to twelve years. The Banking Act of 1935, approved Aug. 23, 1935, changed the name of the Federal Reserve Board to the Board of Governors of the Federal Reserve System and provided that the Board should be composed of seven appointed members; that the Secretary of the Treasury and the Comptroller of the Currency should continue to serve as members until Feb. 1, 1936; that the appointed members in office on the date of that act should continue to serve until Feb. 1, 1936, or until their successors were appointed and had qualified; and that thereafter the terms of members should be fourteen years and that the designation of Chairman and Vice Chairman of the Board should be for a term of four years.

2. Date following *Resigned* and *Retired* denotes final day of service.

3. Successor took office on this date.

4. Chairman and Vice Chairman were designated Governor and Vice Governor before Aug. 23, 1935.

5. Served as Chairman Pro Tempore from February 3, 1948, to April 15, 1948.

6. Served as Chairman Pro Tempore from March 3, 1996, to June 20, 1996.

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April 15, 2005

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April 15, 2005

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ANNUAL PERCENTAGE RATE TABLES (Truth in Lending—Regulation Z) *Vol. I* (Regular Transactions). 1969. 100 pp. *Vol. II* (Irregular Transactions). 1969. 116 pp. Each volume $5.00.

ANNUAL REPORT, 2004.

ANNUAL REPORT: BUDGET REVIEW, 2005.

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Guide to Business Credit for Women, Minorities, and Small Businesses
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- Board of Governors of the Federal Reserve System
- Federal Open Market Committee
- Federal Reserve Bank Board of Directors
- Federal Reserve Banks

There's a Lot to Learn about Money
What You Should Know About Home Equity Lines of Credit (also available in Spanish)
What You Should Know About Your Checks
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STAFF STUDIES: Only Summaries Printed in the BULLETIN

Studies and papers on economic and financial subjects that are of general interest. Staff Studies 1–158, 161, 163, 165, 166, 168, and 169 are out of print, but photocopies of them are available. Staff Studies 165–176 are available online at www.federalreserve.gov/pubs/staffstudies. Requests to obtain single copies of any paper or to be added to the mailing list for the series may be sent to Publications Fulfillment.

159. New Data on the Performance of Nonbank Subsidiaries of Bank Holding Companies, by Nellie Liang and Donald Savage. February 1990. 12 pp.
160. Banking Markets and the Use of Financial Services by Small and Medium-Sized Businesses, by Gregory E. Elliehausen and John D. Wolken. September 1990. 35 pp.
162. Evidence on the Size of Banking Markets from Mortgage Loan Rates in Twenty Cities, by Stephen A. Rhoades. February 1992. 11 pp.
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174. Bank Mergers and Banking Structure in the United States, 1980–98, by Stephen Rhoades. August 2000. 33 pp.
175. Future of Retail Electronic Payments Systems: Industry Interviews and Analysis, Federal Reserve Staff, for the Payments System Development Committee, Federal Reserve System. December 2002. 27 pp.
176. Bank Merger Activity in the United States, 1994–2003, by Steven J. Pilloff. May 2004. 23 pp.

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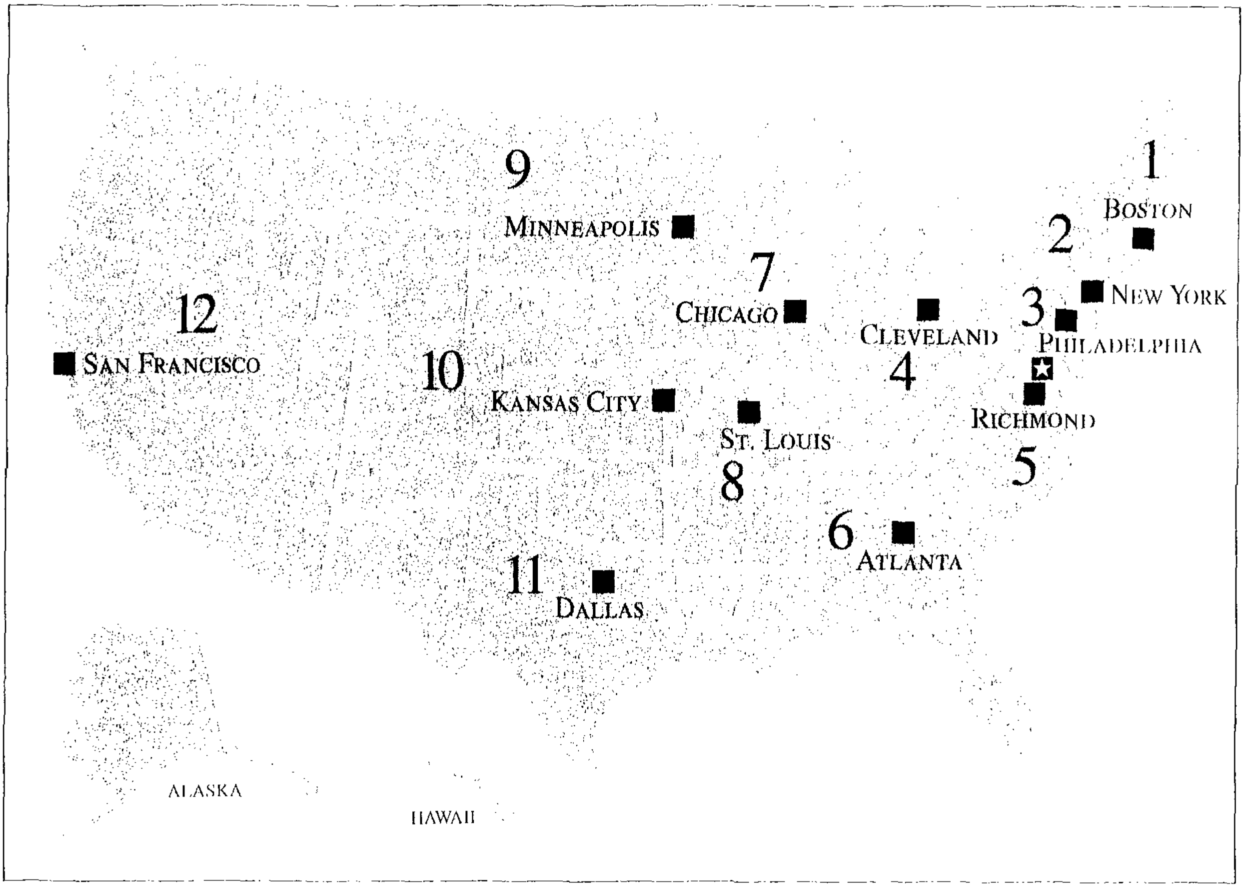
For ordering assistance, write PUBLICATIONS FULFILLMENT, MS-127, Board of Governors of the Federal Reserve System, Washington, DC 20551, or telephone (202) 452-3245, or FAX (202) 728-5886. *You may also use the publications order form available on the Board's World Wide Web site* (www.federalreserve.gov). *When a charge is indicated, payment should accompany request and be made payable to the Board of Governors of the Federal Reserve System or may be ordered via MasterCard, VISA, or American Express. Payment from foreign residents should be drawn on a U.S. bank.*

Release number and title	Annual mail rate	Annual fax rate	Approximate release days[1]	Period or date to which data refer	Corresponding *Bulletin* or *Statistical Supplement* table numbers[2]
Weekly Releases					
H.2. Actions of the Board: Applications and Reports Received	$55.00	n.a.	Friday	Week ending previous Saturday	. . .
H.3. Aggregate Reserves of Depository Institutions and the Monetary Base[3]	$20.00	n.a.	Thursday	Week ending previous Wednesday	1.20
H.4.1. Factors Affecting Reserve Balances of Depository Institutions and Condition Statement of Federal Reserve Banks[3]	$20.00	n.a.	Thursday	Week ending previous Wednesday	1.11, 1.18
H.6. Money Stock Measures[3]	$35.00	n.a.	Thursday	Week ending Monday of previous week	1.21
H.8. Assets and Liabilities of Commercial Banks in the United States[3]	$30.00	n.a.	Friday	Week ending previous Wednesday	1.26A–F
H.10. Foreign Exchange Rates[3]	$20.00	$20.00	Monday	Week ending previous Friday	3.28
H.15. Selected Interest Rates[3]	$20.00	$20.00	Monday	Week ending previous Friday	1.35
Monthly Releases					
G.5. Foreign Exchange Rates[3]	$ 5.00	$ 5.00	First of month	Previous month	3.28
G.17. Industrial Production and Capacity Utilization[3]	$15.00	n.a.	Midmonth	Previous month	2.12, 2.13
G.19. Consumer Credit[3]	$ 5.00	$ 5.00	Fifth working day of month	Second month previous	1.55, 1.56
G.20. Finance Companies[3]	$ 5.00	n.a.	End of month	Second month previous	1.51, 1.52

Release number and title	Annual mail rate	Annual fax rate	Approximate release days[1]	Period or date to which data refer	Corresponding *Bulletin* or *Statistical Supplement* table numbers[2]
Quarterly Releases					
E.2. Survey of Terms of Business Lending[3]	$ 5.00	n.a.	Midmonth of March, June, September, and December	February, May, August, and November	4.23
E.11. Geographical Distribution of Assets and Liabilities of Major Foreign Branches of U.S. Banks	$ 5.00	n.a.	15th of March, June, September, and December	Previous quarter	. . .
E.16. Country Exposure Lending Survey[3]	$ 5.00	n.a.	January, April, July, and October	Previous quarter	. . .
Z.1. Flow of Funds Accounts of the United States: Flows and Outstandings[3]	$25.00	n.a.	Second week of March, June, September, and December	Previous quarter	1.57, 1.58, 1.59, 1.60

1. Please note that for some releases, there is normally a certain variability in the release date because of reporting or processing procedures. Moreover, for all series unusual circumstances may, from time to time, result in a release date being later than anticipated.
2. Beginning with the Winter 2004 issue (vol. 90, no. 1) of the *Bulletin*, the corresponding table for the statistical release no longer appears in the *Bulletin*. Statistical tables are now published in the *Statistical Supplement to the Federal Reserve Bulletin*; the table numbers, however, remain the same.
3. These releases are also available on the Board's web site, www.federalreserve.gov/releases.
n.a. Not available.

Maps of the Federal Reserve System



LEGEND

Both pages

■ Federal Reserve Bank city

⊡ Board of Governors of the Federal Reserve System, Washington, D.C.

Facing page

• Federal Reserve Branch city

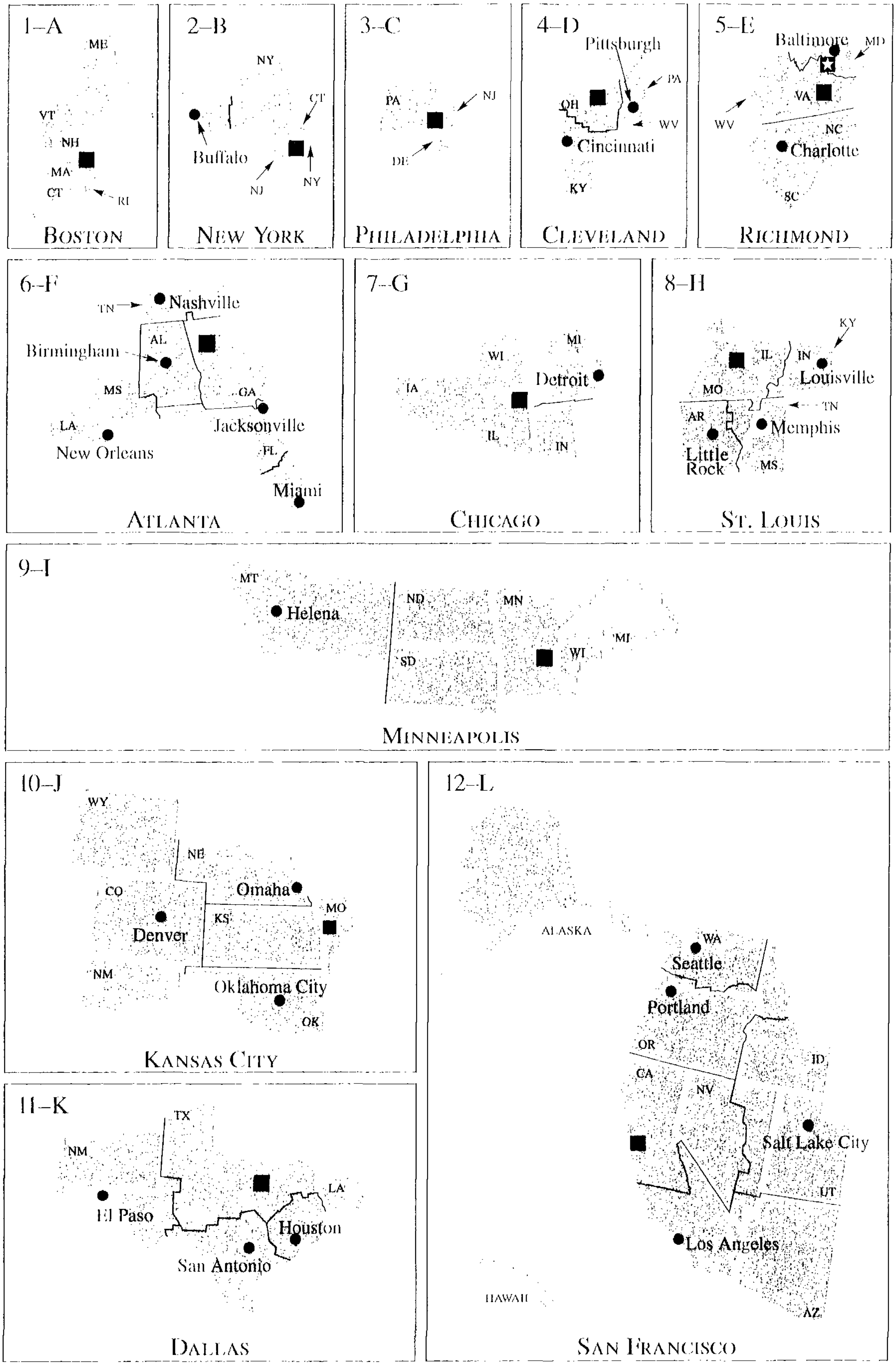
— Branch boundary

NOTE

The Federal Reserve officially identifies Districts by number and Reserve Bank city (shown on both pages) and by letter (shown on the facing page).

In the 12th District, the Seattle Branch serves Alaska, and the San Francisco Bank serves Hawaii.

The System serves commonwealths and territories as follows: the New York Bank serves the Commonwealth of Puerto Rico and the U.S. Virgin Islands; the San Francisco Bank serves American Samoa, Guam, and the Commonwealth of the Northern Mariana Islands. The Board of Governors revised the branch boundaries of the System most recently in February 1996.


1–A
ME
VT
NH
MA
CT
RI
BOSTON
2–B
NY
CT
Buffalo
NJ
NY
NEW YORK
3–C
PA
NJ
DE
PHILADELPHIA
4–D
Pittsburgh
PA
OH
WV
Cincinnati
KY
CLEVELAND
5–E
Baltimore
MD
VA
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NC
Charlotte
SC
RICHMOND
6–F
TN
Nashville
AL
Birmingham
MS
GA
LA
Jacksonville
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Miami
ATLANTA
7–G
MI
WI
IA
Detroit
IL
IN
CHICAGO
8–H
KY
IL
IN
Louisville
MO
TN
AR
Memphis
Little Rock
MS
ST. LOUIS
9–I
MT
Helena
ND
MN
MI
SD
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MINNEAPOLIS
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WY
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CO
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KS
Denver
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OK
KANSAS CITY
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NM
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El Paso
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WA
Seattle
Portland
OR
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CA
NV
Salt Lake City
UT
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HAWAII
AZ
SAN FRANCISCO

Federal Reserve Banks, Branches, and Offices

April 15, 2005

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2. Executive Vice President
3. Acting
4. Senior Branch Executive
5. Assistant Vice President