



fed LETTER

Colorado ★ Kansas ★ Missouri ★ Nebraska ★ New Mexico ★ Oklahoma ★ Wyoming

October 2008

FEDERAL RESERVE BANK of KANSAS CITY

DISTRICT MANUFACTURING DECLINES MODERATELY

Tenth District manufacturing activity declined moderately in September, and firms' expectations about future factory activity dropped noticeably, according to the monthly [Survey of Tenth District Manufacturing](#), which was released Sept. 25.

Most price indexes in the survey fell sharply, following more modest decreases in the previous two months. Still, considerably more firms continued to plan finished goods price increases heading forward than planned price decreases.

The monthly survey asks plant managers about a variety of manufacturing indicators. The information is compiled into a snapshot of manufacturing activity in the Tenth District.

BEIGE BOOK REPORTS IMPROVED GROWTH IN TENTH DISTRICT

Economic growth in the Tenth District improved slightly in late July and early August, according to the [latest Beige Book](#), released Sept. 3. The Beige Book is published eight times per year and includes anecdotal information on current economic conditions in each Federal Reserve District.

In the Tenth District, retail and restaurant sales rose, although auto sales remained weak. Manufacturing activity rebounded after weakening in early summer, and expectations for the next six months were positive. Residential real estate sales experienced a modest improvement, but sales volume and home prices remained well below year-ago levels.

Reports from the 12 Federal Reserve districts indicate that the pace of economic activity has been slow in most districts. Many districts described business conditions as "weak," "soft" or "subdued."

FALL ISSUE OF TEN
EXAMINES EXPORTS' IMPACT
ON FARM BOOM

The fall issue of TEN, "Shipping out," takes a look at whether rising exports can sustain the U.S. farm boom. Global factors such as droughts, tightening food supplies and the weak dollar making U.S. goods more affordable overseas mean prosperity for farmers. But historically, a bust followed times like these.

The fall issue also includes a message from Bank President Tom Hoenig titled "Is Your Bank Account Safe?"

Also in this issue: Read how Greensburg, Kan., bankers are recovering after a devastating tornado; get a glimpse inside the Kansas City Fed's free, interactive Money Museum and find out how you can visit; learn how to get help with your financial institution; find out why there are fewer community banks and what this means for customer relationships; and get an overview of the Kansas City Fed's 2008 Jackson Hole Symposium, which focused on the transformation of financial systems around the world.

PAYMENTS SYSTEM RESEARCH
FOCUSES ON MERCHANT
ACQUIRERS

The latest edition of Payments System Research Briefing looks at the role of merchant acquirers. This article by Terri Bradford and Christian Hung discusses the origin and roles of merchant acquiring; the models for acquiring; and relevant developments in legislation, PCI compliance, and the Single Euro Payments Area.

NEW RESEARCH FEATURED IN
ECONOMIC REVIEW

The third quarter edition of the Bank's *Economic Review* is now available. The publication is a quarterly research publication with articles by Bank staff on topics including macroeconomics and monetary policy, regional and international economics, banking, financial markets and payments systems.

The latest issue contains the following articles:

"Monetary Policy Transparency and Private Sector Forecasts: Evidence from Survey Data," by Gordon Sellon, examines whether private sector forecasts of future monetary policy actions have improved since the Federal Reserve has provided increased information about the monetary policy process.

"Can Smart Cards Reduce Payments Fraud and Identity Theft?" by Rick Sullivan, explores why smart cards have the potential to provide strong payment authorization and thus put a substantial dent into the problems of payments fraud and identity theft.

"The Growth and Volatility of State Tax Revenue Sources in the Tenth District," by Alison Felix, looks at how tax portfolio composition impacts state tax revenue in the Tenth District.

"Is Commercial Real Estate Reliving the 1980s and Early 1990s?" by Alan Garner, explores how current commercial real estate market conditions compare with the conditions leading up to the real estate bust in the late 1980s and early 1990s

HOLIDAY REMINDER

The Federal Reserve Bank of Kansas City will be closed Monday, Oct. 13, for Columbus Day. The FRB Financial Services website features a [complete listing](#) of holidays observed by the Federal Reserve.

REGULATORY DEVELOPMENTS

Interagency examination procedures for the affiliate marketing regulation issued

On Aug. 26, the Board issued [Consumer Affairs \(CA\) 08-6](#), which contains a recently approved Federal Financial Institutions Examination Council examination module for the affiliate marketing regulation. This regulation implements a portion of the Fair and Accurate Credit Transactions Act of 2003 and is incorporated into the Board's Regulation V.

This regulation generally prohibits a financial institution from using certain information received from an affiliate to make a solicitation to a consumer unless the consumer is given notice and a reasonable opportunity to opt out of such solicitations, and the consumer does not opt out. Compliance with this regulation is mandatory as of Oct. 1, 2008.

Interagency examination procedures for Regulation E updated

Also on Aug. 26, the Board issued [CA 08-7](#), which updates existing examination procedures for Regulation E. The updated procedures incorporate all amendments to Regulation E (and the Federal Reserve's Official Staff Commentary) since the prior version was released in 1998. The updates include procedures related to electronic check conversions, payroll cards and electronic terminal receipts. They also include new provisions that address the electronic delivery of consumer disclosures.

Regulation R guidance released

A *Small Entity Compliance Guide for Regulation R* was released on Aug. 29, 2008, by the Federal Reserve Board of Governors. Regulation R, adopted jointly by the Board and the Securities and Exchange Commission in September 2007, implements certain of the key exceptions and exemptions for banks from the definition of the term "broker" under Section 3(a)(4) of the Securities Exchange Act of 1934, as amended by the Gramm-Leach-Bliley Act.

The exceptions and exemptions outlined in the [Small Entity Compliance Guide](#) focus on the types of securities activities more commonly found in community banks, including:

- Referral fees paid to bank employees under third-party networking arrangements with brokers;
- Securities transactions for trust and fiduciary accounts;
- Custody and safekeeping activities for bank or trust customers; and
- Deposit "sweep" activities.

Any bank that wants to rely on one of the exceptions or exemptions to the definition of broker provided by Regulation R should review the rule itself and understand the terms, limits and conditions to the particular exception or exemption.

*Proposed Capital Rules
regarding goodwill deduction from
tier 1 capital issued*

The Board of Governors of the Federal Reserve System is proposing to permit banks and bank holding companies to reduce the amount of goodwill that a banking organization must deduct from tier 1 capital by the amount of any deferred tax liability associated with that goodwill. **The proposed change** would effectively reduce the amount of goodwill that a banking organization must deduct from tier 1 capital and would reflect a banking organization's maximum exposure to loss in the event that such goodwill is impaired or derecognized for financial reporting purposes. Comments must be received on or before Oct. 30, 2008.

Under the existing regulatory capital rules, a banking organization must deduct certain assets from tier 1 capital. A banking organization is permitted to net any associated deferred tax liability against some of those assets prior to deduction from tier 1 capital. Included among those assets are certain intangible assets arising from a nontaxable business combination. Such netting generally is not permitted for goodwill and other intangible assets arising from a taxable business combination. In these cases, the full or gross carrying amount of the asset is deducted. This proposed rule will de-link the goodwill deduction from the tax treatment of the underlying business combination transaction.

FED LETTER • OCTOBER 2008

Fed Letter is published by the Federal Reserve Bank of Kansas City,
1 MEMORIAL DRIVE, Kansas City, Missouri, 64198-0001, (800) 333-1010.

Editor: BILL MEDLEY

Graphic Designer: BETH NORMAN