



BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Financial Statements

December 31, 2003

(With Independent Auditors' Report Thereon)



KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report on Financial Statements

To the Board of Governors of the Federal Reserve System:

We have audited the accompanying balance sheets of the Board of Governors of the Federal Reserve System (the Board) as of December 31, 2003 and 2002, and the related statements of revenues and expenses and changes in cumulative results of operations, and cash flows for the years then ended. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Board at December 31, 2003 and 2002, and the results of its operations, and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our reports dated April 2, 2004, on our consideration of the Board's internal control over financial reporting and its compliance with certain provisions of laws and regulations. Those reports are an integral part of an audit conducted in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

KPMG LLP

April 2, 2004



BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

BALANCE SHEETS

	<u>As of December 31,</u>	
	<u>2003</u>	<u>2002</u>
ASSETS		
CURRENT ASSETS		
Cash	\$ 56,179,654	\$ 8,635,164
Accounts receivable	1,251,117	871,626
Prepaid expenses and other assets	2,614,354	801,031
Total current assets	<u>60,045,125</u>	<u>10,307,821</u>
NONCURRENT ASSETS		
Property and equipment, net (Note 2)	149,595,059	143,971,006
Collections (Note 1)		
Total noncurrent assets	<u>149,595,059</u>	<u>143,971,006</u>
Total assets	<u>\$ 209,640,184</u>	<u>\$ 154,278,827</u>
LIABILITIES AND CUMULATIVE RESULTS OF OPERATIONS		
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$ 15,347,390	\$ 11,450,099
Accrued payroll and related taxes	5,056,647	8,102,710
Accrued annual leave	13,428,993	11,873,527
Capital lease payable (current portion)	206,590	50,546
Unearned revenues and other liabilities	390,698	442,066
Total current liabilities	<u>34,430,318</u>	<u>31,918,948</u>
LONG-TERM LIABILITIES		
Capital lease payable (non-current portion)	763,699	32,153
Accumulated retirement benefit obligation (Note 3)	595,601	614,108
Accumulated postretirement benefit obligation (Note 4)	5,322,053	4,917,787
Accumulated postemployment benefit obligation (Note 5)	4,949,892	4,299,252
Total long-term liabilities	<u>11,631,245</u>	<u>9,863,300</u>
Total liabilities	<u>46,061,563</u>	<u>41,782,248</u>
CUMULATIVE RESULTS OF OPERATIONS		
Working capital	25,821,397	(21,560,581)
Unfunded long-term liabilities	(10,867,546)	(9,831,147)
Net investment in property and equipment	148,624,770	143,888,307
Total cumulative results of operations	<u>163,578,621</u>	<u>112,496,579</u>
Total liabilities and cumulative results of operations	<u>\$ 209,640,184</u>	<u>\$ 154,278,827</u>

See accompanying notes to financial statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

**STATEMENTS OF REVENUES AND EXPENSES
AND CHANGES IN CUMULATIVE RESULTS OF OPERATIONS**

	For the years ended December 31,	
	<u>2003</u>	<u>2002</u>
BOARD OPERATING REVENUES		
Assessments levied on Federal Reserve Banks for Board operating expenses and capital expenditures	\$ 297,020,200	\$ 205,110,800
Other revenues (Note 6)	<u>8,835,440</u>	<u>9,039,417</u>
Total operating revenues	<u>305,855,640</u>	<u>214,150,217</u>
BOARD OPERATING EXPENSES		
Salaries	156,547,392	146,022,212
Retirement and insurance contributions	28,263,776	25,560,734
Contractual services and professional fees	17,501,035	18,073,228
Depreciation and net losses on disposals	12,194,612	12,426,581
Postage and supplies	8,175,120	5,961,699
Utilities	7,664,716	7,218,999
Travel	5,981,254	5,925,674
Software	5,910,128	6,822,066
Repairs and maintenance	4,029,441	4,666,439
Printing and binding	1,864,006	2,026,370
Other expenses (Note 6)	<u>6,642,118</u>	<u>5,141,590</u>
Total operating expenses	<u>254,773,598</u>	<u>239,845,592</u>
RESULTS OF OPERATIONS	<u>51,082,042</u>	<u>(25,695,375)</u>
ISSUANCE AND REDEMPTION OF FEDERAL RESERVE NOTES		
Assessments levied on Federal Reserve Banks for currency costs	508,144,248	429,568,393
Expenses for currency printing, issuance, retirement and shipping	<u>508,144,248</u>	<u>429,568,393</u>
CURRENCY ASSESSMENTS OVER (UNDER) EXPENSES	<u>0</u>	<u>0</u>
TOTAL RESULTS OF OPERATIONS	51,082,042	(25,695,375)
CUMULATIVE RESULTS OF OPERATIONS, Beginning of year	<u>112,496,579</u>	<u>138,191,954</u>
CUMULATIVE RESULTS OF OPERATIONS, End of year	<u>\$ 163,578,621</u>	<u>\$ 112,496,579</u>

See accompanying notes to financial statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

STATEMENTS OF CASH FLOWS

	For the years ended December 31,	
	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES		
RESULTS OF OPERATIONS	\$ 51,082,042	\$ (25,695,375)
Adjustments to reconcile results of operations to net cash provided by (used in) operating activities:		
Depreciation and net losses on disposals	12,194,612	12,426,581
(Increase) decrease in assets:		
Accounts receivable, prepaid expenses and other assets	(2,192,814)	518,815
Increase (decrease) in liabilities:		
Accounts payable and accrued liabilities	3,897,291	(4,675,698)
Accrued payroll and related taxes	(3,046,063)	794,956
Accrued annual leave	1,555,466	1,141,171
Unearned revenues and other liabilities	(51,368)	50,494
Accumulated retirement benefit obligation	(18,507)	(37,520)
Accumulated postretirement benefit obligation	404,266	362,300
Accumulated postemployment benefit obligation	650,640	707,681
Net cash provided by (used in) operating activities	64,475,565	(14,406,595)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from disposals	15,790	5,200
Capital expenditures	(16,809,964)	(17,507,186)
Net cash provided by (used in) investing activities	(16,794,174)	(17,501,986)
CASH FLOWS FROM FINANCING ACTIVITIES		
Capital lease payments	(136,901)	(244,819)
Net cash provided by (used in) financing activities	(136,901)	(244,819)
NET INCREASE (DECREASE) IN CASH	47,544,490	(32,153,400)
CASH BALANCE, Beginning of year	8,635,164	40,788,564
CASH BALANCE, End of year	\$ 56,179,654	\$ 8,635,164
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Capital lease obligations incurred	\$ 1,024,491	\$ 0

See accompanying notes to financial statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

(1) SIGNIFICANT ACCOUNTING POLICIES

Organization - The Federal Reserve System was established by Congress in 1913 and consists of the Board of Governors (Board), the Federal Open Market Committee, the twelve regional Federal Reserve banks, the Federal Advisory Council, and the private commercial banks that are members of the System. The Board, unlike the Reserve Banks, was established as a federal government agency and is supported by Washington staff numbering approximately 1,800, as it carries out its responsibilities in conjunction with other components of the Federal Reserve System.

The Board is required by the Federal Reserve Act to report its operations to the Speaker of the House of Representatives. The Act also requires the Board, each year, to order a financial audit of each Federal Reserve Bank and to publish each week a statement of the financial condition of each such Reserve Bank and a consolidated statement for all of the Reserve Banks. Accordingly, the Board believes that the best financial disclosure consistent with law is achieved by issuing separate financial statements for the Board and for the Reserve Banks. Therefore, the accompanying financial statements include only the operations and activities of the Board. Combined financial statements for the Federal Reserve Banks are included in the Board's annual report to the Speaker of the House of Representatives.

Basis of Accounting - The financial statements have been prepared on the accrual basis of accounting.

Revenues - Assessments for operating expenses and additions to property are based on expected cash needs. Amounts over or under assessed due to differences between actual and expected cash needs flow in to or out of "Cumulative Results of Operations" during the year.

Issuance and Redemption of Federal Reserve Notes - The Board incurs expenses and assesses the Federal Reserve Banks for currency printing, issuance, retirement and shipping of Federal Reserve Notes. These assessments and expenses are separately reported in the statements of revenues and expenses because they are not Board operating transactions.

Property and Equipment - The Board's property, buildings and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, which range from 3 to 10 years for furniture and equipment and from 10 to 50 years for building equipment and structures. Upon the sale or other disposition of a depreciable asset, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is recognized.

Collections - The Board has collections of works of art, historical treasures, and similar assets. These collections are maintained and held for public exhibition in furtherance of public service. Proceeds from any sales of collections are used to acquire other items for collections. As permitted by FAS 116, the cost of collections purchased by the Board is charged to expense in the year purchased and donated collection items are not recorded. The value of the Board's collections has not been determined.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications - Certain 2002 amounts have been reclassified to conform with the 2003 presentation.

(2) PROPERTY AND EQUIPMENT

The following is a summary of the components of the Board's property and equipment, at cost, net of accumulated depreciation.

	As of December 31,	
	2003	2002
Land and improvements	\$ 18,640,314	\$ 18,640,314
Buildings	129,161,957	113,309,775
Furniture and equipment	43,890,215	37,044,828
Software	11,425,411	9,830,112
Construction in process	0	9,467,020
	203,117,897	188,292,049
Less accumulated depreciation	(53,522,838)	(44,321,043)
Property and equipment, net	\$ 149,595,059	\$ 143,971,006

Furniture and equipment includes \$1,156,000 and \$864,000 for capitalized leases as of December 31, 2003 and 2002, respectively. Accumulated depreciation includes \$195,000 and \$654,000 for capitalized leases as of December 31, 2003 and 2002, respectively. The Board paid interest related to these capital leases in the amount of \$76,007 and \$15,731 for 2003 and 2002, respectively.

The Board began the Eccles Building Infrastructure Enhancement Project in July 1999. This \$12.5 million project, scheduled for nineteen phases over three and a half years, included asbestos removal, lighting and plumbing improvements, cabling and other enhancements. This project was completed in 2003.

During 2002, fully depreciated furniture and equipment totalling \$22,350,000 was retired.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

(3) RETIREMENT BENEFITS

Substantially all of the Board's employees participate in the Retirement Plan for Employees of the Federal Reserve System (System Plan). The System Plan is a multi-employer plan which covers employees of the Federal Reserve Banks, the Board, and the Plan Administrative Office.

Employees of the Board who became employed prior to 1984 are covered by a contributory defined benefits program under the System Plan. Employees of the Board who became employed after 1983 are covered by a non-contributory defined benefits program under the System Plan. Contributions to the System Plan are actuarially determined and funded by participating employers at amounts prescribed by the System Plan's administrator. Based on actuarial calculations, it was determined that employer funding contributions were not required for the years 2003 and 2002, and the Board was not assessed a contribution for these years. Excess Plan assets are expected to continue to fund future years' contributions. Because the plan is part of a multi-employer plan, information as to vested and nonvested benefits, as well as plan assets, as it relates solely to the Board, is not readily available.

A relatively small number of Board employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS). The Board matches employee contributions to these plans. These defined benefit plans are administered by the Office of Personnel Management. The Board's contributions to these plans totaled \$312,000 and \$327,000 in 2003 and 2002, respectively. The Board has no liability for future payments to retirees under these programs, and it is not accountable for the assets of the plans.

Employees of the Board may also participate in the Federal Reserve System's Thrift Plan. Under the Thrift Plan, members may contribute up to a fixed percentage of their salary. Board contributions are based upon a fixed percentage of each member's basic contribution and were \$7,692,000 and \$7,185,000 in 2003 and 2002, respectively.

Effective January 1, 1996, Board employees covered under the System Plan are also covered under a Benefits Equalization Plan (BEP). Benefits paid under the BEP are limited to those benefits that cannot be paid from the System Plan due to limitations imposed by Sections 401(a)(17), 415(b) and 415(e) of the Internal Revenue Code of 1986. Pension costs attributed to the BEP reduce the pension costs of the System Plan. Activity for the BEP for 2003 and 2002 is summarized in the following table:

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

	2003	2002
<u>Change in Benefit Obligation</u>		
Projected Benefit Obligation at Beginning of Year	\$ 12,866	\$ 2,125
Service Cost	13,689	3,363
Interest Cost	3,412	561
Plan Participants' Contributions	0	0
Plan Amendments	0	2,852
Actuarial (Gain)/Loss	44,989	3,965
Benefits Paid	0	0
Projected Benefit Obligation at End of Year	\$ 74,956	\$ 12,866
<u>Change in Plan Assets</u>		
Fair Value of Plan Assets at Beginning of Year	\$ 0	\$ 0
Actual Return on Plan Assets	0	0
Employer Contributions	0	0
Plan Participants' Contributions	0	0
Benefits Paid	0	0
Fair Value of Plan Assets at End of Year	\$ 0	\$ 0
<u>Reconciliation of Funded Status at End of Year</u>		
Funded Status	\$ (74,956)	\$ (12,866)
Unrecognized Net Actuarial (Gain)/Loss	(231,189)	(297,773)
Unrecognized Prior Service Cost	(289,456)	(303,469)
Retirement Benefit Liability	\$ (595,601)	\$ (614,108)
<u>Weighted-average assumptions used to determine net periodic benefit cost for years ended December 31</u>		
Discount Rate	6.75%	7.00%
Expected Asset Return	N/A	N/A
Salary Scale	4.25%	4.50%
Corridor	10.00%	10.00%
<u>Components of Net Periodic Benefit Cost</u>		
Service Cost	\$ 13,689	\$ 3,363
Interest Cost	3,412	561
Expected Return on Plan Assets	0	0
Amortization of Prior Service Cost	(14,013)	(14,013)
Recognized Actuarial (Gain)/Loss	(21,595)	(27,431)
Net Periodic Benefit Cost	\$ (18,507)	\$ (37,520)

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

(4) POSTRETIREMENT BENEFITS

The Board provides certain life insurance programs for its active employees and retirees. Activity for 2003 and 2002 is summarized in the following table:

	<u>2003</u>	<u>2002</u>
<u>Change in Benefit Obligation</u>		
Benefit Obligation at Beginning of Year	\$ 6,134,395	\$ 5,868,425
Service Cost	170,636	158,179
Interest Cost	414,319	386,215
Plan Participants' Contributions	0	0
Plan Amendments	0	0
Actuarial (Gain)/Loss	673,998	(63,554)
Benefits Paid	<u>(227,202)</u>	<u>(214,870)</u>
Benefit Obligation at End of Year	<u>\$ 7,166,146</u>	<u>\$ 6,134,395</u>
<u>Change in Plan Assets</u>		
Fair Value of Plan Assets at Beginning of Year	\$ 0	\$ 0
Actual Return on Plan Assets	0	0
Employer Contributions	227,202	213,958
Plan Participants' Contributions	0	0
Benefits Paid	<u>(227,202)</u>	<u>(213,958)</u>
Fair Value of Plan Assets at End of Year	<u>\$ 0</u>	<u>\$ 0</u>
<u>Reconciliation of Funded Status at End of Year</u>		
Funded Status	\$ (7,166,146)	\$ (6,134,395)
Unrecognized Net Actuarial (Gain)/Loss	1,760,246	1,126,688
Unrecognized Prior Service Cost	83,847	89,920
Prepaid/(Accrued) Postretirement Benefit Liability	<u>\$ (5,322,053)</u>	<u>\$ (4,917,787)</u>
<u>Components of Net Periodic Cost for Year</u>		
Service Cost	\$ 170,636	\$ 158,179
Interest Cost	414,319	386,215
Amortization of Prior Service Cost	6,073	6,073
Amortization of (Gains)/Losses	<u>40,440</u>	<u>26,706</u>
Total Net Periodic Cost	<u>\$ 631,468</u>	<u>\$ 577,173</u>

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

The liability and costs for the postretirement benefit plan were determined using discount rates of 6.25 percent and 6.75 percent as of December 31, 2003 and 2002, respectively. Unrecognized losses of \$1,760,246 and \$1,126,888 as of December 31, 2003 and 2002, respectively, result from changes in the discount rate used to measure the liabilities. Under Statement of Financial Accounting Standards No.106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*, the Board may have to record some of these unrecognized losses in operations in future years. The assumed salary trend rate for measuring the increase in postretirement benefits related to life insurance was an average of 4.00 percent.

The above accumulated postretirement benefit obligation is related to the Board sponsored life insurance programs. The Board has no liability for future payments to employees who continue coverage under the federally sponsored life and health programs upon retiring. Contributions for active employees participating in federally sponsored health programs totaled \$7,188,000 and \$6,205,000 in 2003 and 2002, respectively.

(5) POSTEMPLOYMENT BENEFIT PLAN

The Board provides disability and survivor income benefits to eligible employees after employment but before retirement. Effective January 1, 1994, the Board adopted Statement of Financial Accounting Standards No. 112, *Employers' Accounting for Postemployment Benefits*, which requires that employers providing postemployment benefits to their employees accrue the cost of such benefits. Prior to January 1994, postemployment benefit expenses were recognized on a pay-as-you-go basis.

<u>Change in Benefit Obligation</u>	<u>2003</u>	<u>2002</u>
Benefit Obligation at Beginning of Year	\$ 4,299,252	\$ 3,591,571
Service Cost	955,926	891,192
Interest Cost	157,545	166,520
Plan Participants' Contributions	0	0
Plan Amendments	0	0
Actuarial (Gain)/Loss	(156,797)	(76,282)
Benefits Paid	(306,034)	(273,749)
Benefit Obligation at End of Year	<u>\$ 4,949,892</u>	<u>\$ 4,299,252</u>

Weighted-average assumptions as of December 31

Discount Rate	6.25%	6.75%
Expected Asset Return	N/A	N/A
Salary Scale	4.00%	4.25%
Corridor	10.00%	10.00%

**BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002**

(6) OTHER REVENUES AND OTHER EXPENSES

The following are summaries of the components of Other Revenues and Other Expenses.

	As of December 31,	
	2003	2002
Other Revenues		
Data processing revenue	\$ 4,639,084	\$ 4,830,600
Rent	2,029,514	1,996,893
Subscription revenue	799,356	810,032
Reimbursable services to other agencies	588,894	788,095
Board sponsored conferences	275,110	115,965
National Information Center	24,422	30,334
Miscellaneous	479,060	467,498
Total other revenues	<u>\$ 8,835,440</u>	<u>\$ 9,039,417</u>
Other Expenses		
Tuition, registration and membership fees	\$ 1,615,074	\$ 1,642,013
Public transportation subsidy	732,124	745,973
Contingency operations	704,699	264,232
Subsidies and contributions	627,854	900,049
Meals and representation	534,618	378,387
Former employee related payments	507,082	158,066
Security investigations	473,659	229,387
Equipment and facilities rental	439,751	318,132
Administrative law judges	307,173	147,830
Miscellaneous	700,084	357,521
Total other expenses	<u>\$ 6,642,118</u>	<u>\$ 5,141,590</u>

(7) COMMITMENTS

The Board has entered into several operating leases to secure office, training and warehouse space for remaining periods ranging from one to four years. In addition, the Board has entered into an agreement with the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency, through the Federal Financial Institutions Examination Council (the "Council") to fund a portion of enhancements for a central data repository project through 2013.

Minimum annual payments under the operating leases having an initial or remaining noncancelable lease term in excess of one year at December 31, 2003, are as follows:

2004	\$ 157,079
2005	163,363
2006	71,991
After 2006	0
	<u>\$ 392,433</u>

Rental expenses under the operating leases were \$156,000 in 2003 and 2002.

**BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002**

(8) FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

The Board is one of the five member agencies of the Council, and currently performs certain management functions for the Council. The five agencies which are represented on the Council are the Board, Federal Deposit Insurance Corporation, National Credit Union Administration, Office of the Comptroller of the Currency, and Office of Thrift Supervision. The Board's financial statements do not include financial data for the Council. Activity related to the Board and Council for 2003 and 2002 is summarized in the following table:

	<u>2003</u>	<u>2002</u>
Board paid to the Council:		
Assessments for operating expenses of the Council	\$ 105,920	\$ 300,000
Central Data Repository	630,000	0
Uniform Bank Performance Report	201,666	0
Total Board paid to the Council	<u>\$ 937,586</u>	<u>\$ 300,000</u>
Council paid to the Board:		
Data processing related services	\$ 3,485,701	\$ 3,350,412
Administrative services	72,250	69,593
Total Council paid to the Board	<u>\$ 3,557,951</u>	<u>\$ 3,420,005</u>

(9) FEDERAL RESERVE BANKS

The Board performs certain functions for the Reserve Banks in conjunction with its responsibilities for the Federal Reserve System, and the Federal Reserve Banks provide certain administrative functions for the Board. Activity related to the Board and Reserve Banks for 2003 and 2002 is summarized in the following table:

	<u>2003</u>	<u>2002</u>
Board paid to the Reserve Banks:		
Assessments for employee benefits	\$ 2,137,781	\$ 2,014,839
Data processing and communication	1,963,247	2,154,087
Contingency site	704,699	264,232
Total Board paid to the Reserve Banks	<u>\$ 4,805,727</u>	<u>\$ 4,433,158</u>
Reserve Banks paid to the Board:		
Assessments for currency costs	\$ 508,144,248	\$ 429,568,393
Assessments for operating expenses of the Board	297,020,200	205,110,800
Data processing	1,484,015	1,281,759
Total Reserve Banks paid to the Board	<u>\$ 806,648,463</u>	<u>\$ 635,960,952</u>



KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report on Internal Control over Financial Reporting

To the Board of Governors of the Federal Reserve System:

We have audited the balance sheets of the Board of Governors of the Federal Reserve System (the Board) as of December 31, 2003 and 2002, and the related statements of revenues and expenses and changes in cumulative results of operations, and cash flows for the years then ended, and have issued our report thereon dated April 2, 2004. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

In planning and performing our fiscal year 2003 audit, we considered the Board's internal control over financial reporting by obtaining an understanding of the Board's internal control, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. The objective of our audit was not to provide assurance on the Board's internal control over financial reporting. Consequently, we do not provide an opinion thereon.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses under standards issued by the American Institute of Certified Public Accountants. Material weaknesses are conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the internal control and its operation that we consider to be material weaknesses as defined above.

This report is intended solely for the information and use of the members of the Board and its management, the Office of Inspector General, the U.S. Office of Management and Budget, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

April 2, 2004





KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report on Compliance with Laws and Regulations

To the Board of Governors of the Federal Reserve System:

We have audited the balance sheets of the Board of Governors of the Federal Reserve System (the Board) as of December 31, 2003 and 2002, and the related statements of revenues and expenses and changes in cumulative results of operations, and cash flows for the years then ended, and have issued our report thereon dated April 2, 2004. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

The management of the Board is responsible for complying with laws and regulations applicable to the Board. As part of obtaining reasonable assurance about whether the Board's 2003 financial statements are free of material misstatement, we performed tests of the Board's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

The results of our tests of compliance with the laws and regulations described in the preceding paragraph disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the members of the Board and its management, the Office of Inspector General, the U.S. Office of Management and Budget, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

April 2, 2004

