GUIDANCE & SUPERVISION

Financial Accounting Manual for Federal Reserve Banks

May 2025

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

The Federal Reserve System is the central bank of the United States. It performs five key functions to promote the effective operation of the U.S. economy and, more generally, the public interest.

The Federal Reserve

- **conducts the nation's monetary policy** to promote maximum employment and stable prices in the U.S. economy;
- **promotes the stability of the financial system** and seeks to minimize and contain systemic risks through active monitoring and engagement in the U.S. and abroad;
- **promotes the safety and soundness of individual financial institutions** and monitors their impact on the financial system as a whole;
- **fosters payment and settlement system safety and efficiency** through services to the banking industry and U.S. government that facilitate U.S.-dollar transactions and payments; and
- **promotes consumer protection and community development** through consumer-focused supervision and examination, research and analysis of emerging consumer issues and trends, community economic development activities, and administration of consumer laws and regulations.

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About This Manual

This *Financial Accounting Manual for Federal Reserve Banks* (FAM) contains the accounting standards that should be followed by the Federal Reserve Banks.[1]

Accounting principles for entities with the unique powers and responsibilities of the nation's central bank have not been formulated by accounting standard-setting bodies. The Board of Governors has developed specialized accounting principles and practices that it considers to be appropriate for the nature and function of a central bank. These accounting principles and practices are documented in this manual. The Board of Governors has delegated, within certain parameters, the authority to the director of the Division of Reserve Bank Operations and Payment Systems (RBOPS) to set accounting policy for the Reserve Banks and to define, amend, and interpret FAM as prescribed by Board policy. Periodic amendments to FAM are made primarily to codify changes in accounting policy that result from new transactions and other accounting developments. Although setting accounting policy and updating FAM are responsibilities of the RBOPS Financial Accounting Policy and Reporting Section, Reserve Banks' accounting staff also play significant consultative roles in the development of accounting policies included in this manual.

FAM provides guidance to Reserve Banks that should result in uniform accounting policies conforming to the standards established. In some places, FAM provides examples of subsidiary accounts to facilitate an understanding of the scope of the broader balance sheet items. In these cases, unless otherwise noted, the maintenance of such accounts is discretionary with the Reserve Bank.

Although FAM covers the receipt and disbursement of funds and specifies their location on the balance sheet, and is thus the controlling document on capitalization, rates of depreciation, correction of errors in expenses, entries to Profit and Loss, and so on, it does not provide guidance for cost accounting. The Federal Reserve *Cost Accounting for Strategic Planning and Reporting* (CASPR Manual) sets rules for cost accounting.

Federal Reserve Bank staff should consult with the RBOPS Financial Accounting Policy and Reporting Section on financial accounting questions or issues that are not specifically covered in this manual. The section's email group is RBOPS Financial Accounting Policy and Reporting.

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[1] Portions of the *FASB Accounting Standards Codification®* , are copyrighted by the Financial Accounting Foundation, 401 Merritt 7, Norwalk, CT 06856, and are reproduced with permission. In June 2009, the Financial Accounting Standards Board issued ASC Topic 105, *The FASB Accounting Standards Codification,* ("codification"), which has become the single source of U.S. GAAP. References to U.S. GAAP include both the codification as well as the legacy references.

Abbreviations

ACH	Automated clearinghouse
AICPA	American Institute of Certified Public Accountants
AOCI	Accumulated Other Comprehensive Income
ASC	Accounting Standards Codification
AWH	Annual work hours
BEP	Bureau of Engraving and Printing
BIS	Bank for International Settlements
BOG	Board of Governors
BTFP	Bank Term Funding Program
CARES Act	Coronavirus Aid, Relief, and Economic Security Act
CASPR	Cost Accounting for Strategic Planning and Reporting
CBAF	Central Business Administration Function
CCF	Corporate Credit Facility
CFPB	Consumer Financial Protection Bureau
CMBS	Commercial Mortgage Backed Securities
CPFF	Commercial Paper Funding Facility
CP	Currency processors
DCP	Deferred Compensation Plan
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
EASy	Enterprise Accounting System
ESF	Exchange Stabilization Fund
FAM	Financial Accounting Manual for Federal Reserve Banks
Fannie Mae	Federal National Mortgage Association
FASB	Financial Accounting Standards Board
FAST Act	Fixing America's Surface Transportation Act
FDIC	Federal Deposit Insurance Corporation
FICA	Federal Insurance Contributions Act
FOMC	Federal Open Market Committee
FRB	Federal Reserve Bank

FRBA	Federal Reserve Bank of Atlanta
FRBB	Federal Reserve Bank of Boston
FRBNY	Federal Reserve Bank of New York
Freddie Mac	Federal Home Loan Mortgage Corporation
GAAP	Generally accepted accounting principles
Ginnie Mae	Government National Mortgage Association
GSE	Government-sponsored enterprise
IMF	International Monetary Fund
ISA	Interdistrict Settlement Account
LLC	Limited liability company
MAC	Material adverse change
MBS	Mortgage-backed securities
MLF	Municipal Liquidity Facility
MSELF	Main Street Expanded Loan Facility
MSNLF	Main Street New Loan Facility
MSPLF	Main Street Priority Loan Facility
NOELF	Nonprofit Organization Expanded Loan Facility
NONLF	Nonprofit Organization New Loan Facility
OAH	Outside agency help
OEB	Office of Employee Benefits
PPM	Program and Project Management
PPPLF	Paycheck Protection Program Lending Facility
RBOPS	Reserve Bank Operations & Payment Systems
RFARS	RBOPS Financial Accounting Reports System
RMBS	Residential Mortgage Backed Securities
ROB	Retirement and other benefits
RS	Reconciling stations
SDRs	Special drawing rights
SOMA	System Open Market Account
SPE	Special-purpose entity
SPV	Special Purpose Vehicle
TALF	Term Asset-Backed Securities Loan Facility
TBA	To-be-announced
TCOM	Treasury Currency Operations Manual
Thrift BEP	Thrift Benefits Equalization Plan
VIE	Variable interest entity
WTB	Working Trial Balance

Summary of Revisions

Effective January 1, 2025, the revisions of the Financial Accounting Manual for Federal Reserve Banks (FAM) clarify policy guidance around credit losses and update the description of the discount window lending programs.

Summary of Revisions

Chapter 8: Special Topics

The descriptions of the Reserve Bank's lending programs were updated, and the language was better aligned with the accounting standard for credit losses.

- Paragraph 81.02—Recognizing an Allowance for Credit Losses
- Paragraph 81.07—Program Specific Analysis
- Paragraph 81.09—Modifications to Debtors Experiencing Financial Difficulty

1 Balance Sheet

Contents

1.00 General

The balance sheet, form FR 34, shows in detail the assets, liabilities, and capital accounts of the Federal Reserve Banks and certain additional information such as U.S. Government deposits with special depositaries, collateral and custodies held, classifications of "Other deposits—Miscellaneous," and certain memorandum accounts.

The Federal Reserve Act (11(a)(1)) requires the Board to publish a weekly statement of the condition of each Reserve Bank and a consolidated statement for all Reserve Banks, reflecting assets and liabilities, money held as a reserve, and details of investments owned or held by the Reserve Banks. The Board publishes the *Factors Affecting Reserve Balances of Depository Institutions and Condition Statement of Federal Reserve Banks (H.4.1),* weekly pursuant to this requirement.[1] The H.4.1 also furnishes the Board of Governors with basic, original source material for statistical data, much of which is published, relating to the condition of Federal Reserve Banks. Additional periodic Federal Reserve Bank reporting is included in chapter 6.

Each Reserve Bank should set up such general ledger and subsidiary accounts as it requires for its own purposes to prepare the balance sheet and to maintain satisfactory internal controls. This chapter provides general descriptions of the scope of the balance sheet accounts to promote uniformity of accounting treatment. It is not the intent of this manual to redefine basic accounting principles. In those cases where the accounting treatment is unclear, Reserve Banks should contact the RBOPS Financial Accounting Policy and Reporting Section for a FAM interpretation. Transactions of the Reserve Bank must be recorded in the general ledger and reflected on the Balance Sheet; none of the principles or possible lack of specific instructions for any given transaction in this manual should be interpreted as allowing otherwise. Proper accounting practice requires consistent application of accounting principles throughout the District (i.e., head office and Branches) from year to year. If this manual permits Reserve Banks to choose optional treatment for transactions, Reserve Banks should consistently apply the chosen option to all similar transactions. In general, the provisions of this manual address Reserve Bank accounting issues and should be applied from a District perspective (for example, the process for accruals required by paragraph 11.56 should be applied on a Districtwide basis rather than department or Branch basis).

[1] The H.4.1 is available at www.federalreserve.gov/releases/h41/current/h41.pdf.

Balance Sheet

ASSETS

GOLD CERTIFICATE ACCOUNT	110-025	
SPECIAL DRAWING RIGHTS certificate account	120-025	
COIN	130-025	
LOANS AND SECURITIES:		
Loans to depository institutions	140-025	
Loans to others	140-050	
Loans to others—PPPLF	140-055	
Loans to others—BTFP	140-057	
Acceptances		
Bought outright	140-070*	
Securities held under repurchase agreement	140-075	
Federal agency obligations:		
Bought outright	140-100	
Held under repurchase agreement	140-125	
U.S. Govt. securities bought outright:		
Bills	140-150	
Notes	140-175	
Bonds	140-200	
U.S. Govt. sec. held under repurchase agreement	140-225	
Total U.S. Government securities	140-275	
Total loans and securities	140-800	
Principal - floating rate notes	142-125	
FIMA Repo	142-150	
Loan fees deferred	145-040	
Loans payable to FRBNY/FRBB	145-050	
Expansion account	145-075	
Expansion account	145-175	
Other assets—Markets	145-260	
Other assets—SOMA	145-275	
Fed agency MBS	145-300	
Fed agency MBS—fail to deliver	145-315	
Fed agency MBS—temporary investments	145-330	
Allowance for credit losses	145-360	
TALF—loans extended to borrowers	145-400*	
TALF—ABS held by FRBNY at FV	145-415*	
TALF—assets, discounts	145-430*	
TALF—other investments	145-445*	
TALF—assets, face	145-460*	
TALF—FV adjustment to ABS held by LLC	145-515*	
TALF—interest receivable	145-530*	
TALF—FV adjustment of loans	145-575*	
Investment in LLC	145-600*	
Expansion account	145-615	
Loan Participation—MSNLF	145-660**	
Investments—MSNLF	145-662**	
Loan Participation—MSELF	145-675**	
Investments—MSELF	145-677**	
Loan Participation—MSPLF	145-678**	
Investments—MSPLF	145-680**	
Loan Participation—NONLF	145-681**	
Investments—NONLF	145-683**	
Loan Participation—NOELF	145-684**	
Investments—NOELF	145-686**	
Investments at Par—MLF	145-700*	
Investments Discounts & Premiums—MLF	145-701*	
Other investments—MLF	145-702*	
Expansion account	145-715	

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Balance Sheet—*continued*		
Expansion account	145-730	
Expansion account	145-745	
Expansion account	145-760	
Expansion account	145-775	
Expansion account	145-800	
Expansion account	145-815	
ITEMS IN PROCESS OF COLLECTION:		
Transit items—		
Federal Reserve Banks	150-025	
Depository institutions	150-050	
Other items in process	150-100	
Adjustments, net	150-150	
Total items in process of collection	150-900	
BANK PREMISES:		
Land	160-025	
Buildings (including vaults)	160-050	
Construction account	160-100	
Total bank premises	160-110	
Less depreciation	160-125	
Bank premises, net	160-150	
OTHER ASSETS:		
Furniture and equipment	170-025	
Claims account closed banks	170-075	
Foreign currencies	170-100	
(gross $)	170-110*	
Reimbursable exp. and other items receivable	170-125	
Less allowance for doubtful reimbursement	170-130	
Reimbursable expenses, net	170-135	
FDIC assumed indebtedness	170-140	
Interest accrued	170-150	
Premium on securities	170-175	
Overdrafts	170-200	
Deferred charges	170-225	
Prepaid expenses:		
Materials and supplies	170-250	
Pension costs	170-260	
Other	170-275	
Difference account, net	170-300	
Suspense account—general	170-325	
Other real estate, net	170-350	
Currency and coin exhibits	170-375	
Old currency series	170-400	
Miscellaneous cash items	170-425	
Suspense account—pricing	170-450	
Accrued service income	170-475	
Foreign currency liquidity swap arrangements	170-525	
Foreign currency swap arrangements	170-530	
Treasury Credit Protection—Main Street	170-540**	
Expansion account	170-550	
Expansion account	170-560	
Expansion account	170-570	
Expansion account	170-580	
Expansion account	170-590	
Total other assets	170-800	
Interdistrict settlement account	180-025	
TOTAL ASSETS	**190-050**	

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Balance Sheet—*continued*

LIABILITIES

FEDERAL RESERVE NOTES:		
Outstanding (Received from Agent, net)	210-025	
Less—		
Held by Bank and branches	210-050	
In transit	210-075	
Federal Reserve notes, net	210-100	
DEPOSITS:		
Depository institutions	220-025	
Due to Other F.R. Banks—Collected Funds	220-075	
U.S. Treasury—general account	220-100	
Foreign	220-125	
Foreign (gross $)	220-130*	
Other deposits:		
U.S. Treasury—special account	220-140*	
Officers' and certified checks	220-150	
International organizations	220-175	
Secy. of Treasury special account	220-200*	
Govt.-sponsored enterprise accounts	220-225	
Less unclassified charges	220-250	
Net	220-275	
FRB as Fiscal Agent	220-325*	
Joint Accounts	220-330	
Miscellaneous	220-400	
Total other deposits	220-450	
Total deposits	220-500	
DEFERRED CREDIT ITEMS:		
Other Federal Reserve Banks	230-050	
U.S. Treasury—general account	230-075	
Depository institutions	230-100	
Other items in process	230-125	
Adjustments, net	230-150	
Total deferred credit items	230-500	
OTHER LIABILITIES:		
Accrued dividends unpaid	240-025	
Unearned discount	240-050	
Discount on securities	240-075	
Sundry items payable	240-125	
Suspense account—general	240-150	
Exchange translation liability—central bank liquidity swaps	240-190	
Accrued expenses unpaid—estimated	240-200	
Accumulated Benefit Obligation	240-300	
Interest on reserves due to depository institutions	240-430	
Expansion account	240-445	
Treasury equity contribution	240-475	
Expansion account	240-480	
Expansion account	240-485	
Total other liabilities	240-800	
Term Deposit Facility	240-850	
Federal Agency MBS Related Liabilities	240-875	
Designated Financial Market Utilities Deposits	240-900	
Accrued Remittances to Treasury/Deferred Asset	240-925	
Other Liabilities—Markets	240-950	
Central bank liquidity swap accounts	242-100	
Reverse repurchase agreements—foreign official and international accounts	242-120	
Reverse repurchase agreements—primary dealers and expanded counterparties	242-140	
Expansion account	242-160	

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Balance Sheet—*continued*		
Expansion account	242-180	
Expansion account	242-200	
Expansion account	242-220	
Expansion account	242-240	
TOTAL LIABILITIES	**250-025**	
CAPITAL ACCOUNTS		
CAPITAL PAID IN	**310-025**	
SURPLUS	**320-025**	
INCOME, EXPENSES, AND DIVIDENDS:		
Current income	330-025	
Operating expenses (deduct)	330-050	
Other Components of Net Benefit Costs	330-060	
Interest on reserves and term deposits	330-078	
Provision for credit loss expense	330-080	
Expansion account	330-082	
Expansion account	330-085	
Current net income	330-090	
Profit and loss, net	330-100	
Cost of unreimbursed Treasury services	330-110	
Assessment by Board of Governors (deduct)		
Board expenditures	330-125	
Expansion account	330-130	
Assessments by Board of Governors—Bureau of Consumer Financial Protection	330-135	
Assessments by Board of Governors—F.R. currency costs	330-150	
Net income available for distribution	330-160	
Deduct:		
Dividends accrued since January 1	330-175	
Earning Remittances to Treasury	330-200	
Transferred to or from surplus	330-225	
Retained Earnings—Current Year	330-275	
TOTAL CAPITAL ACCOUNTS	**340-025**	
TOTAL LIABILITIES & CAPITAL ACCTS:	**350-025**	
(Monthly)		
Special depositaries, Treasury tax and loan accounts	$	
	Definitive	Book Entry
Collateral for Treasury tax and loan accounts:	$	$
Held in own vaults		
Held by other offices in own district		
Held by other F.R. Banks		
Held by depository institutions		
Collateral for loans:		
Held in own vaults		
Held by other offices in own district		
Held by other F.R. Banks		
Held by depository institutions		
Accountability to Treasury for U.S. Government securities:		
Marketable securities—		
Retired		
Canceled redeemed		
Non-marketable securities—		
On hand		
On consignment with—		
Issuing agents		
Branches		
Savings bonds issued—book entry		

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Balance Sheet—*continued*		
Accountability for other securities:		
U.S. Government agencies—		
*Unissued		
Retired		
Canceled redeemed		
International Organizations—		
*Unissued		
Retired		
Canceled redeemed		
Other custodies held as fiscal agent of the Treasury:		
Gold—		
Held in own vaults		
Held by other F.R. Banks		
Other		
Custodies held for:		
Commodity Credit Corporation		
U.S. Treasury—		
Special gold custody account:		
For display purposes		
Other		
Other Government departments, agencies, and officials—		
Held in own vaults		
Held by other offices in own district		
Held by other F.R. Banks		
Held by depository institutions		
Other offices in own district—		
Unissued U.S. Government securities on consignment—		
On hand		
With issuing agents		
Other		
System Open Market Account		
Other F.R. Banks		
Depository Institutions—		
Securities, etc.—		
Held in own vaults		
Held by other offices in own district		
Held by other F.R. Banks		
Held by depository institutions		
Foreign correspondents—		
Acceptances		
Securities—		
Held in own vaults		
Held by others		
Earmarked gold—Held in own vaults		
Foreign Debt Collateral		
Held in own vaults		
Held by others		
International Bank for Reconstruction & Dev.—securities		
International Finance Corporation—securities		
International Monetary Fund—		
securities		
gold		
International Development Association—securities		
Inter-American Development Bank—securities		
Asian Development Bank—securities		
Miscellaneous custody items		
Collateral and custody items in process		
TOTAL		

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Balance Sheet—*continued*

OTHER DEPOSITS—MISCELLANEOUS

Name of Account	Amount
	$
Memorandum Accounts	
Food coupons pending—	
verification	
destruction	
Noncash collection items:	
Securities and coupons on hand	
U.S. Government and agency coupons:	
Unclassified (or redeemed)	
Suspense or holdover	
Miscellaneous cash items	
International coupons:	
Redeemed	
Suspense or holdover	
Coupons detached from safekeeping holding awaiting shipment to paying agents	
Coupons clipped from unissued Treasury and agency stock	

MATURITY DISTRIBUTION

Maturity distribution of loans:		
15 days or less	615-020	
16–90 days	615-025	
91 days–1 year	615-030	
1–5 years	615-031	
5–10 years	615-032	
Loans over 10 years	615-033	
Total loans	615-035	
Maturity distribution of acceptances:		
15 days or less	615-040*	
16–90 days	615-045*	
Over 90 days	615-050*	
Total Acceptances	615-055*	
Supplemental #1	615-110	
Supplemental #2	615-115	
Supplemental #3	615-120	
Supplemental #4	615-125	
Supplemental #5	615-130	
Supplemental #6	615-135	
Supplemental #7	615-140	
Supplemental #8	615-145	
Supplemental #9	615-150	

* Reported by New York only
** Reported by Boston only

2.10 Gold Certificate Account (110-025)

The Secretary of the Treasury is authorized to issue gold certificates to the Reserve Banks to monetize gold held by the U.S. Department of the Treasury (Treasury). At any time, Treasury may reacquire the gold certificates by demonetizing the gold.

Treasury maintains an account with the Board of Governors entitled "Gold certificate fund—Board of Governors of the FR System." When the Treasury monetizes gold, it credits this account in return for deposit credit at the Federal Reserve Bank of New York (FRBNY). When demonetizing gold, Treasury decreases the account and authorizes the FRBNY to charge its deposit account. The offsetting entry in each case on the

FRBNY's books is made to the Gold Certificate account and the U.S. Treasury—general account. The FRBNY accounting staff sends an advice of these entries to the Board. Also, whenever the official price of gold is changed, Treasury adjusts the account and, simultaneously, the deposit account.

The Board maintains the account in the exact amount as shown on Treasury's books at all times. The entries are made pursuant to advice from the FRBNY and Treasury. The amount of gold certificates on each Bank's balance sheet must agree with the total in the Board's records. Monthly statements of the account are received from Treasury and confirmed by the RBOPS Financial Accounting Policy and Reporting Section.

The Board participates substantially all of the total gold among Reserve Banks based on Federal Reserve notes outstanding (see paragraph 40.70) with an additional amount allocated to the FRBNY as a cushion to accommodate Treasury sales during the year. By law, each Bank may pledge all or any part of its account with the Federal Reserve Agent as security for Federal Reserve notes. Prior to 1978, each Bank pledged a specific amount which was then earmarked in the Board's records on a separate ledger sheet, and thereafter was subject to and reduced only with prior approval from the Assistant Federal Reserve Agent. Beginning in 1978, each Bank's holdings were pledged automatically pursuant to a continuing agreement. The amount of gold certificates pledged with the Agent—currently the same as the balance sheet total at each Bank—is reported on the Daily Statement of the Federal Reserve Agent, Form FR 5 and is also confirmed periodically.

The gold certificate account serves as the medium for affecting an annual settlement among the Reserve Banks for amounts accumulated in the Interdistrict Settlement Account (ISA) (paragraph 5.00). Following the annual settlement, each Bank's gold certificate account is restored relative to the average Federal Reserve notes outstanding through a reallocation of securities in the System Open Market Account. (See paragraph 40.70.)

2.20 Special Drawing Rights Certificate Account (120-025)

Special Drawing Rights (SDRs) are issued by the International Monetary Fund (IMF) to its members in proportion to each member's quota in the IMF at the time of issuance. SDRs serve as a supplement to international monetary reserves and may be transferred from one national monetary authority to another. Under the law providing for U.S. participation in the SDR system, the Secretary of the Treasury is authorized to issue SDR certificates (broadly comparable with gold certificates) to the Federal Reserve Banks. The Banks are required to purchase them for the purpose of financing SDR acquisitions or for financing exchange stabilization operations.

The Treasury, when it wishes to monetize a specific amount of SDRs, authorizes and requests the FRBNY to credit a special account of the Secretary of the Treasury with the total amount of such monetization and to debit the Bank's SDR certificate account by a corresponding amount. The Board participates the SDR certificate transactions among all 12 Federal Reserve Banks in proportion to Federal Reserve notes outstanding in each District at the end of the preceding year. Each of the other Federal Reserve Banks pays for its share of the SDR certificates through its Interdistrict Settlement account. Each of the eleven Banks, therefore, has an increase in one asset (SDR certificates) offset by a decline in another balance sheet asset. The FRBNY has an increase in its deposit liabilities (special account of the Secretary of the Treasury) matched by increases in two assets (SDR certificates—to the extent of its share in overall distribution effected by the Board—and Interdistrict Settlement account). In addition, pursuant to an agreement between the Federal Reserve and Treasury made in the 1960s, whenever the SDR account reaches a level of surplus, Treasury authorizes and requests the demonetization of SDRs. When this occurs, the FRBNY debits the special account of the Secretary of the Treasury with the total amount of such demonetization and credits the Bank's SDR account by a corresponding amount. As in a monetization, the Board participates these balances among all 12 Federal Reserve Banks.

The FRBNY maintains an account for each Reserve Bank entitled "Special Drawing Rights certificate account." Amounts deposited with the FRBNY are distributed on the day of deposit rounded to the nearest million, and payment is made by direct entry to each Bank's Interdistrict Settlement account; i.e., the FRBNY's account is increased and accounts of other Reserve Banks are decreased. Entries in the opposite direction are made when Treasury reduces the total.

Each Bank pledges the full amount in the SDR certificate account as collateral for Federal Reserve notes under a continuing pledge agreement.

2.30 Coin (130-025)

This account represents all United States coin held by the Reserve Banks except gold coin and coin in exhibits.

For shipments of coin between Districts in which the shipment is not received on the same day the coin is shipped, the receiving District should establish a sub-account, defined as an in transit coin account, and follow the same accounting explained in paragraph 50.40 for shipments of notes between Districts.

2.40 Loans (140-025, 140-050, 140-055, and 140-057)

Extensions of credit by Federal Reserve Banks are governed by Regulation A and Operating Circular 10 of each Bank. Loans to depository institutions are carried at face amount in a single account on the balance sheet. The interest is accrued on a daily basis and collected at maturity. Loans to depository institutions are pledged by each Reserve Bank as collateral for Federal Reserve notes. Loans should be evaluated for risk of credit losses on a quarterly basis and the results of the evaluation should be provided to the RBOPS Financial Accounting Policy and Reporting Section. (See paragraph 81.07 for further details.)

Accounts 140-050 and 140-055 are used for recording loans to others, the authority for which is covered in paragraphs 3 and 13 of Section 13 of the Federal Reserve Act. Account 140-050 includes activity from TALF II LLC (TALF II), the Main Street Lending Program facilities, Municipal Liquidity Facility (MLF), and Bank Term Funding Program (BTFP). Specifically, account 140-055 includes amounts extended to borrowers under the Paycheck Protection Program Lending Facility (PPPLF). See Chapter 7 for more details on these facilities.

140-025	Loans to depository institutions
140-050	Loans to others
140-055	Loans to others—PPPLF
140-057	Loans to others—BTFP

2.70 Acceptances: Bought Outright (140-070)

The FRBNY, in carrying out the domestic policy directive adopted by the Federal Open Market Committee (FOMC), may be authorized to hold acceptances. Acceptances arise out of the shipment of goods between countries or within the United States or from the storage of goods within the United States pending marketing. All holdings of acceptances are retained on the FRBNY's balance sheet and are not participated to other Reserve Banks. When acceptances are purchased or sold, the net amount of the transaction is paid to or collected by the FRBNY from the dealer. Only the par value of this transaction is entered to this account. Other accounts that may be affected are interest accrued, premium on securities, discount on securities and, in the case of sales, profit and loss. The FRBNY has not engaged in transactions involving acceptances for several years.

2.75 Securities Held Under Repurchase Agreements (140-075)

The FRBNY is authorized by the FOMC to acquire Treasury, federal agency and government-sponsored enterprise (GSE) debt securities, and federal agency and GSE residential mortgage-backed securities (RMBS) as well as commercial mortgage-backed securities (CMBS) under agreement with a dealer to repurchase the securities at an established point in time (securities purchased under agreements to resell). (See paragraph 40.15.) The amounts recorded to this account represent the contractual amount of the securities held under repurchase agreements, but does not include related amounts, such as accrued interest.

On the day of settlement, the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank at the current domestic allocation rate. (See paragraph 40.70 for the participation methodology.)

2.80 Federal Agency Obligations: Bought Outright and Held Under Repurchase Agreement (140-100 and 140-125)

The FRBNY is authorized by the FOMC to purchase and sell federal agency obligations for the System Open Market Account (SOMA). This account includes federal agency and GSE securities. The securities are bought from or sold to securities dealers and foreign and international accounts maintained at the FRBNY at market prices. By law, the securities must be either direct obligations of an agency of the United States, or fully guaranteed as to principal and interest by such agency.

When these securities are purchased or sold, the net amount of the transaction is paid to or collected by the FRBNY from the dealer and only the par value is entered to this account. Other accounts that may be affected are interest accrued, premium on securities, discount on securities and, in the case of sales, profit and loss. The amortization or accretion of premiums and discounts is discussed in paragraphs 4.00 and 11.52, respectively. The securities are accounted for at amortized cost rather than fair value; therefore, no unrealized gains or losses are recognized.

On the day of settlement the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank at the current domestic allocation rate. (See paragraph 40.70 for the participation methodology.)

2.90 U.S. Treasury Securities Bought Outright: Bills, Notes, and Bonds (140-150, 140-175, and 140-200)

The FRBNY is authorized by the FOMC to purchase and sell U.S. Treasury securities for the SOMA. The securities are bought from or sold to securities dealers and foreign and international accounts maintained at the FRBNY at market prices. By law, the securities must be either direct obligations of the United States, or fully guaranteed as to principal and interest by the United States. Treasury Inflation-Protected Securities are also recorded in this account, the amounts of which are adjusted for inflation compensation.

When securities are purchased or sold, the net amount of the transaction is paid to or collected by the FRBNY from the dealer and only the par value is entered to this account. Other accounts that may be affected are interest accrued, premium on securities, discount on securities and, in the case of sales, profit and loss. The amortization or accretion of premiums and discounts is discussed in paragraphs 4.00 and 11.52, respectively. The securities are accounted for at amortized cost rather than fair value; therefore, no unrealized gains or losses are recognized.

On the day of settlement the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank according to its current domestic allocation rate. (See paragraph 40.70 for the participation methodology.)

2.95 Federal Agency Obligations, U.S. Treasury Securities, and Federal Agency and GSE Mortgage-Backed Securities: Held Under Repurchase Agreement (140-225)

The FRBNY is authorized by the FOMC to acquire Treasury, federal agency, and GSE debt securities, and federal agency and GSE RMBS as well as CMBS under agreement with a dealer to repurchase the securities at an established point in time (securities purchased under agreements to resell). (See paragraph 40.15.)

On the day of settlement, the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank according to its current domestic allocation rate. (See paragraph 40.70 for the participation methodology.) The repurchase agreements generally consist entirely of agreements through third-party custodial arrangements. The amounts recorded to this account represent the contractual amount of the securities held under repurchase agreements, but does not include related amounts, such as accrued interest.

3.00 U.S. Treasury Securities: Floating Rate Notes (142-125)

The FRBNY is authorized by the FOMC to purchase or sell Treasury floating rate notes.

On the day of settlement, the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank according to its current domestic allocation rate. (See paragraph 40.70 for the participation methodology.) The value of these notes are recorded at amortized cost rather than fair value.

3.01 Foreign and International Monetary Authorities Repurchase (142-150)

The Federal Reserve established a temporary repurchase agreement facility for foreign and international monetary authorities (FIMA Repo Facility) to help support the smooth functioning of financial markets, including the U.S. Treasury market, and thus maintain the supply of credit to U.S. households and businesses. Outstanding balances under the FIMA Repo program are recorded in this account.

3.03 Loan Fees Deferred (145-040)

Nonrefundable fees, such as origination or commitment fees, paid to the Bank by borrowers, based on the terms of the agreement, are recorded in this account. As described in Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 310-20, such fees are to be deferred and recognized as income over the life of the loan. The unamortized balance of deferred loan fees should be reported in the Bank's financial statements as an offset to the related loan balance. The periodic amortization of balances in this account should generally be recorded as an addition to interest income, but in some circumstances may be recorded as fees in the profit and loss accounts (330-100). Contact RBOPS Financial Accounting Policy and Reporting Section staff to discuss the proper accounting for deferred loan fees.

3.04 Loans Payable (145-050)

The Federal Reserve Board authorized the FRBNY and the Federal Reserve Bank of Boston (FRBB) to provide financing to their respective limited liability companies, which is booked to account 145-050. The FRBNY extended loans to the Corporate Credit Facilities LLC (closed December 17, 2021), pursuant to the Primary Market Corporate Credit Facility and Secondary Market Corporate Credit Facility. In addition, the FRBNY extended loans to the CPFF II (closed July 8, 2021), the TALF II, and the MLF.

The FRBB extended loans to the MS Facilities LLC pursuant to the Main Street New Loan Facility (MSNLF), the Main Street Priority Loan Facility (MSPLF), the Main Street Expanded Loan Facility (MSELF), the Nonprofit Organization New Loan Facility (NONLF), and the Nonprofit Organization Expanded Loan Facility (NOELF). See Chapter 7 for more details on these facilities.

3.06 Other Assets—Markets (145-260)

The balance in this account represents infrequent, low-value, non-SOMA Markets-related transactions conducted by the FRBNY and is not participated to other Reserve Banks. Dedicated accounts must be established prior to program start dates for transactions related to non-SOMA Markets programs that are expected to be high-value or recurring. This account may be used, however, to record transactions for newly established programs until a dedicated account is established, when the balances should be reclassified to the dedicated account. At the close of business each December 31, this account balance should include only the low-value and infrequent non-SOMA Markets-related transactions.

3.07 Other Assets—SOMA (145-275)

The balance in this account represents infrequent, low-value transactions for newly established low-value, SOMA programs conducted by the FRBNY and is participated to each Reserve Bank. Dedicated accounts must be established prior to program start dates for transactions related to SOMA programs that are expected to be high-value or recurring. This account may be used, however, to record transactions for newly established programs until a dedicated account is established, when these balances should be reclassified to the dedicated account. At the close of business each December 31, this account balance should include only the low-value and infrequent SOMA-related transactions.

3.08 Federal Agency and GSE Mortgage-Backed Securities (145-300, 145-315, and 145-330)

On January 5, 2009, the RMBS purchase program began to purchase RMBS guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae. On March 23, 2020, the CMBS purchase program began to purchase CMBS guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae. The securities are bought from or sold to securities dealers at market prices. By law, the securities must be fully guaranteed as to principal and interest by an agency of the United States. Outright transactions in RMBS and CMBS are recorded on the scheduled settlement date. (See paragraph 40.13.) If a seller fails to provide a security to the FRBNY on the contractual settlement date, a fail liability is recorded.

When securities are purchased or sold, the net amount of the transaction is paid to or collected by the FRBNY from the dealer and only the current face amount of the RMBS and CMBS is entered to this account. Other accounts that may be affected are interest accrued, premium on securities, discount on securities and, in the case of sales, profit and loss. The amortization or accretion of premiums and discounts is discussed in paragraphs 4.00 and 11.52, respectively. The securities are accounted for at amortized cost rather than fair value; therefore, no unrealized gains or losses are recognized.

On the day of settlement the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank according to its current domestic allocation rate. (See paragraph 11.94 and paragraph 40.70 for the participation methodology.) The following accounts are participated to each Reserve Bank:

145-300	Fed Agency MBS (includes GSE RMBS and CMBS)
145-315	Fed Agency MBS—fail to deliver (includes the receivable for GSE RMBS and CMBS fails and related fees for failing to deliver)
145-330	Fed Agency MBS—temporary investments (includes temporary investments resulting from GSE RMBS and CMBS transactions)

3.10 Allowance for Credit Losses (145-360)

Reserve Banks are required to recognize lifetime expected credit losses on a loan measured at amortized cost, regardless of whether the risk of credit loss is determined to be remote.[2] Detailed instructions on how to recognize, measure, and record an allowance for credit loss are provided in paragraph 81.01, Allowance for Credit Losses. The Reserve Banks should use account 145-360 to record allowances for credit losses. Allowances recorded in this account must be approved by the RBOPS Financial Accounting Policy and Reporting Section.

3.13 Investment in LLC (145-600)

In February 2012, the FRBNY acquired a building and transferred title to a newly formed and wholly owned subsidiary, Maiden & Nassau LLC, a limited liability company (LLC) organized under Delaware law. This account is used to record the investment in the LLC and is eliminated upon consolidation of the subsidiary.

3.30 Items in Process of Collection (150-025, 150-050, 150-100, and 150-150)

Consists of items, including but not limited to cash letters, return items, and automated clearinghouse files, deposited with the Federal Reserve for collection and,

[2] Change effective January 1, 2023, per the adoption of FASB ASC Topic 326, Financial Instruments—Credit Losses.

on the balance sheet date, have not yet been presented to the paying bank. The items are segregated on the FR 34 according to the accounts described in the following paragraphs. Sufficient detail or subsidiary accounts should be maintained to identify the general nature of the transactions for float reporting purposes (see paragraph 11.40), including transportation delays and midweek/holiday closings.

Transit Items—Federal Reserve Banks (150-025)

Represents amounts due from other Federal Reserve Banks. The balance reported on the FR 34 represents the total of items forwarded to and still in process of collection with other Districts, including cash letters, and automated clearinghouse (ACH) activity.

Transit Items—Depository Institutions (150-050)

Represents the amount of items including cash letters, return items, etc., which have been dispatched for collection and will be settled with depository institutions located in their own office territory. This account is charged when items are forwarded for payment. This account also includes: ACH credit transactions when the originating depository institution cannot be debited on the transaction date because of a holiday or mid-week closing; and deferred debit entries for depository institutions settled in another Reserve Bank. Cash letters reported not received by the cut-off hour by paying banks because of transportation delays should be reported in this account. Work that has been identified as lost (i.e., has remained in Transit Items for 3 business days) should not be included in this account, but should be transferred to an Adjustments, net account.

Other Items in Process (150-100)

Represents the aggregate amount of items held overnight for processing or dispatch on the following day, exchanges for clearinghouses, and return items held over for look-up. Only items for which credit has been passed or deferred to depositors are included. Also includes the redemption value of future due securities or coupons held pending maturity and for which the Reserve Bank has elected to credit the deferred credit account and credit has been passed or will be passed to customer accounts on a pre-determined availability schedule, securities transfers where a depository institution has been credited but the Reserve Bank is unable to complete the transaction and debit ACH return items that have been held over.

Adjustments, Net (150-150)

The balance in this account represents the net amount (+ or -) of check related adjustments and any other adjustments relating to items that are debited to items in process of collection including differences that are temporarily held in abeyance pending final resolution. The account contains the net of both debit and credit adjustments to items originally recorded in an items in process of collection account such as un-located differences in settlement, unlocated departmental differences, loose items, cash letters determined to be lost (see Transit Items—Depository Institutions (paragraph 150-050), missing bundles reported by drawee banks, items believed to be listed but not enclosed in outgoing cash letters, adjustment requests received from Banks containing insufficient information, errors on clearinghouse statements discovered too late to correct, and cash letter changes discovered too late for adjustments to be made to accounting charges. Also included are check truncation adjustment items where the adjustment arises from a difference occurring between a depository institution and a Reserve Bank. Treasury check truncation adjustment items and other government related adjustment items where the adjustment arises from a difference between a Reserve Bank and Treasury or another government agency, which do not affect float should be held in Suspense Account—General pending resolution. Transactions involving items in process of collection that have been dispatched by the Federal Reserve office for which the office is unable to determine the destination distinction between other Federal Reserve Banks and depository institutions should also be included in this account. Immaterial items below a certain threshold amount are entered to a difference account in Other assets or a current expense account (as described in paragraph 4.40), as are all other differences where it is probable that the difference will not be resolved or where it is decided that it is not feasible to conduct further research.

3.40 Bank Premises—Land (160-025)

The balance in this account represents the original cost of land (less any charge-offs); incidental expenses in connection with the purchase; cost of wrecking old buildings (less salvage); and paving, grading, or landscaping.

3.45 Bank Premises—Buildings (Including Vaults) (160-050)

Includes the total cost of buildings, improvements, and additions that are owned by the Reserve Bank.

3.55 Bank Premises—Construction Account (160-100)

Includes any material construction or renovation. During construction, all costs of a new building, the purchase price of a building to be renovated, and all improvement and renovation costs are reported in this account. When the construction is completed, amounts to be capitalized should be transferred to the appropriate accounts under "Bank Premises." For detailed accounting procedures, see paragraph 30.30.

3.60 Bank Premises and Furniture and Equipment—Depreciation (160-125)

Depreciation is recorded monthly on each building. A more detailed description of capitalization and depreciation of Bank premise assets together with reporting requirements is contained in paragraph 30.40 and 30.70–30.78. Depreciation is recorded monthly on furniture and equipment in accordance with the provisions contained in paragraph 30.47.

3.65 Furniture and Equipment (170-025)

This account contains furniture, furnishings, fixtures, office equipment, automotive equipment, operating equipment such as computers and shredding machines required for specific operations, and machinery and equipment associated with building structures that are considered part of the building and will convey with the building when it is sold. Examples include air conditioning units, boilers, elevators, and heating or lighting equipment. Refer to paragraph 30.46, for a listing of capitalizable furniture and equipment examples.

3.70 Claims Account Closed Banks (170-075)

Direct costs incurred in connection with the collection of paper of failed banks or other obligations, such as court costs of filing suits, collection fees paid attorneys, cost of recording mortgages, premiums paid on fire, and other insurance policies covering property held under mortgage, etc., should be charged to this account. The amount of any overdraft not offset should be included.

3.85 Foreign Currencies (170-100 and 170-110)

Account 170-100 represents each Bank's participated share in investments denominated in foreign currencies and includes premiums, discounts, and accrued interest. The investments and the related accrued interest are reflected as "Foreign currency denominated investments, net" and "Accrued interest receivable" in the financial statements, respectively. The cost basis of foreign government debt instruments are adjusted for amortization of premiums or accretion of discounts. For further discussion, see paragraph 40.30.

Account 170-110 is a unit account included for presentation purposes and is not presented on the FR 34. It is the sum of the foreign currency accounts across all of the Reserve Banks and is used by the FR5 system for calculating collateral for Federal Reserve notes.

3.90 Reimbursable Expenses and Other Items Receivable (170-125)

This account includes expenses that are reimbursable to the Bank and miscellaneous amounts that the Bank has advanced or paid on behalf of others. Individual ledger accounts are maintained as necessary to facilitate control. Each is based on actual or estimated amounts that will be reimbursed in the future.

For the most part, the accounts will represent claims for fiscal agency work performed for Treasury (e.g., public debt operations) and for government departments and agencies. Other accounts consist of receivables due from employees such as loans or dining room charges and amounts due from others such as security deposits with airlines for the use of credit cards, losses incurred in the handling or transportation of currency that are expected to be recovered, amounts due from Treasury for mutilated currency, or tenant rent receivables. Accounts may also be maintained for miscellaneous services rendered others and purchases of goods and services for other Reserve Banks.

Under ordinary circumstances, the amounts that are included in claims for expenses reimbursable or recoverable will represent a calculated part of items such as salaries, retirement contributions, furniture and equipment rentals, etc., that are paid initially by the Bank and included in gross expenses. In some cases, however, expenditures by the Bank are earmarked at the outset for reimbursement or recovery. Such expenditures are not included in the Bank's expenses and are debited directly to one of the receivable ledger accounts herein pending receipt of payment. This account should not be used for disbursements related to items defined as recoveries in paragraph 12.30.

An account covering estimated fiscal agency reimbursable expenses is carried for the purpose of reflecting a more accurate current expense figure. The reimbursable expenses for the month are estimated at the end of the month and debited to this account and credited to the current expenses account. The following month, the estimated receivable is credited and the actual reimbursables are backdated and debited to this account in the applicable month. When funds are received from Treasury, generally quarterly, the balance is closed out.

3.93 Allowance for Doubtful Reimbursement (170-130)

This account is a contra-asset account to the Reimbursable Expenses and Other Items Receivable Account (170-125). At the time entries are made to the reimbursable account, an estimate is made of the amount of the reimbursable that will not be reimbursed. The original offset to this account is a debit to the Capital account—Cost of Unreimbursed Treasury Services (330-110). When actual amounts are determined that will not be reimbursed, the Allowance account should be debited and the Reimbursable account should be credited. This account should also be used to record allowance for the non-Treasury agencies and receivable from others. As a general rule, there will be little to no activity in this account as full costs of providing services will be passed to the Treasury. The account, however, will be maintained for contingency purposes.

3.94 FDIC assumed indebtedness; PPPLF Collateral; Asset Backed Commercial Paper Collateral (170-140)

This account represents depository institution discount window loans that have been subsequently assumed by the Federal Deposit Insurance Corporation (FDIC). Payment and maturity schedules are worked out with the FDIC on a case-by-case basis. In addition, the account is also used to record the assumed PPPLF and Asset Backed Commercial Paper collateral of the LLCs.

3.95 Interest Accrued (170-150)

This account represents interest accrued, but not yet collected, on earning assets. Earnings of nominal amounts may be credited when received except that all earnings, regardless of amount, should be accrued on the last day of the year. Record a debit to this account and a credit to earnings based on the asset type as follows:

- *Interest accrued on securities, liquidity swaps, repurchase agreements, and securities lending fees in the System Open Market Account*—the FRBNY posts these debit entries directly to each Federal Reserve Bank's accounts. Interest accruals are recognized beginning on the day that securities purchases, swap transactions, or repurchase agreements settle and ending the day before securities, swap transactions, or repurchase agreements mature or sales settle. Daily accruals are computed according to the interest calculation terms of the individual securities, swaps, and repurchase agreements. Securities lending fees are accrued based on the terms of the individual securities lending transaction. Interest accrued on foreign denominated investments is discussed at section 3.85.
- *Interest accrued on investments of consolidated LLCs*—Entries are made to the accounts of the LLCs and, as a result of consolidation, are reported by the FRBNY and the FRBB as a component of accrued interest. Interest accruals are booked at least weekly and are computed on individual issues by dividing the amount of interest to be earned by the number of days to the payment date.
- *Interest accrued on loans to depository institutions*—The daily accrual is based on the rate in effect on the previous day divided by 365 days. Accrual on a one-day loan is unnecessary.

Record the above accruals either daily or as of each Wednesday, and on the last day of the month with the following exceptions:

1. If Wednesday is a holiday, entries made for Tuesday shall include accruals for one day's earnings on Tuesday's opening balance and one day's earnings on Tuesday's closing balance, except when January 1 falls on a Wednesday.
2. If the last day of the month is a non-business day, entries made for the last business day shall include accruals for any day or days thereafter during the calendar month on which the Federal Reserve Bank will be closed. For example, should the 29th day of the month fall on a Friday, entries for accrual of earnings on

Friday the 29th would include one day's earnings on the opening balance on that day, and two days' earnings on the closing balance of the 29th, assuming a 31-day month.

3. If the first day of the month is not a business day, entries of accruals on the first business day shall include accruals for the day or days prior thereto within the calendar month on which the Federal Reserve Bank was closed. If entry of accruals is not made daily, the entry made on the first Wednesday of the month should include accruals for any prior day or days within that calendar month.

4.00 Premium on Securities (170-175)

Premium on securities represents the unamortized amount paid in excess of the face value of securities in the SOMA, excluding foreign denominated investments. On the date of purchase, such excess is debited to this account. The cost bases of Treasury securities and GSE debt securities are adjusted for amortization of premiums on an effective interest method. Floating rate notes, however, continue to be adjusted using the straight-line basis. When securities are sold, any applicable premium is credited to the account. The FRBNY posts these entries to each Federal Reserve Bank's account.

4.10 Overdrafts (170-200)

This account is used to record depository institution overnight overdrafts with the Reserve Bank, and is debited by the amount necessary to restore the depository institution's deposit account to a zero balance.

4.20 Deferred Charges and Prepaids (170-225 and 170-275)

Payments made in advance for services to be rendered over future periods should be recorded as prepaid expenses and amortized as appropriate.[3] Prepayments under $25,000 should be charged directly to expense. Among the types of prepayments normally recorded as prepaid expenses are rent, taxes on real estate, and the cost of printing and supplies. Special accounts are provided on the balance sheet for recording the prepayments of services as well as recording general use type items such as materials and supplies. In particular, the $25,000 limitation is designed only to eliminate the need to amortize small amounts over many periods. Items purchased for future use should be recorded as a prepaid expense upon receipt. Also, prepayments for equipment purchases should be recorded as a prepaid expense until the associated equipment is received.

Deferred charges arise through the balance sheet recognition of software and certain lease transactions. Deferred charges $25,000 or greater should be recorded in this account and amortized over the current and prospective periods that benefit from the expenditure. Deferred charges should include items such as finance lease right-of-use assets and operating lease right-of-use assets costs of major improvements to leased space and lease incentives paid to tenants that should be amortized over the life of the contract or lease respectively. (See paragraph 30.85 for further discussion of leasehold improvements.)

The deferred charges account should also be used to record charges for internal use software, including software licenses under cloud computing arrangements (CCAs),

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[3] Payments are defined as meeting the $25k threshold by expense account (inclusive of all products) and term (three months and greater) per purchase order/invoice.

which is defined as software acquired, internally developed, or significantly modified for use by the Reserve Banks in performing their operations. Additionally, the deferred charges account should be used to record implementation costs associated with CCAs that do not contain a software license. Internally developed software and implementation costs associated with CCAs that do not contain a software license should be capitalized if the cost exceeds $100,000. Externally purchased software should be capitalized if the costs exceed $25,000 per license.[4] Desktop utility software and maintenance should be charged to current expense regardless of amount.[5]

Expenditures for bulk purchases of a number of identical software licenses that are individually below the capitalization threshold can be capitalized as a single asset if the total cost is $100,000 or more and the license agreement is for a period longer than a year with notification to the RBOPS Financial Accounting Policy and Reporting Section.

Costs incurred during software development, as well as implementation costs incurred in a cloud computing arrangement, are capitalized or expensed depending on the project stage (preliminary stage, development stage, and post-implementation stage). See "Accounting Guidance for Internal Use Software Costs" at Appendix D.1 for additional information related to the appropriate accounting for these costs.

Costs incurred during the preliminary stage, such as evaluation of alternatives and prototype development, are expensed. Costs incurred in the development stage that are capitalized include

- external costs of materials and services (e.g., consulting fees and salary, retirement, and other benefit costs of employees directly associated with the product);
- costs associated with time spent specifically to oversee developers (programmers), if determinable;
- expenditures related to system integration, which includes consultant fees and salary, retirement, and other benefit costs of employees directly associated with the integration effort; integration costs must be analyzed to determine the allocation between hardware and software;
- implementation costs associated with activities to integrate, configure and/or customize a hosted cloud computing arrangement service;
- travel costs for staff, consultants, or vendors should be capitalized if they are directly related to the software development; and
- capitalizable costs paid to another Reserve Bank for software development efforts.

Costs incurred during the development stage related to general and administrative expense and end-user testing and training should be expensed. Post-implementation stage costs generally should be expensed, except the cost of prepaid maintenance contracts, provided that the costs meet the FAM thresholds for prepaid assets or deferred charges. Other non-capitalizable costs include process re-engineering costs, data conversion costs, and training costs.

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4 From 1992 until 1998, computer software purchased from vendors with an acquisition cost of $50,000 or greater was capitalized in this account and amortized over its estimated useful life, not to exceed three years. From 1999 to 2004, Reserve Banks capitalized the costs for internal use software whether purchased externally or developed internally if the costs exceeded $100,000 in this account. Beginning in 2005, to make the threshold consistent with other prepaid expenses, the capitalization threshold for externally-purchased software, such as license fees, was lowered from $100,000 to $25,000.

5 Examples of desktop utility software include word processing, electronic mail, and anti-virus software.

When internal use software is purchased and the purchase price includes non-capitalizable items (e.g., training), the price must be allocated among capitalizable and non-capitalizable items based on fair value. The costs for website development are accounted for in the same manner as costs of internal use software.

Expenditures made to change existing software assets are considered either improvements or maintenance. Expenditures to existing software assets that meet the capitalization thresholds discussed above should be capitalized if the improvement provides additional capabilities and meets one of the following criteria:

- The quantity of output or operating efficiency of the asset is significantly increased.
- The quality of output is significantly increased.

Improvements should be recorded as separate assets with unique useful lives determined in accordance with the discussion of useful lives below. When the results of efforts to rewrite or improve the software are significant enough to be considered a replacement to the existing software and the expenditures meet the capitalization criteria, the costs should be capitalized. Because the former software asset is significantly altered, the net book value of the former software asset is expensed.

The costs of shared capitalized software projects (i.e., software developed by more than one Reserve Bank) should be transferred to the books of the Reserve Bank that owns the software. The Bank that owns the software should account for the entire software asset, including related amortization and disposal costs. Absent contracts or agreements that delineate ownership, the Reserve Bank that exercises control over the software is the Bank that owns the software.

The estimated useful life over which the costs will be amortized should reflect the circumstances for that specific asset. The maximum useful life that should be assigned to a software asset is generally five years. For perpetual license agreements, the deferred charge should be amortized over a reasonable period generally, not to exceed five years, based on the type and use of the software. In unusual situations, a request to establish a longer useful life must be submitted for RBOPS Financial Accounting Policy and Reporting Section staff approval. At a minimum, each Bank should assess the useful lives of software assets annually.

Capitalized implementation costs for a cloud computing arrangement that does not contain a software license should be amortized over the non-cancellable term of the hosting arrangement and any optional renewal periods reasonably certain to be exercised.

Categorization of some software development or capitalization of implementation costs in cloud computing arrangements may not be as easily determined from the above guidance and may require more analysis with the product or support office, business area, and review by RBOPS Financial Accounting Policy and Reporting Section staff to determine whether the software costs should be capitalized or expensed.

(Note: The accounting treatment for software developed internally for external use [sale] should be determined in consultation with the RBOPS Financial Accounting Policy and Reporting Section.)

This account reflects all prepaid expenses, such as rent and real estate taxes, not specifically covered by paragraph 4.22. The cost of all prepayments of $25,000 or more is debited to this account. (See paragraph 4.20.) Also include prepayments for equipment purchases until the associated equipment is received. Additionally, some items other than materials and supplies should also be debited to this account as they are received with an offsetting credit to Sundry Items Payable (240-125). At the Reserve Bank's option, items that will be consumed within the month may be expensed and not entered to this account. This account may also be used for various control purposes, such as recording travel advances to employees and salary advances prior to the date of regular salary payment. Individual ledger accounts should be maintained as necessary to permit effective control. Advance payments held in this account for purchases pending delivery should not be amortized.

4.22 Prepaid Expenses—Materials and Supplies (170-250)

Payments made in advance for goods and services to be rendered over future periods should be recorded as prepaid expenses. This account is used to record the cost of materials, forms, and supplies, which are carried in the Bank's general stock for release over future periods. Items that are purchased for immediate delivery to the requesting department, such as food for the cafeteria and PCs, should not be included unless the purchases are clearly for the purpose of being carried in the Bank's general stock. Items purchased for direct usage, however, may be posted to this account when such posting and simultaneous withdrawal facilitates inventory control. Freight charges should be reflected in the cost of supplies purchased, whether to be held in stock or direct usage. When impracticable to distribute freight charges over a number of items, the cost may be applied to the largest item(s) of purchase. Freight charges billed separately, and that relate to items already in stock, may be charged to expense. The treatment of freight charges billed separately must be consistent throughout the District (i.e., either all such charges must be charged to expense, or all such charges must continue to be capitalized). The salaries and related expenses that are incurred within the Bank on duplicating and printing forms, etc., or on making parts or other items of supply, may also be debited to the account and deferred to the month of actual usage, provided senior management has approved a policy for capitalizing such costs.

Appropriate records should be maintained to assure that the cost of materials and supplies in stock, along with materials and supplies that have been delivered to operating departments during a month, may be verified against the balance sheet. Separate subsidiary accounts should be maintained to record supplies issued during the month and the appropriate expense entries should be made by month-end. A physical inventory of materials and supplies should be conducted at least annually and any necessary adjusting entries made to expense. Items which become obsolete or which have only limited use over future periods, such as an unused supply of a monthly bulletin issued two months earlier, should be expensed unless the Reserve Bank feels that the demand for the item is likely to recur at a pace that justifies the continued recordkeeping. In the case of supplies that are sold out of inventory, the offsetting entry should be made to cash, items in process of collection, or other designated payment medium.

Purchases for future consumption should be uniformly debited to this account and expensed by the last business day of the month based on the supplies actually used during the month, and the average cost of such supplies should always be used in calculating the expense charge.

4.23 Prepaid Expense—Pension Costs (170-260)

This account is used by the FRBA to record the funded status of the Retirement Plan for Employees of the Federal Reserve System (System Plan) when the fair value of plan assets exceed the projected benefit obligation, as defined by FASB ASC Topic 715-20, and required by FASB ASC Topic 715-20.

The FRBA recognizes the costs and associated net asset or liability of the System Plan on behalf of all the System's employers. Although the System Plan has characteristics of a multi-employer plan in that the plan's assets are not severable among the participating employers, the FRBA accounts for and discloses the System Plan in a manner similar to a single-employer plan given its close administrative relationship with the Office of Employee Benefits and practice of providing funding to the plan on behalf of the System when needed; refer to appendix F.1 for additional information.

4.40 Difference Account, Net (170-300)

Differences are reported in the account to permit settlement between incoming and outgoing work processed in various areas. A difference is an out-of-balance condition resulting from the normal operation of a department where it is probable that the difference will not be resolved or where it is decided that it is not economically feasible to conduct further research. The account thus contains amounts that the Bank has determined to be either uncollectible or else not worth the effort of doing so. While their disposition is considered final, entries to this account are subject to reversal. The account contains both overages and shortages and is shown net on the asset side of FR 34. The balance in this account should be removed and applied to current expense monthly and at year-end regardless of the year in which the differences originated. At the option of any Reserve Bank, unresolved items in the Adjustments, net or Suspense accounts for which research is complete may be written off directly to Current expense, bypassing the Difference account, providing that sufficient control and documentation exist to ensure a clear audit trail absent the Difference account entries. An expensed item that is resolved subsequently should be applied directly to expenses of the current period. General ledger accounts are maintained as necessary to permit effective control. The sources of differences are generally as follows:

- **Currency and Coin**. Tellers verifying incoming deposits are sometimes unable to locate differences in the work. Also, depository institutions will report back any differences that they find in shipments from the Reserve Bank. Any difference identifiable as to depositing institution is applied back to the depositor and is not entered in this account. Differences that result from counterfeits identified during currency processing should be charged to this account.
- **Other.** Internal differences may occur in a variety of Reserve Bank settlement operations such as the balancing of paid savings bonds, cafeteria receipts, and postmaster's deposits. Any difference that will be resolved and reversed should be posted to a suspense account.

4.50 Suspense Account—General (170-325)

This account represents miscellaneous debit items that are temporarily held in abeyance pending disposition. In the case of differences, the suspense account contains amounts whose disposition has yet to be decided and which the Bank has reason to believe are collectable or payable. The suspense account is used to record other items about which there are questions or which for other reasons are being held pending functioning to the appropriate account. Examples are (1) adjustments for savings bond redemptions, (2) expense items that arrive too late in the day to be vouchered or that are being held for additional information, (3) other transactions that require additional information or verification before the charge can be made to the proper account, and (4) checks cashed for employees that have been returned due to non-sufficient funds, etc. The only check-related items to be held in this account are Treasury check truncation adjustment items, and other government related adjustment items, where an un-located difference arises between a Reserve Bank and Treasury, or another government agency, and a depository institution has been credited pending resolution of the difference. Treasury check truncation adjustment items where an un-located difference occurs between a depository institution and a Reserve Bank that is float related should be held in the adjustments, net account under items in process of collection or deferred credit items as appropriate. Items that cannot be resolved should be cleared from this account by a credit and offset by a Difference account debit or may be debited directly to current expense as described in paragraph 4.40.

4.60 Other Real Estate, Net (170-350)

Property purchased for future Bank use is reported in this account pending final approval of the site for construction. Upon final approval of the site, the property is transferred to the Bank premises accounts. The net book value of Bank-owned property that has been classified as held for sale (see asset impairment in paragraph 30.95) should be transferred to this account and carried at net realizable value. (See paragraph 30.97.)

4.70 Currency and Coin Exhibits (170-375)

Represents the cost of currency and coin contained in exhibits or acquired for display purposes. (Exhibits borrowed from other Reserve Banks or from Treasury are reported as a custody item.) The exhibits are acquired pursuant to the following guidelines:

- There is no objection to the maintenance of currency and coin exhibits by the Reserve Banks, or to their retaining individual silver dollars or other pieces of coin and currency for actual use in such exhibits.
- Duplicate pieces of currency and coin that are in excess of exhibit needs should not be held for "trading" purposes, but instead should be returned to Treasury.
- There is no objection to the Reserve Banks' using the currency and coin received in the ordinary course of business to fill out their exhibits, or to their purchasing individual items from dealers or others for this purpose.
- It is inappropriate for the Reserve Banks to bid on miscellaneous collections of currency and coin offered for sale by executors of estates or others, and also inappropriate for them to trade or sell currency and coin to collectors and dealers.
- In those instances where Reserve Banks receive permanent donations of exhibits, this account should reflect an estimate of the fair market value of the exhibit at the time of the donation. The offset should go to the profit and loss account.

4.80 Old Currency Series (170-400)

This account contains old currency issues held pending forwarding to Treasury for redemption as mutilated currency as follows:

- Treasury notes of 1890 Silver certificates, large size
- Federal Reserve notes, large size
- United States notes, large and small size
- National Bank notes, large and small size
- Federal Reserve Bank notes, large and small size
- Gold certificates large and small issued prior to January 30, 1934

4.90 Miscellaneous Cash Items (170-425)

The account consists of petty cash funds, Canadian and foreign currency and coin that are held pending shipment or exchange. The FRBNY also uses this account for transactions related to the Maiden & Nassau LLC building referenced in paragraph 3.13. The OEB also uses this account to hold deposits with the trustee.

4.91 Suspense Account—Pricing (170-450)

This account includes the net of debit and credit items that have been reversed out of a financial institution's account because of error or other questions. The items are held in this account pending resolution. Those that cannot be resolved and charged back to a financial institution should be removed from this account and from the earnings account to which they were originally entered. Except where there are indications of unreasonable or repetitive exceptions to the billings by the Reserve Bank, some questioned items may not be worth the effort of searching. When such items are credited to the financial institution's account, they should be debited to the earnings account.

4.92 Accrued Service Income (170-475)

The purpose of this account is to allow for the recognition of income from services in the month in which it is earned. Accruals may be made daily but should not be less than weekly, on Wednesday or the preceding business day before Wednesday if Wednesday is a holiday, and at the end of the month. The accruals may be on any suitable basis including projections made from the previous month's experience. Accruals within the month are a means for achieving an orderly recognition of earnings. The month-end accrual should be used to adjust the month's earnings to an amount reasonably close to what will actually be realized from the services rendered during the month, unless, of course, the daily or weekly accruals are designed to automatically achieve such results. To avoid duplications in the combined earnings of all Banks, the amounts owed or due from other Reserve Banks should be taken into account in the accrual process.

Prior to April 2018, accrued service income (the estimated receivable) was recognized at the Reserve Bank (New York, Atlanta, and Chicago), which recognizes the service income. From April 2018, accrued service income is recorded at the host Bank for billing (Minneapolis) and the off-set is recognized as service income (revenue) at Boston, New York, Atlanta, and Chicago. Transactions related to the accrued service income (an asset) and recognized service income (revenue) are passed among the Reserve Banks using the Interdistrict Settlement account (paragraph 5.00).

4.94 Central Bank Liquidity Swap Accounts (170-525 and 170-530)

Central bank liquidity swap facilities include U.S. dollar liquidity and foreign currency liquidity swap arrangements between the FRBNY, acting at the direction of the FOMC, and an FOMC authorized foreign central bank. The parties mutually agree to exchange their currencies up to a prearranged maximum amount, for an agreed-upon period of time. These arrangements give the authorized foreign central bank temporary access to U.S. dollars and give the Federal Reserve temporary access to the foreign currencies to deliver to U.S. institutions if conditions warrant. For further discussion, see paragraph 40.50. The recorded amount of central bank liquidity swaps is held in the SOMA and is participated to each Reserve Bank.

U.S. Dollar Liquidity Swaps

When a foreign central bank initiates a swap agreement with the FRBNY for the purpose of obtaining U.S. dollar liquidity, the resulting asset is recorded by the FRBNY in account *foreign currency held under liquidity swap arrangements* (170-525). The foreign central bank compensates the FRBNY, based on the foreign currency amounts it holds. The FRBNY records the compensation received as interest income.

Foreign Currency Liquidity Swaps

When the FRBNY initiates a swap agreement with a foreign central bank for the purpose of obtaining foreign currency liquidity, any resulting asset is recorded in account *foreign currency held under swap arrangements* (170-530). For example, the FRBNY may enter into foreign currency liquidity arrangements whereby the Bank would obtain foreign currency from a foreign central bank; in a second and related transaction, the FRBNY may enter an agreement with a U.S. depository institution under which it would provide an equivalent amount of foreign currency liquidity to that depository institution. In this example, the foreign currency provided to the depository institution would be recorded as an asset in this account; see paragraph 11.99 for recording of the related liability.

4.95 Treasury Credit Protection (170-540)

Per operation of the Facility Lending Programs, the FRBB received a Treasury credit protection and Treasury Investments for the Main Street Lending Program. They are held at the FRBNY. Account 170-540 includes receivable and payable activity from/to the FRBB for the Main Street Lending Program facilities. See Chapter 7 for more details on these facilities.

5.00 Interdistrict Settlement Account (180-025)

The cumulative net amount owed or due from other Federal Reserve Banks as a consequence of the InterFRB transaction settlement procedure is reported in this account. The settlement between Districts is conducted by the centralized accounting system, which captures the data needed to conduct settlement. Once settlement has been effected, the appropriate entries are posted directly to each Reserve Bank's accounts.

Included in this process are the monthly Federal Reserve note clearings and the annual settlement through the gold certificate account of the cumulative interdistrict settlement position. (See paragraph 40.70.)

Priced Service Transactions between Reserve Banks

Principal Reserve Banks reimburse costs incurred for check, automated clearinghouse, funds, securities, FedNow Service, and electronic access services provided by processing (Agent) Reserve Banks. Principal Reserve Banks estimate monthly reimbursements at the end of each month and through the Interdistrict Settlement account record interbank transfers for the services provided by the Agent Reserve Banks by debiting their service costs incurred expense account and crediting the Agent Reserve Banks' services provided expense account. The following month, the estimates are trued up through the same process based on actual monthly costs incurred.

10.01 Federal Reserve Notes Outstanding (210-025)

Represents the net amount of Federal Reserve notes that are outstanding from the Federal Reserve Agent to the Bank. The account consists of the cumulative net issues of the present size currency minus the amount that has been returned for destruction and credit. Currency of the present size (approximately 2.61 inches by 6.14 inches) was issued beginning in July 1929; the outstanding large-size Federal Reserve notes, which were issued from 1914-1929, were removed from Reserve Bank liabilities in 1961 pursuant to the Old Series Currency Adjustment Act and absorbed into the Public Debt.

Eleven denominations of Federal Reserve notes make up the outstanding amount. Seven denominations—$1, $2, $5, $10, $20, $50, and $100—are currently being issued to the Banks. Issuance of larger denominations of $500, $1,000, $5,000, and $10,000 was discontinued in July 1969 and the notes are returned to Treasury for destruction whenever they are received by Reserve Banks from circulation.

Federal Reserve notes are a first and paramount lien on all of the assets of the issuing Reserve Bank. Certain of these assets are also set aside as a specific pledge with the Federal Reserve Agent in order to meet a requirement in Section 16 of the Federal Reserve Act that the notes that are in circulation outside Reserve Banks be fully collateralized. The collateral must consist of legally specified assets, alone or in any combination: (1) gold certificates, (2) U.S. Government and agency obligations, (3) special drawing rights certificates, (4) certain other assets, chiefly loans under Section 13 and foreign currencies acquired under Section 14, and (5) any other asset of a Federal Reserve Bank. The notes are also obligations of the U. S. Government, but the liability of the Government would arise only in the event of the liquidation of the Reserve Banks and then only to the extent that collateral and remaining assets of the Banks were less than the full amount of notes in circulation.

Federal Reserve notes are printed by the Bureau of Engraving and Printing (BEP) as ordered by the Board of Governors. They are held in the vaults of the BEP until the Board directs that they be shipped to (1) a Federal Reserve Agent, the Board's representative at the Reserve Bank, or (2) upon authorization from the Agent, to the Reserve Bank cash department. Notes held by the Agent are not monetized—i.e., they are not reported on the balance sheet. They are kept in separate vaults and their status is no different in this respect than if they were still in BEP vaults. There is no advantage in keeping stocks of agent cash at Reserve Banks and in practice all notes are shipped from BEP facilities in Washington, D.C., or Ft. Worth, Texas, to the cash departments. They are issued to the Reserve Bank on the day of shipment, at which time Federal Reserve Notes Outstanding account is credited and Federal Reserve Notes Held by Bank and Branches account is debited. The reverse occurs when notes are canceled and destroyed, as explained in paragraph 50.50.

10.25 Federal Reserve Notes—Held by Bank and Branches (210-050)

This account consists of all present size currency held by the Bank, including currency held in off-site locations, regardless of the Bank of issue. All present size currency is handled and processed for balance sheet reporting purposes as Federal Reserve notes even though small amounts of silver certificates or United States notes may be present. The latter are determined by formula when credit is being taken for unfit currency that is destroyed, and appropriate adjustment is made to Treasury general account. Also included is canceled currency held pending destruction and currency destroyed in "late shift" work on the balance sheet date.

10.26 Federal Reserve Notes—In Transit (210-075)

This account is used to record issued notes in transit to or from the Bank, such as new notes that have left the BEP facilities in Washington D.C. or Ft. Worth, Texas, but have not been received by the Reserve Bank, or for notes that have been shipped from one Reserve Bank to another (Fed-to-Fed shipment), but have not been received. This account also includes notes held at a depot site.

10.30 Deposits—Depository Institutions (220-025)

Depository institutions' deposits represent balances maintained by depository institutions in accounts at Federal Reserve Banks. Depository institutions may hold balances in master accounts, excess balance accounts, and temporary transitional accounts. Depository institution balances in all of these accounts are captured in this line item. The Reserve Banks pay interest to depository institutions on balances held in these accounts with Reserve Banks. The interest rate paid on balances is determined by the Board of Governors.

10.40 Due to Other FR Banks—Collected Funds (220-075)

Amounts that are owed to another Federal Reserve Bank and which, in ordinary circumstances, would have been settled during the day are reported in this account. One of the most common examples is related to transactions where one Reserve Bank owes funds to another Reserve Bank that is closed and cannot accept InterFRB transactions. A separate subsidiary account should be maintained for these transactions.

10.50 U.S. Treasury—General Account (220-100)

As part of its function as fiscal agent for Treasury, and as provided by Section 15 of the Federal Reserve Act, the FRBNY maintains a deposit account for Treasury. Deposits in this account include funds realized on the sale of government securities or savings bonds, Federal tax receipts, payments for goods or services rendered by the Government, and payments of Reserve Bank earnings. The account is used by Treasury to make interest payments and redemption payments on government obligations and to pay government checks and other items drawn on the account.

10.60 Foreign Deposits (220-125, 220-130)

Account 220-125 includes uninvested cash balances maintained by foreign central banks, foreign governments, and other foreign official entities with Reserve Banks to facilitate the clearing of official U.S. dollar payments and securities transactions. The accounts are generally opened with the FRBNY. A fixed portion of the balances, estimated to represent a floor for these balance levels, is annually participated among the Reserve Banks on the basis of each Bank's capital and surplus ratio.

Account 220-130 is a units account included for presentation purposes and is not presented on the FR 34. It is the sum of the foreign currency accounts across all of the Reserve Banks and is used by the FR5 system for calculating collateral for Federal Reserve notes.

10.70 U.S. Treasury—Special Account (220-140)

This account is used by the FRBNY at the direction of Treasury for certain Treasury deposits that require segregation from both the general account and the account used for exchange stabilization transactions. (See paragraph 11.10.) Balances related to the Treasury Supplementary Financing Program, which was initiated September 17, 2008, were also recorded in this account.

10.80 Officers' and Certified Checks (220-150)

The balance in this account represents the total of all unpaid checks issued by the Federal Reserve Bank, with exception of noncurrent checks which are periodically written off and charged to the Profit and Loss account.

11.01 International Organizations (220-175)

This account consists of balances of international organizations, such as the International Monetary Fund, International Bank for Reconstruction and Development, Inter-American Development Bank, Asian Development Bank, International Development Bank and International Finance Corporation. The law provides that any Reserve Bank which is requested to do so by such organizations should act as its depository or as its fiscal agent, and requires the Board of Governors to supervise and direct the carrying out of these functions. Accounts may be opened under other authority as well.

11.10 Secretary of Treasury Special Account (220-200)

This account is carried on the books of the FRBNY and is used by Treasury for exchange stabilization transactions.

11.20 Government-Sponsored Enterprise Accounts (220-225); Less Unclassified Charges (220-250); Net (220-275)

GSEs, such as the Federal National Mortgage Association, maintain redemption accounts with the FRBNY to cover maturing coupons and securities that are received by Reserve Banks for payment. Balances are maintained by the GSEs to cover the amounts that are due on any given payment date. Payments on definitive obligations by Reserve Banks other than the FRBNY are carried in the miscellaneous cash items account pending charge to the FRBNY. Payments by the FRBNY are entered directly to the unclassified account. When the paid coupons and securities are verified according to the respective GSE, the FRBNY credits the unclassified account and charges the appropriate GSE account.

11.25 FRB as Fiscal Agent (220-325)

This account is used by the FRBNY to accommodate rare situations in which the Federal Reserve, at the direction of the Treasury under Section 15 of the Federal Reserve Act, must hold funds for certain non-Treasury entities in a “non-Treasury” deposit account. These balances are not aggregated with the U.S. Treasury—general account.

11.26 Joint Accounts (220-330)

This account represents the balances maintained by depository institutions in a joint account at a Reserve Bank. A joint account is an account at a Reserve Bank where the rights and liabilities are shared among multiple account-holders—that is, depository institutions that are eligible to open an account with a Reserve Bank. Joint accounts at Federal Reserve Banks are intended to facilitate settlement between depository institutions participating in private-sector payment arrangements.

11.30 Miscellaneous Deposits (220-400)

A wide range of miscellaneous deposit accounts are carried on the books of the Reserve Banks. The deposits arise from depositary responsibilities assigned to the Reserve Banks by law—such as accounts opened by the Federal Deposit Insurance Corporation to cover closed banks and checking accounts opened by government agencies. Deposits also arise from work in process at the Reserve Banks, such as payments received from new depository institutions which have not opened for business, Term Deposit Facility maturities, collateral for payment system risk and credit accounts, and interest paid on securities held pending redemption in federal estate tax cases.

Deposit accounts are also carried for purposes that are specific to only one or a few Reserve Banks. The Board of Governors, for example, maintains a general fund account at the Richmond Reserve Bank to cover general disbursements and another to cover payroll charges. The individual account descriptions should be adequate to identify the different types of accounts maintained under this heading. For example, "Term Deposit Facility maturities" is a sufficient description, rather than Miscellaneous Deposit account 1, etc.

11.40 Deferred Credit Items (230-050, 230-075, 230-100, 230-125, and 230-150)

These accounts are the counterpart of items in process of collection and arise from the fact that Reserve Banks do not give immediate credit for all checks or other items deposited with them for collection or, in some cases, are unable to pass credit on the due date for items that the Reserve Bank has already collected. Where possible, credit is deferred according to a schedule that allows time for the items to be collected. The difference between the asset accounts and these accounts represents the net of checks or other items that, although not yet collected, have already been credited in accordance with a specified time schedule to the accounts of the institutions that deposited them. This difference, called "float," measures on a System basis the net amount of Federal Reserve credit generated by the collection process by providing credit on items deposited with the Federal Reserve for collection prior to actual collection. Sufficient detail or subsidiary accounts should be maintained, as in items in process of collection (see paragraph 3.30), to identify the general nature of the transactions for float reporting purposes (e.g., cash letters, ACH, noncash).

The amounts are carried in the following accounts:

Other Federal Reserve Banks (230-050)

Represents cash letters or other items which are received from other Districts or their depository institutions for which the other District will process the credit to the depository institution based on notification from the depository institution. Those items received directly from depository institutions in other Districts for which the other District would have no notice should be recorded in the Depository Institutions account below.

U.S. Treasury—General Account (230-075)

Consists of items received for deposit to Treasury's account on which credit is deferred, such as items in payment for federal taxes, marketable securities, savings bonds, and checks deposited by various federal agencies to Treasury's account.

Depository Institutions (230-100)

Represents cash letters and other items received from institutions and ACH items which cannot be credited because the depository institution is closed. Deferred credit entries for depository institutions located and/or settled in another Reserve office using InterFRB transactions should be included in this account.

Other Items in Process (230-125)

Represents credit items held over by the Federal Reserve Bank. This account includes, but is not limited to, electronic transfers where one depository institution has been charged but the Federal Reserve Bank cannot complete the transaction by passing credit to a depository institution, credit ACH return items which have been held over, and any prefunded credit ACH items.

Adjustments, Net (230-150)

Includes the net amount of adjustments (+ or -) that are made to items originally credited to any deferred credit items account prior to the date that the original entries are removed and credited on an immediate basis. Adjustments to deferred Treasury items should be reflected in the Deferred Credit Items: Treasury General Account (see 230-075).

11.50 Accrued Dividends Unpaid (240-025)

This account represents the liability for dividends accrued to date on Reserve Bank capital paid-in from member banks that have not been paid.

As required by the Federal Reserve Act, a bank becoming a member of the System must subscribe to stock in the Federal Reserve Bank in whose territory it is located. All stock issued to banks within a District is issued by and reflected upon the books of the Reserve Bank. After all necessary expenses of a Federal Reserve Bank have been paid or provided for, the stockholders of the Bank shall be entitled to receive an annual dividend on paid-in capital stock.

Semiannual dividends on the paid-in stock are paid by the issuing Reserve Bank on the last business day of June and December. These dividends are accrued daily (based on a 30-day month and 360-day year) and accumulate in this account from one payment date until the next. The total amount of the daily accrual is debited to Dividends Accrued (330-175), representing a deduction from current net earnings, and credited to Accrued Dividends Unpaid as the liability for dividends due but unpaid.

Effective January 1, 2016, Section 7(a) of the Federal Reserve Act was amended by the *Fixing America's Surface Transportation Act* (FAST Act), which revised the per annum dividend rate for member banks with consolidated total assets of more than $10 billion (large member banks) to the lesser of the rate equal to the high yield of the 10-year Treasury note auctioned at the last auction held prior to the payment of such dividend, and 6 percent.[6] The per annum dividend rate for member banks with $10 billion or less of total consolidated assets (small member banks) remains at 6 percent.

The accrual of dividends is based on the following rates:

- For large member banks, the per annum dividend rate paid to large member banks at the last semiannual dividend payment date.
- For small member banks, a per annum dividend rate of 6 percent.

The amount to be accrued daily should be obtained by multiplying the applicable per annum dividend rate by the Reserve Bank's paid-in capital stock from member banks, and dividing the result by 360 days (representing the standard number of days in each annual period). Dividend accruals are computed on the total of such capital paid-in as of the opening of business that day (close of business previous day). No accrual should be made on the last day of months with 31 days, and extra accruals will be required on the last day of February. Accruals for a non-business day should be made on the succeeding business day except when a non-business day is a month-end or a Wednesday. In these cases, the accruals should be included in the previous business

[6] The Federal Reserve Act, as amended by the FAST Act, requires that the threshold amount of member bank total consolidated assets be adjusted annually to reflect the change in the Gross Domestic Product Price Index, published by the Bureau of Economic Analysis.

day provided the non-business day(s) are of the same month. When the non-business days are in different months, the accrual for the non-business days should be split appropriately between the previous and subsequent days. In lieu of accruing dividends daily, accruals may be made as of each Wednesday and the last business day of the month (excluding the 31st day of any month).

Because the dividend rate paid to large member banks at the semiannual dividend payment date will differ from the rate used for daily accruals, an adjustment to the accrual account will be required, equal to the difference between dividends accrued and the amount actually paid.

Banks become members of and withdraw from the System at various times during an accrual period and others may subscribe to additional capital or reduce their holdings of capital between semiannual dividend payment dates. Regulation I, *Issue and Cancellation of Federal Reserve Bank Capital Stock,* describes the calculation for dividend payments when a member bank increases or decreases its capital paid-in.[7] The accounting for dividend accruals resulting from changes in capital paid-in that occur between semiannual dividend payment dates are described as follows:

- **Banks becoming members and increases in stock subscriptions**—In these instances the stock is issued, and the member bank's account at the Reserve Bank (or its correspondent's account at the Reserve Bank) is charged for the amount of the accrued stock dividends from the last dividend payment date through the issuance date. Small member banks continue to accrue stock dividends on a per annum rate of 6 percent. The amount charged for accrued stock dividends for large member banks, as defined in section 7(a) of the Federal Reserve Act, shall be based on the dividend rate paid to large member banks at the last semiannual dividend payment date. The corresponding credit is recorded to the accrued Dividends Unpaid account. At the end of the period, the member bank is paid dividends based on the holding period of the stock. Because the rates used to compute accrued dividends on interim transactions and the amount of the dividend to be paid on the semiannual dividend date will generally differ, the accrued dividend account requires adjustment at the semiannual dividend payment date.
- **Banks withdrawing from membership and decreases in stock subscriptions**—A bank withdrawing from membership is paid accrued dividends upon actual cancellation of stock or at the effective date of stock cancellation (as explained in Regulation I) rather than at the regular dividend payment date. When a small member bank withdraws from membership or decreases its stock subscription, the Reserve Bank must pay accrued dividends at a per annum rate of 6 percent. When a large member bank withdraws from membership or decreases its stock subscription, the Reserve Bank must pay accrued dividends at a per annum rate equal to the high yield of most recent 10-year Treasury note auctioned at the last auction held prior to the payment of such dividend. On the day dividends are credited to the member bank's account at the Reserve Bank (or its correspondent's account at the Reserve Bank), a corresponding summary debit is made to Accrued Dividends Unpaid that will eliminate the previously accrued account balance. Because the dividend rate paid to large member banks at the effective date of the withdrawal or decrease in stock subscriptions will differ from the rate used for daily accruals, an adjustment to the accrual account (240-025) and dividend account (330-175) will be required, equal to the difference between dividends accrued and the amount actually paid.

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[7] The Board of Governors amended Regulation I, effective February 24, 2016, to implement the FAST Act provisions related to the payment of dividends to Reserve Banks.

11.51 Unearned Discount (240-050)

This account includes unearned discount on acceptances and, although rare, the discount on any loans under paragraph 3 of Section 13 of the Federal Reserve Act.

11.52 Discount on Securities (240-075)

Discount on securities represents the amount paid under the face value for securities in the System Open Market Account, excluding foreign denominated investments. The face value is recorded in the asset account for securities. On the date of purchase, the amount of the discount is credited to this account. The cost bases of Treasury securities and GSE debt securities are adjusted for accretion of discounts on an effective interest method. The cost basis of floating rate notes are adjusted for accretion on discounts using the straight-line basis. When securities are sold, any remaining unaccreted discount is debited to this account. The FRBNY posts these entries to each Federal Reserve Bank's account.

11.53 Discounts and Rebates

In the course of procuring goods or services, vendors may offer discounts or rebates of varying amounts to the Reserve Banks based on volume of purchases, timing of payments, etc. Where practical, discounts and rebates associated with a particular capital acquisition or expense, should reduce the acquisition cost recognized by the amount; otherwise, discounts and rebates are recognized as a reduction to current expense as a recovery when they are received.

11.55 Sundry Items Payable (240-125)

This account covers numerous items to be disbursed at a later date, such as amounts deducted from salaries for federal and state income taxes, United Way Fund, insurance, etc. The account also includes specific items that are due but have not yet been paid, staff salaries accrued at month-end, taxes on real estate, transportation charges, equipment purchases, lease payment obligations under lessee finance and operating leases, tenant security deposits and rent payments, active employee medical liabilities, and interest payable accrued for reverse repurchase agreements. Amounts charged to this account for equipment purchases or services must be for items received or services rendered and for which the Reserve Bank has a firm obligation outstanding. (See paragraph 11.56.) Obligations under lessee finance and operating leases are recorded at the commencement of the lease. Separate subsidiary accounts should be established to record obligations under lessee finance and operating leases. The account is also used to record the liabilities of the LLCs, consolidated by the FRBNY and the FRBB.

11.56 Accruals of Expenses

Under accrual accounting, the financial effects of transactions and other economic events are recorded in the periods in which they have their primary economic effect. Accordingly, accrual accounting recognizes revenues and expenses as they are earned or incurred, not as cash is received or paid.

Accruals should be made weekly at a minimum unless otherwise specified. Prior to the end of the reporting period, Reserve Banks should ensure that all accruals are properly reflected in the underlying accounts. Accruals for standard timing lags may be made by using a standard accrual made in the beginning of the year, and then reversed at year-end ("standing accrual").

Accrual of Expenses within the Month—Accrued Expenses Unpaid—Estimated (240-200)

Expenses should be accrued weekly for H.4.1. statutory reporting purposes. On each Wednesday, if accruals are made weekly, or on each day, the difference between total estimated net operating expenses and total net operating expenses recorded for the week or day should be debited (or credited) to the Expenses accrued—estimated subaccount included in an operating expense account (330-050) and credited (or debited) to accrued expenses unpaid—estimated (240-200) included in other liabilities. After these entries are made, the balances in these two accounts will represent the difference between estimated net operating expenses for the month-to-date and total net operating expenses for the month-to-date as recorded.

On the Form FR 34, the **debit** balance in the "Expenses accrued-estimated" account should be included in the "Operating expenses" account (330-050) and the **credit** balance in the "Accrued expenses unpaid—estimated" account (240-200) should be reported under the caption "Other liabilities." If month-to-date net operating expenses recorded exceeds total estimated net operating expenses, resulting in a **credit** balance in "Expenses accrued-estimated" and a **debit** balance in "Accrued expenses unpaid-estimated," these two accounts should be adjusted to zero. On the last day of the month, these accounts should be closed against each other.

Accrual of Expense/Expenditure at Month-End and Year-End

Expenses incurred should be accrued as of the last day of the month and the year. To ensure the proper recognition of expenses and liabilities at month-end and year-end, Reserve Banks are expected to maintain robust accrual processes to identify expenses timely and record them in the proper period. These processes may differ depending on the nature of the transaction as long as they effectively accrue significant expenses. For example, some transactions may be more efficiently accrued on a comprehensive basis than on a transaction basis. Examples of these may include automated accruals associated with purchase orders, purchasing cards, and personnel-related expenses. Other transactions, such as recurring monthly payments for utilities, may be more efficiently recorded on a cash basis if the monthly differences are minor and they are handled consistently month-to-month.

Although some transactions, particularly those acquisitions of goods and services outside the purchase order/purchasing card processes, may be difficult to identify, Reserve Banks must maintain an accrual process to consistently identify and accrue significant transactions in the appropriate period. Because of the importance of producing accurate year-end financial statements, additional procedures, such as subsequent payments testing, should be used to identify and accrue expenses incurred but not paid at year-end.

Amounts accrued should be debited to operating expenses and distributed to the appropriate subsidiary accounts or to the appropriate asset account, and credited to sundry items payable or prepaid accounts. (See paragraph 4.20.) For monthly accruals made for purchasing card transactions, the Bank may choose to offset the accrual for expenses to the current expense undistributed account rather than individual expense accounts. If the Bank makes significant capital purchases with purchasing cards, however, accruals for capital items should be debited to the relevant capital asset account. Generally, each month the previous month-end accruals, except for standing accruals, should be reversed and payments should be debited to current expense. If payment is not expected to be made until a future period, the Bank can elect to not automatically reverse the accrual.

11.61 Accruals for Compensated Absences

Reserve Banks must accrue a liability for employees' compensation for future absences if (1) the obligation is attributable to services already rendered, (2) the obligation relates to rights that vest or accumulate, and (3) payment of the compensation is probable and estimable. This requirement does not extend to sick-pay benefits unless they vest (i.e., an employee is paid for unused sick days upon termination).

The purpose of this accrual is to recognize the liability for vested or accumulated compensated absences.

- Vested rights are those for which the District has an obligation to make payment even if an employee terminates.
- Accumulated rights are earned, but unused, rights to receive payment for compensated absences that may be carried forward to one or more periods. Accumulated rights may be vested, in whole or in part.

The requirement to accrue a liability for compensated absences depends on whether the unused rights expire at the end of the year in which they are earned or accumulated and are carried forward to succeeding years. The cost of accumulated compensated absences should be accrued to the extent that it is probable that employees will use or be paid in future years for the increased benefits attributable to the accumulated rights and that the amount can be reasonably estimated. The accrual for the cost of sick pay benefits, however, should be limited to the vested amount.

> Example 1: Assume an employee accumulates vacation time throughout the year and, at the end of the year, has accumulated four weeks of vacation time. The District's policy allows employees to carry over a maximum of three weeks of vacation to the following year. The District should accrue a liability for the cost of three weeks of accumulated vacation time (accumulated portion), even if the District's policy is to pay only a maximum of two weeks of vacation in the event of termination (vested portion).
>
> Example 2: Assume that an employee earns sick-pay benefits throughout the year and the District's policy allows employees to accumulate sick-pay benefits, but limits the amount that can be paid to the employee at termination to two weeks (vested portion). In this case, the accrual should be limited to the vested portion only, or two weeks.

This accrual should be calculated by multiplying total hours of qualifying compensated absences by actual salary rates. Average salary rates may be used if actual rates are unavailable or as a practical expedient. To ensure the recognition of this liability while avoiding the burdensome requirements of distinguishing between salary and compensated absence expense on a weekly basis, this liability need not be continually adjusted to reflect individual accrual/usage of qualifying benefits. Rather, this liability and related expense should be adjusted at year-end, to reflect overall changes in the level of the liability. This liability should also be adjusted periodically for significant changes in the liability that result from events such as merit increases, significant staff level changes, or policy changes. For example, when merit increases are granted to employees, an adjustment will be required to increase the liability. Districts that grant merit increases on an employee's anniversary date should accrue the annual projected merit increase weekly ratably over the year in which the increases are granted.

11.62 Accruals for Contingent Liabilities

A loss contingency arises when an uncertain existing condition will be resolved by a future event that may result in the impairment of an asset or the incurrence of a liability. Consistent with FASB ASC Topic 450-20, Accounting for Contingencies, a loss contingency should be accrued if (1) it is probable that a future event will confirm the impairment of an asset or the incurrence of a liability, and (2) the amount is reasonably estimable. Examples of contingent liabilities are pending or threatened litigation and conditional asset retirement obligations (refer to paragraph 30.05). Districts should periodically conduct a review to determine if contingent liabilities exist that may require accrual. At a minimum, these accruals should be made at the end of every calendar quarter. Approval to accrue contingent liabilities must be obtained from the RBOPS Financial Accounting Policy and Reporting Section. Note: Information should be maintained on contingent liabilities that do not meet both tests required for establishing an accrual. This information may be required to be included in year-end footnote disclosures.

11.64 Accruals of Expenses for Employee Termination Programs (Involuntary/Voluntary)

Reserve Bank's employee termination plans are accounted for based on FASB ASC Topic 712-10, which is more applicable to Federal Reserve System severance and termination benefit programs than either FASB ASC Topic 420-10 or FASB ASC Topic 712-10. FASB ASC Topic 712-10 essentially defines whether payments should be accrued over the benefiting period under FASB ASC Topic 710-10 or recognized in total when it is probable and estimable in accordance with FASB ASC Topic 450-20. Reserve Banks generally provide separation payments to employees based on years of service and employees have a general understanding that they will be provided with a severance benefit if they are terminated as part of a general downsizing. As a result, the separation payments are considered a standard post-employment benefit rather than a program solely limited to a particular event. Benefits also 'accumulate' in that the amount of the payment increases based on years of service. Such a design is consistent with the FASB ASC Topic 710-10 concept that the payment is more related to past service rather than future service (as contemplated by FASB ASC Topic 420-10). Although these benefits do not vest, FASB ASC Topic 710-10 does allow for the accrual of nonvesting benefits when payment of that benefit is probable. Severance and termination benefits, including salary, Federal Insurance Contributions Act (FICA) taxes, and other related expenses should be accrued when the criteria for accrual are met and not limited to when they are provided as part of a termination program.

Involuntary program: If a Reserve Bank initiates an involuntary employee termination program, it must recognize the associated liability if the termination program is probable and the amounts are estimable. According to ASC 420-10-25-4, the probability test has been met when all four of the following conditions exist and have been communicated to the affected employees (communication date):

1. "Management, having the authority to approve the action, commits to a plan of termination.
2. The plan identifies the number of employees to be terminated, their job classifications or functions and their locations, and the expected completion date.
3. The plan establishes the terms of the benefit arrangement, including the benefits that employees will receive upon termination (including but not limited to cash payments), in sufficient detail to enable employees to determine the type and amount of benefits they will receive if they are involuntarily terminated.
4. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn."

The incremental cost associated with employees who add a year of service (1/2 month additional severance) between the communication date and the termination date should be recognized ratably over the period between the communication date and the service date rather than on the communication date. If the program requires an employee to work more than sixty days beyond notification in order to receive benefits, it may be necessary to accrue the liability over several periods.

Voluntary plan: If a Reserve Bank initiates a voluntary (early retirement program) termination program, it must estimate and recognize the liability for the termination benefits when the following conditions exist: (1) the appropriate level of management has approved and committed to a program that allows employees to terminate employment, (2) employees have accepted the program and it is unlikely that the election will be changed, and (3) the period to complete the termination is not likely to change. Any incremental costs such as retention incentives associated with voluntary retirement programs, unlike the involuntary termination program, should be accrued in total when the employee accepts the offer. If the election window for the program falls within a calendar year, the accrual may be made at the end of the window period; however, if the window crosses year-end, Reserve Banks should accrue only costs that are associated with employees who have indicated acceptance of the program.

Retention Benefits

Incremental additional termination benefits provided to employees as a retention incentive should be accrued evenly over the period from the communication date to the termination date. For retention with multiple payouts, each payout should be accrued from communication date to the end of each retention period (i.e., payout date).

Subsequent Adjustments to Accruals

In periods after initial measurement (communication date), changes in the accrued liability due to revisions in either the timing or amount of the estimated benefit payments should be recognized as an increase or decrease to the same expense line items as when the liability was initially recognized. For example, if employees to be involuntarily terminated leave prior to the payment date (either within or outside the Bank), the liability recognized by the Bank for termination benefits should be reduced, this reduction would result in a credit to expense for that period. Consistent with the current practice of adjusting accruals for compensated absences, Reserve Banks should adjust these accounts whenever there is a significant event, such as the close of a window period.

If current interest rates are low and the time period is relatively short, the difference between present value calculations and the nominal value should be immaterial. Therefore, in order to minimize complexity, cost, and opportunity for error, nominal values should be used for estimates of cash flows less than or equal to five years.

Retirement Related Benefits (Pension and Medical)

In general, the enhanced pension benefits will be treated as an amendment to the retirement plan and accounted for in accordance with FASB Topic ASC Topic 715-30 on the FRBNY's financial statements based on the actuarial valuation. RBOPS Financial Accounting Policy and Reporting Section and OEB staff within the FRBA should coordinate an evaluation of whether the magnitude of the terminations and retirements System-wide is large enough to require curtailment accounting near year-end.

The effect of employee terminations on the accounting for retiree medical plans will differ depending on the number and tenure of employees terminated. If the number and tenure of terminated employees is sufficient to significantly reduce the expected years of future service of the active participants (terminated employees are considered active participants for this test), then a curtailment exists. In general, the System has viewed reductions of less than five percent as not significant for curtailment purposes and reductions of ten percent or greater as significant.

The impact of curtailments varies depending on the nature of each Reserve Bank's retiree medical program. In general, reductions in staff result in curtailment gains. If, however, a Reserve Bank had a substantial amount of unrecognized prior service costs or unrecognized actuarial loss, a curtailment could result in a curtailment loss. Curtailment losses are recognized when probable and estimable (communication date), curtailment gains are recognized when employees terminate.

Given the complexity involved with these programs related to the timing of expense accruals, Reserve Banks should contact RBOPS Financial Accounting Policy and Reporting Section for guidance when considering such plans.

11.66 Accruals for Self-Insured Medical and Dental Expenses

A liability must be recognized for the amount of medical and dental claims that have been incurred but not paid. A claim has been incurred when the event (e.g., medical treatment) that precipitates future payouts has occurred. The amount of this liability should reflect an estimate of the amount that will be paid, ultimately, by the Bank (net of stop-loss insurance, if the Bank maintains such coverage). It is not appropriate to maintain a "reserve" for claims that may be incurred in the future. Any funds related to the provision of self-insured medical and dental expenses that are held on deposit by claims administrators should be reflected separately as an asset of the Bank, rather than as an offset to the accrued self-insured medical and dental liability. A District is considered to be self-insured unless the insurance carrier bears 100 percent of the risk of loss due to shortfalls between claims and premiums.

The liability reflected should be an estimate of the actual amounts of claims incurred but not paid. In order to maintain consistency among Reserve Bank estimates, a standard approach to this estimate has been adopted. The *year-end* liability should be based on the prior years' experience adjusted for current trends in claims. To establish a "subsequent claims ratio," determine the amount of claims paid in the current year that were incurred in the prior year (run-out claims) and divide this amount by the total claims paid in the prior year. This ratio should then be applied to the most recent 12 months of payments data available to obtain the amount of the liability. For the consolidated plans, OEB will make this estimate on a Systemwide basis and allocate differences based on each Bank's funding rate.

Exceptional circumstances (e.g., a change in claims administrator or plan design changes) may exist that would lead to a material misstatement of this liability if additional adjustments were not made. In such situations, the RBOPS Financial Accounting Policy and Reporting Section should be contacted for approval of an appropriate alternative estimation methodology.

Special Considerations:

Remember that medical payments and accruals for retirees and individuals on long-term disability are covered under FASB ASC Topic 715-60 and FASB ASC Topic 712-10, respectively, and should be excluded from the aforementioned calculations.

11.80 Suspense Account—General (240-150)

This account represents (1) miscellaneous items for which credit has been received but processing or information is necessary before final disposition is affected or (2) general ledger interface errors that do not have relevant information to post a balanced journal entry. Items that cannot be resolved should be cleared from this account and credited to either the difference account or a current expense account. (See paragraph 4.40.) Items relating to items in process of collection and deferred credit items should not be included in this account.

11.82 Exchange Translation Liability (240-190)

This account is used to record unrealized gains or losses on unsettled foreign exchange trades, Euro denominated reverse repurchase agreements, and accrued interest payable on Euro denominated reverse repurchase agreements.

11.84 Accumulated Benefit Obligation (240-300)

This account is used to recognize the funded status of various benefit plans. When the projected pension benefit obligation exceeds the fair value of plan assets, the difference is recorded to this liability account, as defined by FASB ASC Topic 715-20. Included in this account are also balances related to (1) the nonqualified retirement Benefits Equalization Plan, (2) the Supplemental Retirement Plan for Selected Officers of the Federal Reserve Banks, and (3) the postretirement medical and life insurance benefit plan. Entries related to these plans are based on actuarial valuations and actual benefit payments made by the OEB on behalf of the Reserve Banks. The accruals for the pension plans are offset to the net periodic pension cost (330-050) (see paragraph 12.30) or Accumulated Other Comprehensive Income (AOCI) (a sub-account of 320-025, Surplus), as required. The offset to the accruals for postretirement medical and life insurance are posted to the Operating Expense account (330-050) or AOCI, as required (see paragraph 12.10). Only service costs go to Operating Expenses (330-050) and all other cost components go to Other Components of Net Benefit Costs (330-060) (see paragraph 12.33).

Post-employment: This account is also used to record the liabilities for the long-term disability, income, medical, life, and survivor's income or workers compensation plan obligations in accordance with FASB ASC Topic 712-10, Employers' Accounting for Post-employment Benefits. Entries for these plans are based on actuarial valuations and actual benefit payments made by the OEB on behalf of the Reserve Banks; the benefit payments should offset the recorded liability for these plans. At year-end, each Reserve Bank adjusts the recorded obligations for the post-employment benefit plans, and the offset is posted to the Operating Expense account (330-050).

Thrift BEP: The liability associated with the Thrift Benefits Equalization Plan (Thrift BEP) is also recorded in this account. The Thrift BEP entries are made using information provided by the OEB at year-end based on the Plan account balance (not actuarially determined). Monthly payments made by the OEB on behalf of each Reserve Bank should offset the Thrift BEP liability. At year-end, each Reserve Bank may have to adjust the recorded obligation for the Thrift BEP, and the offset is posted to the Operating Expense account (330-050).

Deferred Compensation Plan: Effective April 2009, the liability associated with the deferred compensation plan (DCP) is also recorded in this account. The monthly DCP entries are made using information provided by the payroll system, OEB, and the third-party administrator (not actuarially determined). Benefit payments made by the OEB on behalf of each Reserve Bank offset the DCP liability. The monthly report provided by the third-party administrator is used to verify each Bank's DCP liability account.

Curtailments: Significant reductions in staff or changes in pension or medical plan benefits may require the recognition of additional gains or losses. As a practical matter, Reserve Banks should coordinate with RBOPS Financial Accounting Policy and Reporting Section and OEB staff when they anticipate substantial changes to staffing or the plan benefits. The provisions of FASB ASC Topic 715 are applied when determining if staff reductions or benefit changes result in a plan curtailment. A percentage reduction of greater than 10 percent indicates a curtailment. If a percentage reduction of expected future working lifetime is less than 5 percent, no curtailment is deemed to have occurred. A determination of the existence of a curtailment for a percentage reduction between 5 and 10 percent is based on individual facts and circumstances of the events. Reserve Banks should work with RBOPS Financial Accounting Policy and Reporting Section staff in evaluating whether a curtailment exists.

11.86 Interest on Reserves Accounts—Interest Due to Depository Institutions (240-430)

Section 19 of the Federal Reserve Act provides that the Board may prescribe regulations concerning the payment of earnings on balances held at a Reserve Bank. Regulation D: Reserve Requirements of Depository Institutions implements this provision and specifies the interest rate payable on balances of eligible institutions maintained at Reserve Banks, or the interest on reserve balances (IORB) rate. The Board of Governors sets the IORB rate at a rate not to exceed the general level of short-term interest rates and has the discretion to change the IORB rate at any time. Interest on an eligible institution's balance is calculated daily at the specified rate. An aggregate interest payment for all days in a maintenance period is made one business day after the maintenance period ends. Accruals are recorded in this liability account each business day as interest is earned.

Title II of the Financial Services Regulatory Relief Act of 2006 granted the Federal Reserve authority to pay interest to depository institutions for balances held at Reserve Banks effective in 2011. Section 128 of the Emergency Economic Stabilization Act of 2008 accelerated this authority to October 9, 2008. Accordingly, the Reserve Banks began paying explicit interest to depository institutions on balances held at Reserve Banks.

11.93 Term Deposit Facility (240-850)

This account is used to record term deposits of depository institutions held with the Reserve Banks. These term deposits are used by the Reserve Banks as a monetary policy tool to manage the aggregate quantity of depository institutions' reserve balances.

11.94 Federal Agency MBS Related Liabilities (240-875)

This account is used to record the fail liability for federal agency and GSE RMBS and CMBS purchases. A MBS fail liability results from a seller failing to provide a security to the FRBNY on the contractual settlement date. As a result, a liability is recorded for the obligation to fund the purchase. If the FRBNY fails to provide a security to a purchaser, a fail asset is recorded (paragraph 3.08). This account is also used by the FRBNY to record the obligation to return cash collateral posted by counterparties pursuant to commitments to purchase MBS within the SOMA. (See paragraph 40.13.)

11.95 Designated Financial Market Utilities Deposits (240-900)

This account is used to record the deposits for Designated Financial Market Utilities that have been designated as systemically important in accordance with Title VIII of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* of 2010 (Dodd-Frank Act).

11.96 Accrued Remittances to Treasury / Deferred Asset (240-925)

This account is used to record the liability or deferred asset related to earnings remittances to Treasury.

The Federal Reserve Act, as amended by the FAST Act effective December 4, 2015, requires that any amounts of the surplus funds of the Reserve Banks that exceed, or would exceed, the aggregate surplus limitation of $10 billion shall be transferred to the Board of Governors for transfer to the Treasury. Before the effective date of the FAST Act, the Board of Governors required the Reserve Banks to transfer excess earnings to the Treasury as interest on Federal Reserve notes after providing for the costs of operations, payment of dividends, and reservation of an amount necessary to equate surplus with capital paid-in.

The Federal Reserve Act was subsequently further amended by the Bipartisan Budget Act (Budget Act), effective February 9, 2018, by the Economic Growth, Regulatory Relief, and Consumer Protection Act (Consumer Protection Act), effective May 24, 2018, and by the National Defense Authorization Act for 2021, effective January 1, 2021, which reduced the aggregate surplus limitation to $7.5 billion, $6.825 billion, and $6.785 billion, respectively. Therefore, the Federal Reserve Act now requires that any amounts of the surplus funds of the Reserve Banks that exceed, or would exceed, the aggregate limitation of $6.785 billion shall be transferred to the Board of Governors for transfer to the Treasury. Each Reserve Bank remits excess earnings to the Treasury after providing for the cost of operations, payment of dividends, and reservation of an amount necessary to maintain surplus at the Bank's allocated portion of the aggregate surplus limitation.

A credit balance in this account represents the accrued remittances to be distributed to the Treasury. If a Reserve Bank's earnings become less than the costs of operations, payment of dividends, and maintaining surplus at an amount equal to the Bank's allocated portion of the aggregate surplus limitation, remittances to the Treasury would be suspended. A deferred asset is recorded in this account, and this debit balance represents the amount of net excess earnings the Reserve Bank will need to realize before remittances to the Treasury resume.

Deferred asset balances recorded in this account are periodically reviewed for impairment.

See paragraph 60.55 for further discussion.

11.98 Other Liabilities—Markets (240-950)

The balance in this account represents infrequent low-value Markets related transactions conducted by the FRBNY and is not participated to other Reserve Banks. Dedicated accounts must be established prior to program start dates for transactions related to Markets programs that are expected to be high-value or recurring. This account may be used, however, to record transactions for newly established programs until a dedicated account is established, when the balances should be reclassified to the dedicated account. At the close of business each December 31, this account balance should include only the low-value and infrequent Markets related transactions.

11.99 Central Bank Liquidity Swap Accounts (242-100)

When the FRBNY initiates a swap agreement with a foreign central bank for the purpose of obtaining foreign currency, the resulting liability is recorded in this account.

For example, the FRBNY may enter into a foreign currency liquidity arrangement whereby the Bank would obtain a foreign currency from a foreign central bank; in this example the foreign currency obtained from the foreign central bank would be recorded as a liability in this account. (See paragraph 4.94.)

12.00 Reverse Repurchase Agreements—Foreign Official and International Accounts (242-120)

This account is used to record the contract amount of reverse repurchase agreements executed with foreign official and international account holders. The FRBNY is authorized by the FOMC to sell Treasury, federal agency, and GSE securities and federal agency and GSE RMBS and CMBS under agreement with foreign official and international account holders and to repurchase the securities at an established point in time (securities sold under agreements to repurchase). (See paragraph 40.20.) On the day of settlement, the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank according to its current domestic allocation rate. (See paragraph 40.70 for the participation methodology.)

12.01 Reverse Repurchase Agreements—Primary Dealers and Expanded Counterparties (242-140)

This account is used to record the contract amount of reverse repurchase agreements executed with primary dealers, selected money market funds, and others. The FRBNY is authorized by the FOMC to sell Treasury, federal agency, and GSE securities and federal agency and GSE RMBS and CMBS under agreement with primary dealers, selected money markets funds, and others and to repurchase the securities at an established point in time (securities sold under agreements to repurchase). (See paragraph 40.20.) On the day of settlement, the FRBNY participates a share of the transaction to each Reserve Bank. Related interest income and gains and losses are participated to each Bank according to its current allocation rate. (See paragraph 40.70 for the participation methodology.)

12.05 Capital Paid-In (310-025)

The balance of this account represents the outstanding paid-in value of capital stock issued to member banks as required by law. The par value of shares is one hundred dollars and the paid-in value is $50. A member bank is required to subscribe to the capital stock of its Reserve Bank in an amount equal to 6 percent of its capital and surplus.[8] Half of the subscription is paid in and the other half is subject to call. (The shares do not carry the power through voting to control the management of the Reserve Bank as does ordinary stock in private banks and corporations.) Changes in a member bank's stock or surplus may require an adjustment in its holdings of the Reserve Bank's capital stock as outlined in Regulation I. The stock may not be transferred, nor may the owning member bank hypothecate its shares.

12.10 Surplus (320-025)

The balance of this account represents the portion of net income that is retained by the Bank. Before the December 4, 2015 amendments to the Federal Reserve Act, the

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[8] The total subscription of a mutual savings bank shall equal six-tenths of 1 percent of its total deposit liabilities. (12 CFR 209.4(b))

Board of Governors required each Reserve Bank to maintain a surplus balance equal to its capital paid-in. On a daily basis, surplus was adjusted to equate the surplus balance to capital paid-in.[9]

Effective January 1, 2021, the Federal Reserve Act limits aggregate Reserve Bank surplus to $6.785 billion. Reserve Bank surplus is allocated among the Reserve Banks based on the ratio of each Bank's capital paid-in to total Reserve Bank capital paid-in as of December 31 of each year. On a daily basis, the Board of Governors requires an adjustment to surplus to equate the surplus balance to the Reserve Bank's allocated portion of the $6.785 billion aggregate surplus limit. (See paragraph 12.60.)

AOCI is a component of each Reserve Bank's surplus account, and a separate account has been established to record transactions related to AOCI. (See paragraph 11.84.) The balance of AOCI should be included with the Bank's surplus balance in computing the amount necessary to equate surplus to the Reserve Bank's allocated portion of the aggregate surplus limitation.

Each Reserve Bank should ensure that all entries for transactions to the capital paid-in and AOCI accounts have been recorded before equating surplus to its allocated portion of the aggregate surplus limitation. The following adjustment should be recorded:

Dr / Cr:	Transferred to or from Surplus (330-225) $xxx
Cr / Dr:	Surplus (320-025) $xxx.

12.20 Current Income (330-025)

This account includes income from all sources for the year to date. The income is derived from assets as described below. Significant income items should be accrued as described in paragraphs 3.95 and 4.92 when earned. Other income is ordinarily credited when received.

Income—Receipts representing interest on loans to depository institutions or others, penalties on reserve account deficiencies or overdrafts in reserve or clearing accounts, interest from System Open Market Account (SOMA) and foreign currency holdings, and other receipts specifically identified.

1. ***Loans***—Interest earnings on loans to depository institutions, and earnings from any other loans, which may include loans to Federal Intermediate Credit Banks, other Federal Reserve Banks, and participants in programs or facilities with broad-based eligibility in unusual and exigent circumstances.
2. ***Acceptances***—Discount earned on acceptances.
3. ***U.S. Treasury, Federal Agency, and GSE Debt securities - System account***—Interest earned plus discounts accreted less premiums amortized on Treasury, federal agency, and GSE debt securities held in SOMA. Discounts earned on Treasury bills held in SOMA. This line item includes interest income generated from tri-party repurchase agreements.
4. ***Other securities***—Interest earnings on bills, notes, revenue bonds, and warrants issued by any state, county, district, political subdivision or municipality in the continental United States, including irrigation, drainage, and reclamation districts,

[9] Prior to January 1, 2011, surplus was equated to the level of capital at December 31 of each year.

plus discounts accreted and less premiums amortized. Also includes interest earnings on federal agency and government sponsored enterprise mortgage-backed securities.

5. ***Foreign currencies***—Participation in interest received on deposit balances with foreign banks, discount earned on acceptances payable in foreign currencies, and other earnings from investments denominated in foreign currencies.
6. ***Deficiencies in required balances***—Charges assessed depository institutions on the amount of their deficiencies in required balances.
7. ***Daylight and Overnight Overdraft charges***—Charges assessed depository institutions for intra-day (daylight) and overnight overdrafts in accounts maintained with the Reserve Bank.
8. ***Funds Settlement Fees***—Earnings associated with the funds settlement component of the book-entry transfer of Treasury securities.
9. ***All other***—Other earnings that do not come within the above definitions should be included in this classification. Explanations for these amounts should be provided to RBOPS Financial Accounting Policy and Reporting Section.
10. ***Services***—Amounts collected under Section 11A of the Federal Reserve Act for services to depository institutions.

Revenues—Based on FASB ASC Topic 606, Revenue From Customers, Reserve Banks should record revenues earned including amounts collected under Section 11A of the Federal Reserve Act for services to depository institutions for Check, ACH, Electronic Access, Funds, FedNow, Currency Fees, and Securities. Income from services is recorded as current income and should not be netted with the expenses incurred to provide the services or support costs paid to other Reserve Banks for costs that they incur in providing these services.

Individual ledger accounts are maintained for control purposes and to facilitate verification of income according to source. In the case of income from services, the ledger should be supported by subsidiary accounts in the same detail as the schedule of priced services. These subsidiary accounts must be posted currently and, together with any accrual accounts that the Bank elects to maintain separately, added to the total in the ledger at the close of business each day.

A subsidiary account may also be established for each priced service to record variances between accrued service income and the amount actually charged depository institutions due to absorption of differences. The use of this account should facilitate reconcilement of the general ledger with internal cost/revenue reports.

12.30 Operating Expenses (330-050)

The balance of this summary account represents the combined year-to-date actual and estimated net expenses that the Reserve Banks have incurred in performing business operations. The operating expenses subaccounts are as follows:

- *Operating Expenses*. The balance of this subaccount represents year-to-date operating expenses, net of expenses reimbursed. Operating expenses include the service cost component associated with the Reserve Bank's future obligation to provide medical and life insurance benefits to retirees in accordance with FASB ASC Topic 715-60.
  - *Reimbursements*. Receipts representing recoupment of expenses incurred in performing prescribed activities as Fiscal Agent for the Treasury and other Federal agencies.

– *Recoveries*. All receipts other than those defined as Revenue, Income and Reimbursements, including receipts that are not material in amount received in connection with services incidentally related to priced services.

- *Accrued Expenses Estimated.* The balance of this subaccount and the liability account Accrued Expenses Unpaid—Estimated (240-200) provides for the accrual of net operating expenses on an estimated basis during the month. (See paragraph 11.56.)
- *System Net Periodic Pension Cost.* This account is used to record the service cost component of the net periodic pension cost related to the Federal Reserve System Plan, computed in accordance with the provisions of FASB ASC Subtopic 715-30. This account is also used to record at least monthly the net pension costs associated with the nonqualified retirement Benefit Equalization Plan and the Supplemental Retirement Plan for Selected Officers of the Federal Reserve Banks accruals (see paragraph 11.84). The OEB provides information necessary to process entries to this account.

12.33 Other Components of Net Benefit Costs (330-060)

This account is used to record at least monthly the components of net periodic pension cost for all retirement plans, exclusive of the service cost component, in accordance with the provisions of FASB ASC Topic 715. There is also a monthly recording of the other cost components, exclusive of the service cost component, associated with the Reserve Bank's future obligation to provide medical and life insurance benefits to retirees in accordance with FASB ASC Topic 715-60.

12.36 Interest on Reserves and Term Deposits—Interest Expense (330-078)

Interest is paid to depository institutions for balances held in their account at a Federal Reserve Bank. The interest on depository institutions' balances is calculated daily at the IORB rate. Payments are made a day after the maintenance period is finalized. Accruals are recorded in liability account Interest on Reserves Accounts—Interest Due to Depository Institutions (240-430) each business day as interest is earned. Interest is also paid for term deposits held by eligible depository institutions. The cost of interest on reserves balances and on term deposits is recorded to this account.

12.37 Provision for Credit Loss Expense (330-080)

Reserve Banks are required to recognize lifetime expected credit losses on a loan measured at amortized cost, regardless of whether the risk of credit loss is determined to be remote. In the event that it would be needed, detailed instructions on how to recognize, measure, and record an allowance for credit loss are provided in paragraph 81.01, Allowance for Credit Losses. The Reserve Banks should use account 330-080 to record the expense provision. The provision for credit loss expense recorded in this account must be approved by the RBOPS Financial Accounting Policy and Reporting Section.

12.40 Profit and Loss (330-100)

This account is used for recording income and losses which are not current in nature or are not applicable to current earnings or current expenses. These include realized gains and losses on sales of securities and on foreign currencies, profit or loss on the sale of real estate (originally acquired for potential Bank use), the write-off of stale officers' and certified checks (paragraph 10.80), losses that are sustained in the handling or transportation of currency, recoveries and unrealized losses on the value of other real estate (originally acquired for potential Bank use) held for sale, and gains or losses on works of art. The account should not normally be used to adjust prior year income or expenses except for the correction of prior year accounting errors when the amount would seriously distort income or expenses of the current year. Entries to the account for prior year items may be made only with the prior approval of the RBOPS Financial Accounting Policy and Reporting Section.

The profit and loss account should not include dividends and rebates on insurance policies or any additional premium payments on worker's compensation or other insurance regardless of the year for which the refunds or additional payments apply. Such amounts should be entered to current year income or expenses. Other items from the previous year, which should normally be applied to current year income or expenses rather than profit and loss, are receipts from vending machines, refunds from courier contracts, adjustments for the difference between accounts payable and the actual billings, and adjustments for the difference between accrued income from services and actual billings.

The profit and loss account should also exclude losses arising from the ongoing operations of the Reserve Banks. Any such losses should be charged to current expense. The balance represents the net total of miscellaneous entries, such as the following:

1. ***Profit (loss) on sale of Bank premise assets or other real estate***—The difference between net book value and the proceeds from the sale of Bank premises assets and other real estate (formerly used in bank operations).
2. ***Recoveries and unrealized losses on the value of other real estate held for sale***—The difference between net book value and net realizable value of other real estate (formerly used in Bank operations) held for sale. (See 30.97.)
3. ***Profit (loss) on sale of "Other assets—claims account closed banks"***—Book profit or loss resulting from the sale (or other final disposal) of "Other assets—claims account closed banks." When an allowance for estimated losses on such property is carried, the entire difference between gross carrying value of the particular asset and the proceeds received, if disposition results in a loss, may be charged to the allowance unless such a charge would result in a debit balance therein, in which case the excess should be charged to Profit and loss. If disposition results in a profit, the excess should be credited to Profit and loss.
4. ***Losses (not expected to be recovered) on shipments of money***
5. ***Recoveries of losses on shipments of money***
6. ***Other recoveries***—Other recoveries of amounts previously charged to profit and loss, such as recoveries of unclaimed funds.
7. ***Losses covered by loss sharing agreement***—Rewards, advances, and expenses absorbed or prorated under the loss sharing agreement.
8. ***Reimbursement from Treasury for purchases of uncut sheets of Federal Reserve notes***
9. ***Errors found in work of prior years***—Errors involving significant amounts reported in income or expenses prior to the current year. Correction of errors of lesser amounts should be made in the appropriate income or expense account. (The correction of errors between years through Profit and loss should be limited to items involving significant amounts and must have prior approval from the RBOPS Financial Accounting Policy and Reporting Section.)
10. ***Interest expense*** —Interest expense for reverse repurchase agreements undertaken by the System Open Market Desk.

11. ***Profit or loss on foreign exchange transactions (net)***—Participation in foreign exchange profits and losses, including revaluations of foreign currency holdings and outstanding swap commitments at current market exchange rates.
12. ***Discount on foreign currency***
13. ***Loss on counterfeits*** —(Only with approval of RBOPS Financial Accounting Policy and Reporting Section.)
14. ***Profit or loss on sales of Treasury, federal agency, and GSE securities held in SOMA (net)***
15. ***Profit or loss on works of art***
16. ***Profit or loss, including interest income and expenses, incurred by Reserve Banks and consolidated LLCs from lending authorized under section 13(3) of the Federal Reserve Act***

For further discussion of reporting profit and loss, see paragraph 60.28.

12.43 Cost of Unreimbursed Treasury Services (330-110)

This account is used to record the cost of services provided to Treasury for which recovery is not anticipated. At the time entries are made to the reimbursable account, an estimate is made of the amount of the claim that is not expected to be received. The offsetting account would be the contra-asset account, Allowance for Doubtful Reimbursement or Reimbursable expenses for direct write-offs. Near the end of each year, adjusting entries may be required in order for the balance in this account to equal the cost of services provided to Treasury during the year for which Treasury has informed the Federal Reserve reimbursement will not be made or which the Federal Reserve has determined is unlikely. This account should be closed out at the end of each year. Costs in this account should be generated primarily from District or special projects that have not been approved by the Bureau of Fiscal Service of Treasury. This account should also be used to record allowance for the non-Treasury agencies and receivable from others.

12.45 Assessments by Board of Governors (330-125 and 330-150)

Board Expenditures (330-125)

Section 10 of the Federal Reserve Act authorizes the Board to levy semi-annually upon the Reserve Banks, in proportion to their capital stock and surplus, an assessment sufficient to pay its estimated expenses for the half of the year succeeding the levying of such assessment, together with any deficit carried forward from the preceding half year. The Richmond Reserve Bank processes an InterFRB transaction for each Reserve Bank's portion of the assessment with a debit to this account and a credit to the Interdistrict Settlement account. The Board is also authorized to leave on deposit in the Reserve Banks the proceeds of such assessments. Pursuant to this authority, the Board maintains deposit accounts with the Richmond Reserve Bank and at the time of each assessment requests credit for one-half of the amount to its General Fund deposit account at Richmond. The remaining half is called on the first business day in April and October.

F.R. Currency Costs (330-150)

Section 16 of the Federal Reserve Act requires that all expenses in executing the laws relating to the procurement of Federal Reserve notes, including expenses incidental to their issue and retirement, be paid by the Reserve Banks and included in the Board's assessment against the Banks. The Board assesses the Reserve Banks, on a scheduled basis, for currency printing, shipping, issuance, retirement, educational services, research and development, and counterfeit deterrence costs. The costs are allocated based on each Bank's share of the total number of Federal Reserve notes outstanding at all Reserve Banks on December 31st of the previous year. Reserve Banks should debit this account upon payment of these costs. See appendix A.3.

12.46 Assessments by Board of Governors—Bureau of Consumer Financial Protection (330-135)

This account is used to record the Board of Governors' assessments to the Reserve Banks. In accordance with the Dodd-Frank Act the Board of Governors assesses the Reserve Banks to fund the operations of the Bureau of Consumer Financial Protection (CFPB). The funding cannot exceed a fixed percentage of the total operating expenses of the System, and annually it will be adjusted in accordance with the provisions of the Dodd-Frank Act.

12.50 Dividends Accrued Since January 1 (330-175)

The balance of this account represents the year-to-date accumulated dividends on outstanding capital stock paid-in from member banks during the year. The balance is increased daily based on accruals and adjustments; it is closed out as part of the distribution of net earnings (see paragraph 60.55). The amount added to the account each day is computed on the total Reserve Bank capital paid-in from member banks as of the opening of business that day (close of business previous day) as described in paragraph 11.50 (Accrued Dividends Unpaid).

12.60 Earnings Remittances to Treasury, Net (330-200)

Before the enactment of the FAST Act, the Board of Governors, under authority of Section 16 of the Federal Reserve Act, required Reserve Banks to pay the U.S. Treasury, as interest on Federal Reserve notes, all net earnings after providing for dividends and the amount necessary to equate surplus with paid-in capital. This practice began in 1947. As a result of operations essential to Government financing during the war, and operations required by the needs of business and the public for credit and currency, earnings of the twelve Federal Reserve Banks were at relatively high levels. It was expected that net earnings of the Federal Reserve Banks for 1947, after payment of the statutory dividends to member banks, would aggregate more than $60 million. In view of these facts and the fact that at the end of 1946 the surplus of each Federal Reserve Bank was equal to its subscribed capital, the Board decided to invoke its authority, granted to it under Section 16 of the Federal Reserve Act, to levy an interest charge on Federal Reserve notes issued by the Federal Reserve Banks. The purpose of this interest charge was to pay into the Treasury approximately 90 percent of the net earnings of the Federal Reserve Banks for 1947.

The authority to levy an interest charge on Federal Reserve notes not covered by gold certificates had not been used previously, chiefly because of the existence, prior to 1933, of so-called franchise tax provisions of the law that had a similar effect; that is, of transferring excess earnings of the Reserve Banks to Treasury. Under these provisions, which were repealed in 1933, each Federal Reserve Bank was required to pay a franchise tax to the government equal to 90 percent of its net earnings after it had accumulated a surplus equal to its subscribed capital. As of the end of 1932 the Federal Reserve Banks had paid franchise taxes to Treasury amounting to $149 million. At that time the Federal Reserve had accumulated surplus accounts of $278 million, as compared with subscribed capital aggregating $302 million. The Federal

Reserve Act amendment, contained in the Banking Act of 1933, which established the Federal Deposit Insurance Corporation required each Reserve Bank to pay an amount equal to one-half of its surplus on January 1, 1933, as a subscription to the capital stock of the FDIC on which no dividends are paid. These stock subscriptions amounted to $139 million and reduced the surplus of the Federal Reserve Banks to an equivalent figure, or considerably less than one-half of their subscribed capital. Congress, therefore, eliminated the franchise tax in order to permit the Federal Reserve Banks to restore their surplus accounts from future earnings. Net earnings for the next ten years were relatively small, and at the end of 1944 the combined surplus accounts of the Federal Reserve Banks were less than 75 percent of their subscribed capital. During the next two years, however, net earnings increased substantially, due primarily to large holdings of Government securities accumulated through open market operations. This resulted in transfers to surplus accounts that increased the combined surplus of the Federal Reserve Banks to about $439.8 million at the end of 1946, as compared with subscribed capital of nearly $373.6 million.

Under the circumstances, the Board concluded that it would be appropriate for the Federal Reserve Banks to pay to Treasury the bulk of their net earnings after providing for necessary expenses and the statutory dividend. In effect, this involved paying currently to Treasury funds which, under existing law, would otherwise come to it only in the event of liquidation of the Federal Reserve Banks. The Federal Reserve Act still provides that, in case of liquidation of the Federal Reserve Banks, any surplus remaining after the payment of all claims shall be paid to Treasury. By invoking its authority under Section 16 of the Federal Reserve Act, the Board was able to accomplish the same results as were accomplished by the payments of franchise tax, i.e., the transfer of excess earnings to the Government.

Effective December 4, 2015, the Federal Reserve Act was amended to limit the Reserve Banks' aggregate surplus funds to $10 billion. Effective February 9, 2018, the Federal Reserve Act was amended to limit the Reserve Banks aggregate surplus funds to $7.5 billion. Effective May 24, 2018, the Federal Reserve Act was amended to limit the Reserve Banks aggregate surplus funds to $6.825 billion. Effective January 1, 2021, the Federal Reserve Act was amended to limit the Reserve Banks aggregate surplus funds to $6.785 billion. The Federal Reserve Act requires that any amounts of the aggregate surplus funds of the Reserve Banks that exceed, or would exceed, the aggregate limitation of $6.785 billion shall be transferred to the Board of Governors for transfer to the Treasury. Each Reserve Bank remits excess earnings to the Board of Governors for transfer to the Treasury after providing for the cost of operations, payment of dividends, and reservation of an amount necessary to maintain surplus at the Bank's allocated portion of the $6.785 billion aggregate surplus limitation. (See paragraph 60.55 for computation and reporting of remittances.)

Earnings remittances to Treasury, net are accounted for as expense of the period in which they are accrued because the recurring payments are a nondiscretionary cost from the Reserve Banks' perspective.[10]

The Reserve Banks remit accrued earnings to the Treasury on a weekly basis.

[10] Prior to the FAST Act, the Board levied an interest on Federal Reserve notes charge on the Reserve Banks. The FAST Act requires the transfer of excess earnings to Treasury. In both cases, the amount in Reserve Bank surplus is controlled by creating a non-discretionary obligation to transfer excess residual net earnings to Treasury.

The daily accrual is an automated entry processed by the general ledger application each night. If an adjustment to an income or expense account is made during the late general ledger process, the balance in the Undistributed Net Income account requires a manual adjustment to properly record a remittance accrual and the following entry to bring Undistributed Net Income to zero.

Dr / Cr:	Earnings Remittances to Treasury, net (330-200) $xxx
Cr / Dr:	Accrued Remittances to Treasury / Deferred Asset (240-925) $xxx

12.65 Transferred to or from Surplus (330-225)

The purpose of this account is to record the transactions necessary to equate surplus to the Reserve Bank's allocated portion of the $6.785 billion aggregate surplus limitation (see paragraph 12.10). The amount remains in this account until the closing of the books in January of each year. See paragraphs 12.10 and 60.55 for further discussion.

2 Collateral and Custodies

Contents

20.01 General

The preceding chapter discusses the periodic reporting of the assets and liabilities of Federal Reserve Banks. Chapter 2 is concerned with the accounts covering securities and other valuables, which are to be reported at the end of each month on the reverse of the FR 34. Federal Reserve Banks act as custodians for securities and other valuables pledged by depository institutions as collateral for borrowings from Reserve Banks and securities pledged as collateral to the Federal government. As fiscal agents, the Banks also act as custodians for securities pledged by nondepository institutions, including securities that are held for Government departments and officials in a fiduciary capacity. As the issuing and/or paying agents for the U.S. Government and certain Government-sponsored agencies, the Reserve Banks are accountable for unissued stock and for retired or paid securities, held pending shipment or destruction. The Reserve Banks also hold gold and other valuables, in accordance with safekeeping agreements with Treasury, foreign central banks, and other institutions. The objective in reporting the various collateral and custody items on the reverse of the FR 34 is to assure adequate disclosure for purposes of verification and control. For purposes of this chapter, “book entry” securities refer to Fedwire book entry securities only.

20.02 Book Entry vs. Definitive Custodies

Two amount columns are provided on the reverse of form FR 34: one titled “Definitive” and the other titled “Book Entry.” All book entry securities should be reported in the Book Entry column and all definitive securities and other custodies, including custody receipts, should be reported in the Definitive column. Custodies in book entry form that are held for the reporting office by another Federal Reserve office should also be shown in the Book Entry column, and included on the line for “Held by other offices in own District” or “Held by other FR Banks,” as the case may be.

20.03 Special Depositaries, Treasury Tax, and Loan Accounts

As fiscal agents the Reserve Banks maintain records for certain balances in Treasury's deposit accounts at commercial banks and thrift institutions. For example, when qualified depositaries that hold investments of Treasury balances receive payment for Federal taxes, the depositaries hold the funds until Treasury withdraws or calls the balances held at the depositaries. When investments mature or calls are made, the funds are remitted through the reserve accounts of depository institutions. The balance reported in this item should represent the aggregate of the individual demand deposit accounts, as well as open-ended note accounts.

20.04 Classification/Valuation of Holdings

Classification: To properly reflect the location, purpose and accountability for custodies recorded on the books of the Federal Reserve Banks, the various collateral and custody accounts are subdivided into four categories: *Held in Own Vaults*, *Held by Other Offices in Own District*, *Held by Other Federal Reserve Banks*, and *Held by Depository Institutions*. In general, all book-entry securities (except securities issued by international organizations) should be classified as *“Held In Own Vaults.”* For book-entry securities issued by international organizations, all Federal Reserve Banks (except the FRBNY) should classify their holdings of these securities as *“Held By Other FRBs.”* The FRBNY, however, should classify their holdings of these securities as *“Held In Own Vaults.”* The FRBNY should then classify the roll-up of all the other Reserve Banks’ holdings of these securities as *“Custodies Held For Other F.R. Banks.”* (See paragraph 21.10.)

The following characteristics should be considered to determine the proper classifications for custodies on both office and District level FR 34s. The descriptions below focus on definitive holdings; however, except for the reference to trust receipts, the same principles apply to book-entry securities. The classifications of *"Held by DI's"* and *"Held by Other Offices in Own District"* only apply to definitive securities and should never be used for book entry securities:

Location of Physical Security

All custodies held by an office must appear on that office's FR 34 Reverse as *Held in Own Vaults*. Trust receipts held by an office that represent custodies held outside the System are classified as *Held by Depository Institutions*.

Collateral Function

Custodies are recorded on the books of the Federal Reserve System for one of two purposes: collateral to protect the System or a government entity against certain risks; or as a safekeeping service. Custody items held as collateral should be reflected in the appropriate function (Loans, TT&L, etc.); if the same custody is used to collateralize differing transactions during the day, it should be reflected on the FR 34 Reverse under the function it serves at end-of-day and should be recorded and carefully monitored in departmental records to reflect the purpose served intraday. Other security holdings are reflected in the appropriate *Custodies Held for...* accounts.

Location of Applicable Function

The Federal Reserve System has a wide variety of both decentralized and consolidated processes at the District and office levels. In order to reflect proper accountability on the FR 34 Reverse, offices which have functional units that may require collateral must reflect all of this associated collateral on their FR 34 Reverse regardless of where that collateral is located. To distinguish between physical accountability and functional accountability, offices should reflect these custodies as *Held by other offices in own District* or *Held by other Federal Reserve Banks*. Trust receipts held by other offices or FRBs are treated the same as other custodies in these accounts; only the office which has physical possession of the trust receipts is required to distinguish on the FR 34 Reverse whether the security is physically held in a Federal Reserve vault or at a depository institution.

The following are examples of proper classification on each office's FR 34 reverse and on the combined District's FR 34 reverse:

Example #1: Loan Function is centralized at the head office; safekeeping functions are decentralized.

Collateral for Loans:	FR 34 Head Office	FR 34 Branch 1	FR 34 Branch 2	FR 34 District
Held in own vaults	200	100	200	500
Held by other offices in own District	380	-	-	N/A
Held by other FR Banks	25	-	-	25
Held by depository institutions	150	50	30	230

Example #2: Function is decentralized in all offices; Custody safekeeping is entirely centralized at Branch 1 except for trust receipts entirely held at Branch 2. (Each office has 200 TT&L collateral)

Collateral for TT&L	FR 34 Head Office	FR 34 Branch 1	FR 34 Branch 2	FR 34 District
Held in own vaults	-	500[1]	-	500
Held by other offices in own District	200	30	130	N/A
Held by other FR Banks	-	-	-	-
Held by depository institutions	-	-	100[2]	100

[1] Head Office=200; Branch 1=170; Branch 2=130
[2] Branch 1=30 Branch 2=70

Valuation

Definitive collateral that will be redeemed at par at maturity and all book entry collateral should be reported at par value. Holdings of definitive collateral whose par value may increase (as in the case of certain collateralized mortgage obligations) or decrease (as in the case of mortgage-backed securities) should be reported at the current outstanding principal value.

20.05 Collateral for Treasury Tax and Loan Accounts (Definitive and Book Entry)

Pursuant to 31 CFR 203, the funds held in Treasury Tax and Loan accounts, except for amounts covered by FDIC insurance, are secured by the pledge of collateral. The collateral must be of a type deemed acceptable by Treasury as covered in the Code of Federal Regulations. Holdings of collateral should be subdivided and reported as described in paragraph 20.04.

20.10 Collateral for Loans (Definitive and Book Entry)

All loans made by the Reserve Banks are secured, usually by collateral. Where feasible to minimize unnecessary bookkeeping, a Reserve Bank should carry securities in this account even though the owning bank is not currently borrowing. Holdings should be subdivided and reported as described in paragraph 20.04.

20.15 Collateral for Overdrafts (Definitive and Book Entry)

Reserve Banks may, in certain situations, require a depository institution to pledge collateral in the event the institution's deposit account becomes overdrawn during the day or is overdrawn at the close of the business day. Any such collateral pledged for overdrafts is to be subdivided and reported as described in paragraph 20.04.

20.20 Accountability to Treasury for U.S. Government Securities: Marketable Securities (Definitive Only)

Reserve Banks no longer process these items. Items sent to Reserve Banks in error should be forwarded to Treasury's Bureau of Public Debt and reported as Collateral and Custody Items in Process (see paragraph 21.50) until shipped to the Bureau of Public Debt.

20.40 Accountability to Treasury for U.S. Government Securities: Non-marketable Securities (Definitive Only)

Savings Bonds Unissued On Hand—Report the face value of savings bonds (all series), retirement plan bonds, and individual retirement plan bonds that fall into the following categories: Unissued stock; spoiled bonds; issued bonds not reported to Treasury (for example, sales and issues on reissue such as bonds issued for claims to replace valid issued bonds that were lost, stolen, or destroyed); unissued stock claims (bonds lost, stolen, or destroyed before being issued); canceled sales for which the original bond is not in-house; in-transit shipments of unissued stock to the Federal Reserve Bank of Philadelphia; and bond shipments awaiting delivery to issuing agents. Only the Federal Reserve Bank of Minneapolis should report this account.

20.45 Accountability to Treasury for U.S. Government Securities—On Consignment: Non-marketable Securities (Definitive Only)

Savings Bonds on Consignment with Issuing Agents—Report the face value of savings bonds (all series), retirement plan bonds, and individual retirement plan bonds consigned to all issuing agents. Bonds that are lost, stolen, or destroyed should be included until Treasury has notified the Reserve Bank that credit is allowed. Only the Federal Reserve Bank of Minneapolis should report this account.

20.50 Savings Bonds Issued—Book Entry

This account includes book-entry savings bonds held in safekeeping for trustees of qualified employees' savings and thrift plans. Only the Federal Reserve Bank of Minneapolis should report this account.

20.55 Accountability for Other Securities (Definitive Only)

This account should be reported by the FRBNY only.

- *U.S. Government Agencies*—This account includes the total accountability for bearer and registered (designated and undesignated) securities of U.S. Government agencies.
- *Unissued*—Report the par value of the general and reserve stock of bearer and registered (designated and undesignated) U.S. Government agency securities, including spoiled and mutilated securities.
- *Retired*—Report the par value of all bearer and registered U.S. Government agency securities retired before maturity as a result of processing servicing transactions; such as, interdistrict transfers, conversions to book-entry, denominational exchanges, and registered exchanges for bearer.
- *Canceled Redeemed*—Report the par value of all matured bearer and registered U.S. Government agency securities for which the depositors have been paid.

20.70 Accountability for Other Securities (Definitive Only)

- *International Organizations*—This account includes the total accountability for bearer and registered (designated and undesignated) securities issued by international organizations; such as, the International Bank for Reconstruction and Development. This account should be reported by the FRBNY only.
- *Unissued*—Report the par value of the general and reserve stock of bearer and registered (designated and undesignated) securities unissued by international organizations, including spoiled and mutilated securities.

- *Retired*—Report the par value of all bearer and registered securities issued by international organizations that have been retired before maturity as a result of processing servicing transactions; such as, denominational exchanges and transfers of ownership.
- *Canceled Redeemed*—Report the par value of all matured bearer and registered securities issued by international organizations for which the depositor has been paid and the issuer has been charged.

20.80 Other Custodies Held as Fiscal Agent of the Treasury

This account includes gold held for the Exchange Stabilization Fund and any other holdings of gold as agent of the Treasury, as shown below. Custodies besides gold include collateral acquired under the loan guarantee program pursuant to the Defense Production Act of 1950, as amended. “Special custody account: Other” *ordinarily* will be used only by the FRBNY under specific instructions.

- Gold–Held in own vaults
- Gold–Held by other Federal Reserve Banks
- Other

Gold that a Reserve Bank owns should be reported in Currency and Coin Exhibits. (Account 170-375, see paragraph 4.70.)

20.85 Custodies Held for Commodity Credit Corporation

This includes all custodies held for the Corporation. Where Branches do not act as custodians for the Commodity Credit Corporation but hold such custodies for the account of the head office, the Branches should show them as “Custodies held for other offices in own District.” The head office would report the custodies according to the proper classification.

20.90 Custodies Held for Treasury

Custodies held for the Treasury are subdivided according to the captions below. Under the special gold custody account for display purposes, there should be reported gold coins and gold certificates held as specimen under special authority from Treasury.

- Special gold custody account:
- For display purposes gold certificates
- Other gold bars

20.95 Custodies Held for Other Government Departments, Agencies, and Officials (Definitive and Book Entry)

This account includes custodies held for the Directors and Commissioner of Internal Revenue; Judges and Clerks, U.S. District Courts (includes CRIS holdings); Public Housing Administration; General Services Administration; Federal Deposit Insurance Corporation; U.S. Citizenship and Immigration Services; Secretary of the Treasury; Treasury (as security for Government deposits in other than Treasury Tax and Loan Account); State Treasuries; and others. Holdings should be subdivided and reported as described in paragraph 20.04.

21.05 Custodies Held for Other Offices in Own District (Definitive Only)

Custodies held by head office for Branches and by Branches for head office and other Branches are reported in this account. No amount will appear opposite this caption on the combined form FR 34, inasmuch as it would represent a duplication of amounts reported elsewhere under the appropriate classification by the office for whose account the custodies are held.

21.06 Custodies Held for System Open Market Account

Includes all securities held in custody for the SOMA. Securities loaned or undelivered should not be included. This account should be reported by the FRBNY only.

21.10 Custodies Held for Other Federal Reserve Banks (Book Entry Only)

Items included represent custodies held for other Federal Reserve Banks (but not for other offices in own District). The FRBNY should include in this account those securities issued by international organizations, which can officially be held only by the FRBNY but which may, de facto, be held in book entry safekeeping by other Reserve Banks. Thus, this category would include the roll-up of all the other Reserve Banks' holdings of international securities.

21.15 Custodies Held for Depository Institutions (Book Entry Only)

The account covers ordinary safekeeping of regular and "strippable" securities, including the corpus from any stripped security and pledges by depository institutions to various municipalities, county, state, and other officials (other than U.S.) generally referred to as "pledged" securities or "joint safekeeping." Also included are securities issued by international organizations that can officially be held only by the FRBNY but that are, de facto, held by other Reserve Banks. Holdings should be subdivided and reported as described in paragraph 20.04.

21.25 Custodies Held for Foreign Correspondents (Definitive and Book Entry)

All safekeeping items for foreign central banks, foreign governments, and other foreign official entities (including foreign entities whose accounts were established under Regulation N) are reported by the FRBNY only, according to the following captions:

- Acceptances
- Securities
- Earmarked gold–Held in own vaults

21.28 Foreign Debt Collateral (Definitive and Book Entry)

Includes collateral held by the Reserve Bank as collateral agent, as well as trust receipts representing collateral held by other custodians, in accordance with various Foreign Debt agreements. Collateral denominated in foreign currencies should be converted to dollars upon receipt; no further revaluation for fluctuations in exchange rates is necessary. Holdings should be subdivided as shown. This account should be reported by the FRBNY only.

- Held in own vaults
- Held by others

21.30 Custodies Held for International Organizations (Definitive and Book Entry)

All safekeeping items, including securities and gold, held for international organizations, such as Asian Development Bank, International Bank for Reconstruction and Development, International Finance Corporation, and International Monetary Fund are reported by the FRBNY only.

21.40 Miscellaneous Custody Items (Definitive and Book Entry)

This account includes ordinary safekeeping other than such safekeeping referenced earlier in this chapter. It also includes any collateral from dealers held by a Reserve Bank in connection with loans of securities from the SOMA and prepaid postage provided by others for use in the provision of services such as RDS postage provided by Treasury.

21.50 Collateral and Custody Items in Process (Definitive and Book Entry)

This account includes the total accountability for definitive and book-entry securities that are being held pending ultimate disposition. Report the par value of all securities for which processing or delivery has not been completed. For example: Treasury securities erroneously submitted to the Reserve Bank and awaiting return to the customer for forwarding to Treasury; book-entries held pending transfer to Treasury on original issue or release of registered securities; municipal or corporate securities held pending deposit to or delivery from safekeeping; unopened “said-to-contain” envelopes for noncash items; and outgoing security and coupon shipments held by registered mail personnel. Savings bonds received for redemption, exchange, or reissue and paid savings stamps should not be reported.

21.55 Memorandum Accounts (Definitive Only)

Typically, the Reserve Banks do not hold items in definitive form. Please notify the Board of Governors if there is any to report.

3 Property and Equipment

Contents

30.01 General

This chapter discusses property and equipment accounts. These accounts consist of the four accounts listed in the Bank Premises section of the FR 34 balance sheet, the Furniture and Equipment account and its related allowance for depreciation account, and the Other Real Estate account listed in the Other Assets section of the FR 34. This chapter also gives instructions concerning leasehold improvements and software which are discussed in Deferred Charges (see also paragraph 4.20).

Property and equipment, also referred to as fixed assets, are used in the production and distribution of services by all Federal Reserve Banks. Fixed assets have three primary characteristics:

1. Acquired and held for use in operations (i.e., not held for sale).
2. Long-term in nature (greater than one year).
3. Possess physical substance.

Generally accepted accounting principles (GAAP) generally requires fixed assets to be recorded at their cost, including all normal expenditures to bring the asset to a location and condition for its intended use.

Full acquisition cost for fixed assets (except software—see appendix D) includes all expenditures necessary to bring the asset to a location and condition in which it is usable for the purpose intended. Acquisition cost includes the following:

- installation costs
- assembly
- freight
- warehousing
- insurance
- taxes

Full acquisition cost should also include trade-in allowances (i.e., the amount capitalized when an asset is traded-in for a new asset should equal the cash outlay for the new asset plus the lesser of (1) the net book value of the asset traded-in or (2) the allowance provided for the trade-in. Further information on trade-ins is found in paragraph 30.90).

The capitalized cost of equipment should include installation and/or integration costs incurred. This may include consultant expense (including associated travel) for contractors and/or internal salary, benefits, and travel expenses incurred by staff who are directly involved with the installation project; and the initial programming and software as part of the integration cost, if the programming and/or software is an integral part of the equipment and the equipment cannot function without it.

Internal use computer software with an acquisition cost of $100,000 or greater should be capitalized as a deferred charge. (See paragraph 4.20 for further information.)

The capitalized cost of an asset is written off periodically, or depreciated, in a manner that is systematic and rational after consideration of any salvage values (see paragraph 30.75). Allocating the cost of a long-lived asset over the accounting periods which the asset is used matches its cost with revenue generated throughout its useful life. The Federal Reserve System uses the straight-line method for depreciating fixed assets.

In general, assets should be capitalized using the individual asset method, which is based on the individual asset unit. Asset units should be readily identifiable (subject to verification of existence without disassembly) and provide economic benefit through distinct, substantive functionality. Thus, in some instances, an asset may be an integrated unit made up of components that individually do not provide functionality without connection to the other components.

Prior to 2021 an alternate method of capitalization, the pooled method, was used when capitalizing furniture, furnishings, and fixtures. Beginning in 2021, furniture, furnishings, and fixtures will have a capitalization threshold applied to the individual asset level. The pooled method may still be used to capitalize a bulk purchase of low-cost furniture or equipment (depreciation should begin once the assets are put into service), at the Reserve Bank's option, when the RBOPS Financial Accounting Policy and Reporting Section has been notified. The pooled asset method is described in paragraphs 30.47 and 30.55–30.58. All other paragraphs relate to individual asset accounting. The useful lives and capitalization thresholds discussed in the following paragraphs reflect minimum accounting requirements for Reserve Banks. Based on local experience or practice, Reserve Banks may establish policies authorizing shorter useful lives or lower capitalization thresholds. Such policies must be in writing, applied consistently within the District, and provided as information to the RBOPS Financial Accounting Policy and Reporting Section.

30.05 Historical Information

The accounting rules for capitalizing and depreciating property and equipment have remained the same over the years with only minor departures for special circumstances. Prior to 1922, for example, several offices were authorized to charge larger amounts of depreciation against earnings because of inflated construction costs during and after World War I, and in 1922 FRB-Minneapolis was authorized to write off $500,000 to reduce the book value of its quarters to the approximate market value.

In 1995, the Federal Reserve Banks began recognizing impairment losses consistent with FASB ASC Topic 840-30, which was superseded by FASB ASC Topic 360-10, Accounting for the Impairment or Disposal of Long-Lived Assets. Accordingly, write-downs of property and equipment occur periodically as a result of adjusting assets to their estimated fair values. (See paragraph 30.95.)

Prior to 1996, construction costs for improvements or additions to a building were capitalized as part of the original building only if the addition or improvement significantly increased the useful life of the building beyond the current depreciation schedule or added functionality or space, in accordance with GAAP. In practice, ensuring accounting consistency for large improvement projects became burdensome, especially as some buildings approached the end of their initial useful lives. Since 1996, improvements to existing buildings are evaluated, capitalized, and depreciated as separate assets as a practical expedient. Accordingly, underlying asset values are not adjusted for capitalized improvements regardless of when the underlying asset was acquired. Improvement assets and accumulated depreciation, however, are adjusted if replaced or modified by a subsequent capitalized improvement and charged to depreciation expense.

Two fixed asset policy changes were implemented in 2021 to align with standard accounting practices in parallel with the implementation of a new financial system: elimination of pooled accounting for furniture, furnishings, and fixtures; and elimination of the separate Building Machinery and Equipment account. The pooled asset method is described in paragraphs 30.47 and 30.55–30.58. The separate Building Machinery and Equipment (160-075) asset account was used to account for stand-alone or supplemental equipment with a shorter expected life than the building but that would remain as part of a building upon its sale or abandonment by the Reserve Bank. Existing Building Machinery and Equipment assets were moved to Furniture and Equipment, and any new Building Machinery and Equipment type assets will be booked as Furniture and Equipment.

Accounting for Asset Retirement Obligations (FASB ASC Topic 410-20) requires recording an asset and related liability for conditional asset retirement obligations, such as the legal obligation associated with the retirement of long-lived tangible assets. Accounting for Environmental Obligations (FASB ASC 410-30) provides guidance on accounting for environmental remediation liabilities and discusses expense or capitalization treatment. Application of these standards can be complex, and Reserve Bank staff must obtain approval (including for asbestos abatement) from the RBOPS Financial Accounting Policy and Reporting Section prior to making any accounting entries.

30.06 Publication of Property and Equipment Information

Property and equipment information is published weekly, monthly and annually in various publications as described in paragraphs 60.15, 60.20, and 60.35. A detailed table showing costs and net book values, by office, for land and buildings, construction, and other real estate also appears in the Board's *Annual Report*.[1]

30.10 Land

This account includes all expenditures to acquire a site (such as purchase price, closing costs, and attorney/recording fees), and costs to prepare a site for construction (such as the removal of existing structures, draining, filling, and clearing).[2] The account should be debited when property is purchased for immediate Bank use or when a property that was previously carried in Other Real Estate is approved for construction. Land is carried on the Reserve Bank's books at cost and is not depreciated.

If the property includes a building or other structure which is intended to be used for banking purposes, the portion to be charged to Land should be based on the assigned value in the purchase document or, in the absence of such specific information, on the appraised value. When appraised values are used and are different from the purchase price, the cost should be distributed on a pro-rata basis in the same proportion as the value of Land and Building bears to total appraised value. If the purchased property includes a building or other structure, which is to be razed, the entire purchase price should be allocated to this account. The cost of removing such structures should be charged to this account and the proceeds from the sale of salvaged materials should be credited. Incidental costs of demolishing the building (such as liability insurance, measures taken to maintain adjacent property during operation, reinforcement of walls of adjacent buildings, other repairs made for safety, and reconnection or construction of sewers) should also be included in this account.

30.15 Land Improvements

The Land Improvements account is used to record costs incurred for capital land improvements which have limited lives (e.g., sidewalks, fountains, and fences). Land

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1 The Annual Report may be found at www.federalreserve.gov/publications/annual-report/default.htm.

2 Refer to paragraph 30.05 for accounting guidance on environmental remediation costs, which must be approved by the RBOPS Financial Accounting Policy and Reporting Section.

improvements that cost $100,000 or more must be capitalized. The Land Improvements account is reported as a sub-account to Land. The allowance for depreciation for land improvements is reported as a sub-account to the bank premises allowance for depreciation.

The cost of each improvement should be recorded in a subsidiary ledger within the Land Improvements sub-account and depreciated over its own unique estimated useful life. Depreciation is recorded by debiting depreciation expense and crediting Accumulated Depreciation for Land Improvements. The maximum useful life for land improvements is 20 years.

30.20 Building

This account is used to record costs of acquiring or constructing a building to be used by the Bank. The cost of a building should include all expenditures related directly to its acquisition or construction. Generally, all costs incurred, beginning with excavation through completion of construction, are considered part of the building costs. The cost of the building should not include the cost of land, land improvements, or fixed machinery and equipment.

This account should be charged when a building is purchased for immediate Bank use or when the Construction account is closed upon completion of a project. Thereafter, only major alterations, renovations and improvements may be added to the capitalized cost of the building.[3] Building improvements must be capitalized if the cost is $100,000 or more, and if the improvements meet the capitalization criteria defined in paragraph 30.70.

Such major improvements should be recorded and depreciated individually in the Bank's subsidiary records. The account should be credited only when the building or major improvement is sold, demolished, or otherwise retired, such as by transfer to the Other Real Estate account.

Projects such as repairing, painting or refurbishing should be charged to expense unless they meet the capitalization tests for improvements as defined in section 30.70. The maximum useful life of a building is 50 years. Improvements should be assigned unique useful lives, not to exceed 50 years.

30.30 Construction Account

This account is used to accumulate all capitalizable costs relating to a building or renovation project, and is closed out following completion of the project. This account should be charged for all costs of a new building, the purchase price of a building to be held for future use pending renovation, and all renovation and improvement costs. Receipts from the sale for such items as scrap or recoveries of building costs for such items as change orders and insurance should be deducted from the amount of the project to be capitalized.

Upon completion of a given project, amounts that were accumulated in this account should be analyzed and capitalized in accordance with the provisions contained in this chapter. Construction projects should be capitalized in a timely fashion (i.e., when the project is substantially complete) and, if necessary, in portions. Resolution of punch list items and billing disputes should not delay capitalization unless their nature is so

[3] Refer to paragraph 30.05 for accounting for any environmental remediation costs, such as asbestos abatement, because they should be approved by the RBOPS Financial Accounting Policy and Reporting Section.

significant that the asset(s) are rendered virtually unusable until resolution. Reserve Banks may capitalize and depreciate salaries of employees directly engaged in construction projects if they are performing functions that an outside contractor or consultant would be retained to perform if the internal staff were not available or did not have the necessary expertise. Personnel costs associated with management oversight should not be capitalized if they are of an administrative nature. See 30.40 for examples of capitalized items.

As costs are incurred, they should be analyzed for propriety as capital costs related to the project. Expense items should not be carried in this account except as necessary when commingled with other costs. When such expense items are finally determined, they should normally be applied to the current year's expenses. Similarly, costs related to building and construction projects, such as consulting fees and survey costs, that have not been and are not likely to be approved by the Board in the near future should be expensed when incurred, rather than included in this account.

30.40 Examples of Classification of Capitalized Bank Premises Assets

The following are examples of disbursements, which are to be capitalized as land, land improvements, and building. The list is intended to suggest the scope of the Bank Premises accounts and is not exhaustive.

Land

- Amount paid to vendor
- Back taxes (not paid before acquisition)[1]
- Clearing
- Commissions (real estate)
- Cost of options and appraisals
- Demolition
- Earth work
- Internal Revenue stamps
- Legal expenses
- Outdoor landscaping—new building or significant redesign of the land
- Permits
- Recording deed and lease
- Relocation costs (paid to or for tenants requested to vacate)
- Site drainage
- Soil treatment
- Subsurface exploration
- Title examination
- Unexpired leases
- Utility relocations

[1]Amounts paid after acquisition should be expensed.

Land Improvements

- Built-in concrete benches and planters
- Fences and gates
- Flag poles
- Fountains, pools, and monuments
- Irrigation systems
- Environmental remediation[1]
- Other site improvements (retaining walls, stationary bollards)
- Parking lots
- Plazas and patios
- Sidewalks, curbs, pavers, and handrails
- Site lighting

[1]Reserve Banks must consult with the RBOPS Financial Accounting Policy and Reporting Section to determine if capitalization is appropriate.

Building

All permanent and demountable partitions (except freestanding)
Architects and consultants fees (including design development, schematic designs, and construction artifacts)
Book and record vaults
Brick, marble, limestone and granite cut stone work foundation
Builders' risk and other insurance
Built-in fire protection equipment (e.g., sprinkler systems)
Built-in loading dock equipment
Built-in maintenance systems
Built-in shooting range equipment (e.g., stops/traps)
Built-in window treatments (including film)
Built-in window washing equipment
Casework (built-in furniture)
Ceiling and support systems
Cement or metal floors and stairs
Damp proofing and water proofing
Ducts, conduits, cables, wiring and power points not associated with a specific building machinery and equipment
Electrical wiring
Elevator doors
Elevator shafts
Environmental remediation[1]
Excavation
Finished hardware
Fire and storm doors
Floor and roof construction (including structural and raised)
Foundation systems (piles, walls, piers, and footings)
Fuel connections
Hoist
Indoor built-in artwork
Indoor built-in landscaping[2]
Licenses and permits
Lighting fixtures
Mail chutes and conveyors
Mill work and dimension lumber
Moving stairs and walks
Paint—Wall paper and wall graphics
Parking garages/structures
Permanent flooring (including initial installation of carpeting in building)
Plastering
Plumbing
Reinforced concrete work
Rolled steel doors
Sanitation/sewer lines
Sheet metal work
Sky lights
Structural steel work
Temporary construction fencing
Temporary utilities and facilities during construction
Restroom and bath accessories
Vapor barriers and insulation
Vaults including racks and files, doors and day gates
Walls and wall systems (including studs)
Windows

[1]Reserve Banks must consult with the RBOPS Financial Accounting Policy and Reporting Section to determine if capitalization is appropriate.
[2]When landscaping involves the roof of a secure wing and the roof of the space below plaza ground level, these landscape costs should be prorated between building and land improvements.

30.45 Furniture and Equipment

Furniture and equipment includes computing equipment, automotive equipment, furniture, furnishings, and fixtures, operating equipment, and artwork. This account also includes machinery and equipment associated with building structures that are considered part of the building and will convey with the building when it is sold. Examples include air conditioning units, boilers, elevators, and heating or lighting equipment.

30.46 Examples of Classification of Capitalized Furniture and Equipment Assets

The following are examples of expenditures that are to be capitalized as furniture and equipment. The list is intended to suggest the scope of the furniture and equipment accounts, and is not exhaustive.

Furniture and Equipment

Equipment
(if > $10,000 or bulk purchased with notification to RBOPS)
Computing Equipment:
Computers
Desktops, tablets, and laptops
Virtual/Augmented Reality Equipment
Network: routers, switches, wireless equipment
Peripheral equipment
Telecommunication systems
Disc drives
Mass storage units (network attached storage)
Printers, copiers, and fax machines
Scanners
Smartboards
Storage area network
Tape drives / libraries
Security assets, including visual display terminals, and intrusion detection and prevention systems
Public Key Infrastructure identity and authentication systems
Servers
Portable uninterrupted power sources
IT vending machines

Automotive Equipment
Automobiles
Tractors
Trucks

Furniture, Furnishings and Fixtures
(if > $10,000 or bulk purchased with notification to RBOPS)
Furniture: Desks, chairs, credenzas, bookcases, cabinets, tables, files (except operationally dedicated high-density filing systems), lockers, outside patio benches and tables, initial stock of cafeteria tableware and dishes, etc.
Furnishings and Fixtures: Window treatments, attached Sit-To-Stand desks, freestanding partitions and cubicle components (such as shelves, work surfaces, cabinets, and file drawers).

Operating Equipment[2]
Heating and Air Conditioning Equipment:
Boilers
Commissioning (testing of all HVAC equipment)
Compressors and fans
Cooling towers, chillers, water tanks, and hot water heaters
Environmental control consoles
Heating, ventilating, and air handling equipment
Pumps
Electrical and Mechanical Equipment:
Built in Sound Masking System (installed in ceiling)
Dynamos and stationary electric motors
Electrical panels and transformers
Non-portable uninterrupted power sources
Non-portable power-distribution units
Elevators
Pumps
Switchgear and generators
Operating Equipment: Built-in and operationally dedicated material handling and conveying systems; lobby exhibits (A/V, lighting, built-in displays); coin and currency counting and sorting machines; spare sensors; currency shredding equipment; fork lift trucks; electric Car Stations; internal currency and coin transport systems; phone Charging Stations; TV surveillance cameras and monitors; etc.[1]
Building Maintenance Equipment: Vacuum cleaners, waxing machines, sanding machines, portable trash compactors, plumbing snake, etc.
Shop Equipment: Drill presses, lathes, electric saws, etc.
Kitchen and Dining Facilities Equipment: Refrigerators (other than built-in, walk-in refrigerators and freezers), cash registers, microwaves, vending machines, etc.
Medical Services Equipment: Sterilizers, sunlamps, scales, hospital beds, stretchers, etc.
Audio-Visual Equipment: Video equipment, cameras, projectors and screens, sound systems, speakers, portable and integrated videoconferencing equipment, computerized system for shooting range, etc.
Protection Equipment: Biometric devices, access control devices, MAG locks, magnetometers, x-ray machines, bomb detectors, K-9 dogs, etc.
Fitness Center Equipment: Treadmills, ellipticals, exercise bikes, etc.

Artwork
Moveable original works of art created by professional artists, including paintings, outdoor artwork, and graphics. Does not include framed poster art.

Kitchen and Dining Room Equipment
Built-in dishwashers
Built-in hoods and vents
Built-in stoves and ovens
Built-in grilles
Built-in walk-in freezers and refrigerators
Steam tables and serving line equipment
Built-in dispensing equipment
Built-in ice makers
Built-in pizza ovens
Other Equipment:
Cash residue equipment
Parking equipment
Retractable bollards and moveable gates
Surveillance and protection equipment (security Portal, Speed Lanes)

[1] Equipment designated with a maximum 15-year useful life: incinerators, high-density filing systems, high-speed equipment. See 30.78.
[2] Initial installation costs of equipment may be recorded as a building cost if not readily identifiable in construction contracts or invoices. Costs incurred to replace ducts, conduits, cables, wiring, and power points that support specific building, machinery, and equipment should be recorded as installation costs.

30.47 Methods of Capitalization—Furniture and Equipment

Prior to 2021, two accounting methods were followed in capitalizing and depreciating these assets—the "individual asset" method (as is used for all other asset categories) and the "pooled asset" method.

Assets classified as furniture, furnishings, and fixtures were previously capitalized and depreciated using the pooled asset method, as described in paragraph 30.55 below. Beginning in 2021, furniture, furnishings, and fixtures will have a capitalization threshold applied to the individual asset level rather than a pooled method. In addition to purchased furniture, a Reserve Bank may, at its option, capitalize and depreciate salaries and the outside cost of materials that are consumed in the construction of furniture and equipment by Reserve Bank personnel. These costs are capitalized and depreciated using the individual asset method.

Equipment with a cost of $10,000 or more must be capitalized using the individual asset method. Equipment with a purchase cost below $10,000 should be expensed. If equipment costs less than $10,000 for an individual item but significant quantities are acquired, and the total purchase exceeds $100,000, then the purchase may be capitalized and recorded with notification to the RBOPS Financial Accounting Policy and Reporting Section, which has 10 business days to object to the accounting treatment.

The pooled asset method of capitalizing, depreciating, and handling improvements is discussed in paragraphs 30.55–30.58. All other paragraphs in this chapter relate to the individual asset accounting method. Maximum useful lives for furniture and equipment asset groupings under both the individual asset and pooled asset method are found in table 30.78.

30.50 Equipment

Equipment (with the exception of those items that are pooled as a bulk purchase) should be capitalized on an individual item basis and recorded within the appropriate asset account. This account should be charged for the full acquisition cost as described in paragraph 30.01 and care should be taken to ensure asset and liability accounts are properly reflected at the time the asset is received.

30.51 Artwork

Artwork should be capitalized on an individual item basis and under the threshold set forth for equipment. Artwork should be recorded based on the full acquisition cost as described in paragraph 30.01. Non-capitalizable artwork should be expensed and recorded to operating expense (330-050).

30.55 Pooled Asset Method

Prior to 2021, the pooled asset method was used to account for furniture, furnishings, and fixtures. Pooling allowed small dollar/large quantity assets to be appropriately reflected on the financial statements without imposing the unnecessary tracking of each asset individually as a practical expedient. Under the pooled asset accounting concept, no individual item had a recorded and separately identifiable book value. Rather, it was the group (pool) account that carries a book value. Accordingly, as was noted from the following instructions, once a pool account had been established, the amount in the pool account remains unchanged for as long as the pool account remains in existence (until it is fully depreciated). Any furniture, furnishings, and fixtures purchased in 2021 will use the individual asset method of capitalization.

All purchases handled under the pooled asset method were to be capitalized into pooled accounts at full acquisition cost, including, where applicable, such items as outside installation costs, furniture assembly, freight charges, warehousing, insurance, and taxes. Each calendar year was considered as a separate pool and all purchases made within a given calendar year were considered a part of that pool account. The change from pooled accounting will be applied prospectively, only.

If a Reserve Bank capitalizes a particular bulk purchase of low-cost equipment based on paragraph 30.01, that purchase will still be handled similarly to previously pooled assets, in that the items will not be individually tracked or have separately identifiable book values but depreciation should begin once the assets are put into service.

30.56 Pooled Asset Depreciation

For 2020 and prior-year pooled assets, depreciation will be calculated monthly on the gross amount of each pool account, using the “straight-line method.” Depreciation on each furniture pool account will begin in the first month following the end of the pool year (calendar year). Guidelines on useful lives of pooled assets are found in table 30.78. Depreciation will continue until the allowance for depreciation equals the amount of the pool account, at which time the pool account will be credited and the related allowance for depreciation will be debited for the amount of the pool account (effectively removing these accounts from the balance sheet).

30.57 Pooled Improvements (or Betterments)

For 2020 and prior-year pooled improvements, the costs paid to an outside vendor for significant improvements or betterments made to furniture, furnishings, and fixtures was capitalized. When such expenditures were made, the amount was added or capitalized in the appropriate pooled asset account for the year in which the expenditures were made. Such capitalized improvement or betterment costs was treated as a purchase made during the year and were depreciated, along with the other purchased assets in the pool, over the life of that particular pool account.

30.58 Disposals and Trade-ins of Pooled Asset Items

The following is the treatment to be used when any item carried in a legacy pooled asset account: (a) is sold—the salvage received from the sale should be credited against the appropriate pool; (b) is traded in—the new item (for which the pooled item was traded) should be expensed at the net purchase price, unless the asset meets the capitalization thresholds for fixed assets; (c) is lost, stolen, or disposed, with no salvage or trade-in value received—no entries are necessary for accounting and reporting purposes.

30.70 Expenditures for Existing Buildings and Equipment

Expenditures for existing buildings and equipment consist of the cost of additions, improvements, and major replacements to an asset (see descriptions below). These expenditures should be analyzed to determine if they should be capitalized or charged to expense in the current accounting period. Generally, expenditures for existing assets that meet the capitalization threshold of the Reserve Bank for similar assets are considered capitalizable if at least one of the following criteria is met:

1. The useful life of the existing asset is increased by more than one year.
2. The quantity of output or operating efficiency of the asset is significantly increased.
3. The quality of output is significantly increased.

The cost incurred for any asset that does not meet the criteria described above or the capitalization threshold for similar assets should be expensed in the period incurred. Repairs and maintenance costs incurred to maintain an asset at its current level of operation are not capitalizable and should be charged to expense.

Additions:

Additions are the increases to, or extensions of an existing building or equipment. Additions that meet one or more of the criteria described above should be recorded in a separate subsidiary account of the Buildings or Equipment account and generally depreciated over the remaining life of the principal asset. If the addition is considered to have an independent service life of its own, depreciation is recognized over the service life of the addition.

Improvements:

Improvements (or betterments) represent major modifications of an existing asset such as major renovations to an existing building or overhaul to equipment that will significantly increase its efficiency, its useful life, or the quality of the asset. Demolition costs resulting from the improvements of internal structures such as walls or flooring are also considered part of the improvement.

Improvements made to buildings or equipment that meet one or more of the criteria described above should be recorded separately in the appropriate subsidiary account. The depreciation rate for the improved asset should be recalculated based on the new useful life, net book value, and salvage value of the improved asset. If the improvement is made to a building and is considered to have an independent useful life, depreciation is recognized over the service life of the improvement. The revised depreciation charges should begin in the first month following final payment or when the asset is placed in service, whichever occurs first.

Specialized improvements are separately identifiable building improvements or renovations that usually have a distinct useful life and may not meet the improvement criteria above, but are significant changes to the original asset.[4] For specialized improvements, any remaining costs of the original improved or replaced asset cannot be separately identified from the cost of the original building asset; therefore, it cannot be written-off or the useful life cannot be accelerated. Any loss associated with the impairment of a specialized improvement is charged to expense.

When conducting floor renovations, Reserve Banks should look to their historical renovation trends to determine if the renovation should be capitalized and given a distinct useful life. For example, if the Reserve Bank has a history of renovating floors every ten years, a useful life of ten years would most likely be assigned to a current renovation. However, if floor renovations are rare, or no particular trend emerges in the

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[4] FAM was revised in 1996 to allow for specialized improvements.

frequency of the renovation, a Reserve Bank may consider assigning the remaining useful life of the building as the useful life of its current renovation. Improvements that replace assets with a separately distinguishable book value should be treated as a replacement (see replacement requirements below). See paragraphs 30.85–30.87 for the appropriate treatment of leasehold and tenant improvements.

The accounting for costs associated with improvements made to computer equipment should be capitalized if the improvement meets the $10,000 capitalization threshold of individual assets and the improvements are tangible. To illustrate, assume that a two-year old computer is initially purchased for $l,000,000 and the expected useful life is set at six years. At the end of four years, an improvement is made for $300,000 which is considered tangible and is expected to extend the useful life two years beyond the original useful life period (four years from the time of the improvement) and increase the salvage value $30,000. Initially, the computer was being depreciated at $150,000 per year to a salvage value of $100,000. After the improvement, it would be depreciated at $142,500 per year to a salvage value of $130,000. An equipment improvement that can function independent of the underlying asset (for example, a storage array added to a server that can be moved to another server if needed) should be capitalized as a separate asset with a unique useful life. If the improvement cannot function independent of the underlying asset, the costs associated with the improvement should be depreciated over the remaining useful life of the original underlying asset.

Replacements:

A replacement is a substitution of an existing asset by a new asset. Replacements should be capitalized if they meet one of the criteria discussed above. Replacements should be accounted for under the substitution approach which requires removing the cost of the existing asset and its accumulated depreciation from the books and charging current expense for the difference. The new asset should be depreciated over its own useful life.

30.71 Capitalization Thresholds

For an outlay to be capitalized, it should be material in value. For purposes of recognizing long-term physical assets, materiality is defined as equal to or greater than established capitalization thresholds. Table 30.72 provides the capitalization thresholds for the types of assets described in this chapter. The thresholds stated in the table represent the lower limit above which these transactions must be capitalized. A Reserve Bank has the option to implement more stringent (lower) thresholds if it deems such a policy preferable. If a more stringent threshold is used, the Reserve Bank must consistently apply the threshold throughout the District (i.e., the head office and Branches must all use the same capitalization thresholds for all asset classes.) Such policy must be documented and provided as information to the RBOPS Financial Accounting Policy and Reporting Section.

30.72 Capitalization Thresholds Table

Capitalization Thresholds	
Asset Classification	Capitalization Thresholds (Individual Assets)
Land	All acquisitions
Land Improvements	$100,000
Building and Improvements	$100,000
Equipment, Artwork, and Improvements	$ 10,000
Furniture, Furnishings, and Fixtures	$ 10,000
Externally Purchased Software	$ 25,000
Internally Developed or Significantly Modified Software	$100,000
Implementation Costs for Cloud Computing Arrangement that does not contain a software license	$100,000
Leasehold Improvements	$ 25,000
Tenant Improvements	$ 25,000

30.75 Depreciation

Depreciation is defined as the accounting process of allocating the cost of tangible assets to current expense in a systematic and rational manner in those periods expected to benefit from the use of the asset. Depreciation is an occupancy or usage cost and therefore, should begin the month following the date equipment is placed into production. When constructing a building, if it is occupied prior to closing the Construction account, depreciation should be estimated as closely as possible and applied to current expense effective in the month following when at least 50 percent of the Reserve Bank's staff is operating from the new quarters. Any adjustments for over or under estimates of depreciation, as may be determined when the Construction account is closed and final figures for Building and Equipment are capitalized, should be adjusted to current expense in the current month.

For all fixed assets (except software) reported on the balance sheet, depreciation starts the month following when the fixed asset is placed into service. Depreciation is recorded by debiting current expense and crediting the related allowance for depreciation on the balance sheet. Thus, the amount of accumulated depreciation reported on the balance sheet represents the sum of the individual depreciation charges for each asset that have been recorded in the subsidiary accounts of the Bank.

Assets are depreciated on a straight-line basis. The depreciable basis of an asset is its acquisition cost less its estimated salvage value. The formula for calculating the straight-line method of depreciation is as follows:

Cost less Salvage Value/Estimated Useful Life (in months) = Monthly Depreciation Charge

Depreciation should continue until the asset is fully depreciated or disposed. At the end of an asset's estimated useful life, the asset's net book value should equal its salvage value and depreciation should be discontinued. Depreciation on impaired assets should continue until the Reserve Bank ceases the operations for which the asset is used. Assets that are held for sale are reclassified to other real estate and depreciation ceases. The asset and related allowance for depreciation should not be removed from the balance sheet until the asset is retired or disposed, even if the net book value of the asset is zero. (See paragraph 30.95.)

Appropriate subsidiary records, reflecting the original acquisition cost, the cost of any improvements, and allowance for depreciation balance should be maintained in all cases. Land, artwork, and assets held for sale or future use are not depreciated.

30.76 Depreciation Rate and Salvage Value

Table 30.78 provides information for establishing useful lives and salvage values for the types of assets described within this chapter. Similar assets, within an asset category, that have the same useful lives may be grouped for depreciation purposes, as long as memorandum records are maintained detailing the original charges to the account by piece of equipment. It should be noted that Table 30.78 provides parameters within which the Reserve Bank may determine the appropriate depreciation schedule for assets. It should not be viewed as an indication of rates that are automatically to be assigned to new or used equipment. If a Reserve Bank has a special case where the documented useful life or salvage value of an asset exceeds the guidelines set forth, a request, with substantiating documentation, should be sent to the Manager of the RBOPS Financial Accounting Policy and Reporting Section for review and approval. A Reserve Bank may utilize a lesser useful life or salvage value than the guidelines listed without Board notification with the exception of the bank building (excluding improvements).

The depreciation rate should be based on the expected unique useful life to the Reserve Bank, taking into account such factors as probable technological obsolescence and projected capacity limitations consistent with the Bank's long-range procurement plans, industry information, and improvements. The salvage value assigned to an asset should reflect the Reserve Bank's expected recovery upon sale or trade-in of the asset. Assessments of the useful life and salvage value of all assets, excluding building but including Building Improvements and Equipment should be reviewed annually, at a minimum. Should the Reserve Bank note a change in the expected remaining useful life or salvage value of the asset, the depreciation rate should be adjusted prospectively such that the remaining net book value is depreciated to the estimated salvage value over the expected remaining useful life of the asset.

30.78 Maximum Useful Lives and Salvage Values Table

Maximum Useful Lives and Salvage Values

Asset Classification	Maximum Estimated Useful Life [1]	Maximum Estimated Salvage Value
Land Improvements	20 years	0
Building	50 years	0
Improvements	Unique life or remaining life of building	
Equipment:		
Computing equipment (other than PCs)	As determined by Reserve Bank (see 30.76)	(See paragraph 30.76)
Operating equipment	6 years	10 percent
PCs	3 years for standard technology; 4 years for state-of-the-art technology	0
Automotive Equipment (including vans & minivans)	5 years	20 percent
Furniture, Furnishings, and Fixtures	10 years	0
Software	5 years	0
Implementation Costs for Cloud Computing Arrangement that does not contain a software license	Non-cancellable term of the hosting arrangement and any optional renewal periods reasonably certain to be exercised	0
Leasehold and Tenant Improvements	Shorter of the non-cancelable lease term or unique useful life of the asset	0

[1] The Division of Reserve Bank Operations and Payment Systems has assigned specific maximum estimated useful lives to the following assets:

- Ten (10) year useful life, zero salvage value (1) Unisys check processing equipment and (2) currency storage containers.
- Fifteen (15) year useful life: (1) High speed currency equipment, currency disintegrators and incinerators, and high density filing systems. (2) Offset printing presses, and (3) automated guided vehicles.
- Twenty (20) year estimated useful life: (1) Uninterruptable power systems. (2) Materials handling systems. (3) Building Machinery and Equipment type assets.
- Twenty five (25) year estimated useful life: Solar water heat.
- Forty (40) year estimated useful life: Solar vent preheat.

Note: Peripheral equipment that is expected to have the same useful life as a mainframe computer should be depreciated over the life of the mainframe. However, if the useful life of such equipment is projected to be different from that of the computer, the equipment may be depreciated over a different period provided the equipment is not dedicated to, or an integral part of, the mainframe.

30.80 Leases

A lease is defined as an agreement conveying the right to use property, plant, or equipment (land and/or depreciable assets) usually for a stated period of time. A contract is or contains a lease if the contract conveys the right to control the use of identified property, plant, or equipment ("identified asset") for a period of time in exchange for consideration. To determine whether a contract conveys the right to control the use of an identified asset for a period of time, the Reserve Bank needs to assess whether, throughout the period of use, the Reserve Bank has both the right to obtain substantially all of the economic benefits from use of the identified asset and the right to direct the use of the identified asset.

Leases will be classified at the commencement date of the lease (i.e., the date on which a lessor makes an underlying asset available for use by a lessee).

Classification:

A Reserve Bank lessee classifies a lease as a finance lease and a Reserve Bank lessor classifies a lease as a sales-type lease if the lease meets any one of the following criteria:

1. The lease transfers ownership of the underlying asset to the lessee by the end of the lease term.
2. The lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise.
3. The lease term is 75 percent or more of the remaining economic life of the underlying asset. *This criterion is not applicable for leases that commence within 25 percent or less of the underlying asset's economic life*.
4. The present value of the sum of the lease payments and any residual value guaranteed by the lessee that is not already included in the lease payments equal or exceed 90 percent of the fair value of the underlying asset.[5]
5. The underlying asset is of such a specialized nature that it is expected to have no alternative use to the lessor at the end of the lease term.

When none of the criteria noted above are met:

1. A Reserve Bank lessee shall classify the lease as an operating lease.
2. A Reserve Bank lessor shall classify the lease as either a direct financing lease or an operating lease.

A Reserve Bank lessor shall classify a lease as an operating lease unless both of the following criteria are met, in which case the Reserve Bank lessor shall classify the lease as a direct financing lease:

1. The present value of the sum of the lease payments and any residual value guaranteed by the lessee and/or by any other third party unrelated to the Reserve Bank lessor that is not already reflected in the lease payments equals or exceeds substantially all of the fair value of the underlying asset.[6]
2. It is probable that the Reserve Bank lessor will collect the lease payments plus any amount necessary to satisfy a residual value guarantee.

Lease Term

A Reserve Bank shall determine the lease term for any lease classification as the non-cancellable period of the lease including optional periods to extend the lease if the

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[5] For lessees, the discount rate used to evaluate the "substantially all" criterion is a risk-free discount rate (i.e., Treasury borrowing rate) determined using a period comparable with that of the lease term.

[6] A guarantee made to a lessor that the value of an underlying asset returned to the lessor at the end of a lease will be at least a specified amount.

lessee is reasonably certain to exercise; termination options that the lessee is reasonably certain not to exercise; and extension or termination options controlled by the lessor.

At the commencement date, a Reserve Bank shall include the periods listed above in the lease term having considered all relevant factors that create an economic incentive for the lessee (that is, contract-based, asset-based, entity-based, and market-based factors).[7]

Lease Payments

A Reserve Bank shall determine lease payments for any lease classification as consisting of the following payments relating to the use of the underlying asset during the lease term determined as noted above:

1. Fixed payments, including in substance fixed payments, less any lease incentives paid or payable to the lessee.
2. Variable lease payments that depend on an index or a rate (such as the consumer price index or a market interest rate), initially measured using the index or rate at the commencement date.
3. The exercise price of an option to purchase the underlying asset if the lessee is reasonably certain to exercise that option.
4. Payments for penalties for terminating the lease if the lease term reflects the lessee exercising an option to terminate the lease.
5. Fees paid by the lessee to the owners of a special-purpose entity for structuring the transaction.
6. For a Reserve Bank lessee only, amounts probable of being owed under residual value guarantees.

Lease payments do not include variable lease payments other than those noted above, any guarantee by the lessee of the lessor's debt, and amounts allocated to nonlease components.

Reserve Bank Lessee Accounting

Initial Measurement of All Leases

At the commencement date of a lease, a Reserve Bank lessee shall measure for any lease classification both a lease liability computed as the present value of the lease payments not yet paid, discounted using the discount rate for the lease at lease commencement and a right-of-use asset. The Reserve Bank lessees shall use a risk-free discount rate (i.e., Treasury borrowing rate) determined using a period comparable with that of the lease term. However, if the interest rate implicit in the lease, as computed by the lessor, is readily determinable, such interest rate should be used as the risk-free discount rate.

The measurement cost of the right-of-use asset shall consist of the amount of the initial measurement of the lease liability, any lease payments made to the lessor at or

[7] Those factors shall be considered together, and the existence of any one factor does not necessarily signify that a lessee is reasonably certain to exercise or not to exercise an option.

before the commencement date, and any initial direct costs incurred by the Reserve Bank lessee minus any lease incentives received.[8]

A materiality threshold has been established for the balance sheet recognition of lessee leases: the materiality test for a finance lease is that each identified leased asset value equals or exceeds $100,000; the materiality test for an operating lease is that lease payments over the lease term for each operating lease item equals or exceeds $100,000. Potential finance leases with lease payments over the lease term in excess of $500,000 along with the proposed accounting treatment should be sent to the RBOPS Financial Accounting Policy and Reporting Section for review.

Remeasurement of the Lease Liability

Any changes to lease payments after the commencement date including incentive payments for tenant allowances shall be reflected by the Reserve Bank lessee as a remeasurement of the lease liability through an adjustment to the right-of-use asset. However, if the carrying amount of the right-of-use asset is reduced to zero, any remaining amount of the remeasurement is recognized in the Statement of Operations. The Reserve Bank lessee shall update the discount rate for the lease at the date of remeasurement on the basis of the remaining lease term and the remaining lease payments.

The discount rate will not be required to be updated unless the remeasurement of the lease liability is the result of one of the following:

1. A change in the lease term or the assessment of whether the Reserve Bank lessee will exercise an option to purchase the underlying asset and the discount rate for the lease already reflects that the Reserve Bank lessee has an option to extend or terminate the lease or to purchase the underlying asset.
2. A change in amounts probable of being owed by the Reserve Bank lessee under a residual value guarantee.
3. A change in the lease payments resulting from the resolution of a contingency upon which some or all of the variable lease payments that will be paid over the remainder of the lease term are based.

Short-Term Leases

A short-term lease is defined as "*A lease that, at the commencement date, has a lease term of 12 months or less and does not include an option to purchase the underlying asset that the lessee is reasonably certain to exercise.*" A Reserve Bank lessee will not apply the balance sheet recognition requirements to short-term leases meeting this definition. Instead, a Reserve Bank lessee will recognize the lease payments in the Statement of Operations on a straight-line basis over the lease term and variable lease payments in the period in which the obligation for those payments is incurred. If the lease term or the assessment of a Reserve Bank lessee option to purchase the underlying asset changes such that, after the change, the remaining lease term extends more than 12 months from the end of the previously determined lease term or the Reserve Bank lessee is reasonably certain to exercise its option to purchase the underlying asset, the lease no longer meets the definition of a short-term lease and

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[8] Initial direct costs are the incremental costs of a lease that would not have been incurred if the lease had not been obtained. These include broker commissions and payments made to an existing tenant to incentivize that tenant to terminate its lease.

the Reserve Bank lessee shall apply the lease accounting guidance in this section of FAM as if the date of the change in circumstances is the commencement date.

Subsequent Measurement and Recognition for Finance Leases

After the commencement date for a finance lease, the Reserve Bank lessee shall measure the lease liability by increasing the carrying amount to reflect interest on the lease liability and reducing the carrying amount to reflect the lease payments made during the period. The Reserve Bank lessee shall determine the interest on the lease liability in each period during the lease term as the amount that produces a constant periodic discount rate on the remaining balance of the liability, taking into consideration any reassessment requirements. The Reserve Bank lessee shall measure the right-of-use asset at cost less any accumulated amortization and any accumulated impairment losses, taking into consideration any reassessment requirements.

After the commencement date, the Reserve Bank lessee shall recognize in the Statement of Operations the amortization of the right-of-use asset and interest on the lease liability, variable lease payments not included in the lease liability in the period in which the obligation for those payments is incurred, and any impairment of the right-of-use asset.

Subsequent Measurement and Recognition for Operating Leases

After the commencement date, for an operating lease, a Reserve Bank lessee shall measure the lease liability at the present value of the lease payments not yet paid discounted using the discount rate for the lease established at the commencement date (unless the rate has been updated due to a required remeasurement after the commencement date in which case that updated rate shall be used). The Reserve Bank lessee shall measure the right-of-use asset at the amount of the lease liability, adjusted for prepaid or accrued lease payments, remaining balance of any lease incentives received, which is the amount of the gross lease incentives received net of amounts recognized previously as part of the single lease cost, unamortized initial direct costs, and impairment of the right-of-use asset.

After the commencement date, the Reserve Bank lessee shall recognize in the Statement of Operations a single lease cost, calculated so that the remaining cost of the lease is amortized over the remaining lease term on a straight-line basis, variable lease payments not included in the lease liability in the period in which the obligation for those payments is incurred, and any impairment of the right-of-use asset.

Amortization and Impairment of the Right-of-Use Asset

A Reserve Bank lessee shall amortize the right-of-use asset from the commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term on a straight-line basis. If the lease transfers ownership of the underlying asset to the Reserve Bank lessee or the Reserve Bank lessee is reasonably certain to exercise an option to purchase the underlying asset, the Reserve Bank lessee shall amortize the right-of-use asset to the end of the useful life of the underlying asset. When the lease liability is remeasured and the right-of-use asset is adjusted, amortization of the right-of-use asset shall be adjusted prospectively from the date of remeasurement.

If a right-of-use asset is impaired, it shall be measured at its carrying amount immediately after the impairment less any accumulated amortization. A Reserve Bank lessee shall amortize the right-of-use asset from the date of the impairment to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. Due to the complexity of this impairment, Reserve Banks should contact RBOPS Financial Accounting Policy and Reporting Section for guidance.

Lease Termination

A termination of a lease before the expiration of the lease term shall be accounted for by the Reserve Bank lessee by removing the right-of-use asset and the lease liability, with net result recognized in the Statement of Operations for the difference.

Reserve Bank Lessor Accounting

Operating Lease

At the commencement date, a Reserve Bank lessor shall defer initial direct costs and recognize those as an expense over the non-cancelable lease term.[9] After the commencement date, a Reserve Bank lessor shall recognize (unless collectability is not probable) lease payments as rental income over the non-cancelable lease term on a straight-line basis. Lease incentives, including tenant allowances granted to the lessee in cash or rent credits, that are reasonably estimable through contractual terms and probable for future payment or credit should be recorded in a deferred charge account on the lease commencement date and recognized ratably over the remaining lease term as a reduction of rental income. Variable lease payments shall be recognized as rental income in the period in which the changes in facts and circumstances on which the variable lease payments are based occur.

30.85 Leasehold Improvements

Major expenditures made in connection with the renovation or alteration of a space rented for Bank use should be capitalized in Deferred Charges (see paragraph 4.20). A leasehold improvement must be capitalized if the cost is $25,000 or more. The cost of minor repairs and maintenance involved in the upkeep of leased quarters should be charged to current expense. The term “renovations and alterations” as used here is intended to include the construction of any new building for Bank use on leased property where the title to the building passes to the owner of the land either upon completion of construction or termination of the lease agreement.

30.86 Amortization of Leasehold Improvements

Leasehold improvements should be amortized to current expense as rent over the shorter of the non-cancelable lease term as noted in paragraph 30.80 or the unique useful life of the asset, unless the lease transfers ownership of the underlying asset to the Reserve Bank lessee or the Reserve Bank lessee is reasonably certain to exercise an option to purchase the underlying asset, in which case, the Reserve Bank lessee shall amortize the leasehold improvements to the end of their useful life.

30.87 Tenant Improvements

For payments made to tenants for them to build out improvements in leased Bank premises, Reserve Banks should carefully evaluate the terms and conditions of the

[9] Initial direct costs are the incremental costs of a lease that would not have been incurred if the lease had not been obtained. These include broker commissions and payments made to an existing tenant to incentivize that tenant to terminate its lease.

lease contract to assess which entity has control over the improvements i.e. the ability to direct the use of and obtain substantially all the remaining benefits from the improvements during the term of the lease agreement. Reserve Banks should also evaluate if a modification to lease agreements was required in order for the tenant to build out the improvement. A modification could indicate that the asset is owned by the Reserve Bank. All factors including full ownership (i.e. no partially owned assets unless there is an agreement for joint ownership) of the improvements during the lease term should be evaluated. If determined that the Reserve Bank does not have control over the improvements over the term of the lease agreement, associated payments to tenants would be recorded as a lease incentive.

Payments for improvements considered to be owned by the Reserve Bank over the term of the lease agreement should be capitalized as tenant improvements. These should be accumulated in a subsidiary construction account until completion of the project and capitalized in one or more subsidiary accounts under the appropriate Bank premises asset. A tenant improvement must be capitalized if the cost is $25,000 or more and amortized to current expense as depreciation over the shorter of the non-cancelable lease term or the unique useful life of the asset. In the event that a tenant leaves before the expiration of the lease, any remaining unamortized amount should be charged to current expense as a loss on disposal of fixed assets. Should a Reserve Bank need further accounting guidance in evaluating payment to tenants for improvements, Reserve Banks should contact the RBOPS Financial Accounting Policy and Reporting Section.

30.90 Disposals and Trade-ins

When disposing of assets (either voluntarily or involuntarily) the gross asset value and the related accumulated depreciation should be deducted from the appropriate asset account and from the allowance for depreciation account. Any difference between the net book value (gross asset value less accumulated depreciation) and the proceeds from a sale should be debited or credited to current expense. When an asset is traded in, if the net book value exceeds the trade-in allowance, that difference should be debited to current expense (i.e., the amount capitalized when an asset is traded in for a new asset should equal the cash outlay for the new asset plus the lesser of (1) the net book value of the asset traded-in, or (2) the allowance provided for the trade in). In the event equipment is sold by one Reserve Bank to another, any net difference between book value and selling price should be recorded as an increase or decrease to current expense on the books of the selling office. Any transfer of assets between offices of the same District should be made at book value. The receiving office should record the asset on a cost basis equal to the net book value. Disposals are not necessarily write-downs or impairments, which must be approved by the RBOPS Financial Accounting Policy and Reporting Section, as detailed in paragraph 30.95. In contrast, disposals do not require RBOPS approval as they are typically undertaken during the ordinary course of business. Asset disposal requires that the asset be removed from the balance sheet. Disposal indicates that the asset will yield no further benefits. Depending on the value of the asset, a gain or loss may need to be recorded for the reporting period during which the asset is disposed. Please consult with RBOPS Financial Accounting Policy and Reporting Section if you have any questions determining the nature of a disposal.

30.95 Asset Impairment

ASC 360 defines impairment as the condition that exists when the carrying amount of a long-lived asset (asset group) exceeds its fair value. Contrary to disposals or trade-ins of assets that are typically undertaken in the normal course of business, impairments may arise whenever events or changes in circumstances indicate that the carrying amount of the long-lived asset (group) might not be recoverable. At the time an asset is judged to be materially and permanently impaired (whether partial or total), a loss should be recognized in accordance with FASB ASC Topic 360-10. As a general rule, the loss associated with the impairment of land and building (in-service date ending 1995) should be charged to Profit & Loss. The loss associated with impairments of land improvements, building improvements (in-service date beginning 1996), and furniture and equipment should be charged to Current Expense.[10] The offset should be recognized by reducing the book value of the asset through a credit to the asset account if the asset is held for use. The reduction in book value for impaired assets held for disposal should be credited to the corresponding asset account. The asset account may be adjusted for subsequent revisions in estimates of fair value less costs to sell, provided that the carrying amount of the asset does not exceed its original carrying value (prior to any impairment recognition). Regardless of the outcome of the impairment analysis, the useful life and salvage value of the asset should be evaluated and adjusted in accordance with FAM 30.75 and 30.76.

In contrast to asset disposals, all assets that have been determined to be impaired, whether in-service or work-in-process, must be approved by the RBOPS Financial Accounting Policy and Reporting Section. Information such as the description of the asset, whether the asset will be written down or written-off, the reason for the impairment, and the proposed entries to account for the asset impairment should be provided along with the request for approval. The fair value of assets considered for impairment should be determined in accordance with FASB ASC Topic 820-10, Fair Value Measurements.[11] A fair value measurement assumes that an asset is exchanged in an orderly transaction between market participants, and assumes the highest and best use of the asset. In determining the amount of an impairment, the fair value is not to be reduced for transaction costs such as incremental direct costs to sell the asset.

Asset Grouping

For purposes of evaluating and recognizing impairment losses, assets should be grouped with other assets at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets.[12] For example, a check only facility to be closed would group all of its equipment into one group. Other likely groupings include: buildings including general improvements, land, specialized improvements (those related to a unique function), and leasehold improvements.[13] In the case of assets (groups) that do not have cash flows that are identifiable as largely independent of the other assets of the Bank, such as head office buildings, those assets should be grouped with all the assets of the Bank.

Is this asset (group) available for sale?

If an asset is held for sale, then it is recorded at its fair value less selling costs and not depreciated (even if it is held and used). There are six conditions that must be met in order to classify an asset as held for sale.

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[10] See paragraph 30.70 for specialized improvement additions.

[11] See paragraph 30.05.

[12] To the extent these assets have an associated liability, such as with a capitalized lease, the liability should also be included.

[13] Software should be included with the applicable equipment. When it is no longer probable that computer software being developed will be completed and placed in service, the asset shall be reported at the lower of the carrying amount or fair value, if any, less costs to sell. The rebuttable presumption is that such uncompleted software has a fair value of zero consistent with FASB ASC Topic 350-40-35-3.

1. Management commits to a plan to sell the asset (group).
2. The asset (group) is available for immediate sale in its current condition.
3. An active program to find a buyer has been initiated.
4. The sale is expected to be completed within one year.
5. The asking price is reasonable in relation to fair value.
6. Actions taken indicate that it is unlikely that the plan to sell will be withdrawn or significantly changed.

Evaluating for Impairments

Whenever major events or changes in operating circumstances indicate that the carrying amount of an asset may not be recoverable, perform an evaluation of the recorded carrying value of the associated asset to determine if a write-down due to impairment is needed.[14] The following tests should be applied when such events or changes in circumstances occur or on an annual basis in the absence of such events or changes to determine if asset impairment is appropriate:

- A significant decrease in the fair value of an asset held for disposal.[15]
- A significant change in the extent or manner in which an asset is used or a significant physical change in an asset.
- A significant adverse change in legal factors or in the business climate that could affect the value of an asset or an adverse action or assessment by a regulator.
- An accumulation of costs significantly in excess of the amount originally expected to acquire or construct an asset where these costs are not anticipated to be recoverable in the future.
- A current period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with an asset used for the purpose of producing revenue.
- A current expectation that it is "more likely than not" that the asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

Does the carrying value (book value) exceed the amount that can be recovered (undiscounted net cash flows)?

This step is focused on whether the current value is recoverable not whether it is impaired. It is possible, for example, that an asset could have a carrying value well in excess of current market prices that still produces enough cash flows to cover its costs. Loss impairments are not recognized in these cases. The undiscounted cash flows include the cash flows throughout the life of the asset (group) including disposal. If, for example, the useful life of the asset is shorter because of changes in the extent of how it will be used, the cash flows should be measured over the shorter life. In the absence of a better source for cash flow information, Reserve Banks should consider the current depreciation costs as a proxy for undiscounted cash flows on assets that

[14] Refer to appendix D for evaluating for software impairments.

[15] This does not include assets that have been in production (and depreciated accordingly) and that will continue to be used for their intended purpose throughout their useful life.

will continue to be used at "pre-impairment" production levels.[16] If the assets will be used in a reduced capacity, a reasonable pro-ration of the current depreciation should be made. In order to balance the costs associated with estimating and evaluating an impairment loss with the benefits, impairments should only be pursued if the carrying value exceeds recovery amount by the following thresholds.[17] For those assets that are grouped, the thresholds apply to the group. These measurements, and those in the remaining steps, should be made as of the date the impairment was probable and estimable.

- Land: $500,000
- Buildings: Larger of $500,000 or $50,000 x the remaining useful life of the building
- Specialized Improvements: $100,000
- Equipment: $50,000
- Software: $50,000

Asset Fair Value and Impairment Loss Based on the Difference between Carrying Value and Fair Value

The fair value of the asset (group) is the amount at which the asset could be bought or sold in a current arms-length transaction. The ideal method for determining fair value is to use the price for the asset if it is traded in an active market. The next best method is to base fair value on the prices for similar assets (appraisal). The remaining method is to use the discounted present value of the expected cash flows for the asset. In general, assumptions and techniques used to determine fair value should be the same that marketplace participants would use if the information is available without undue cost and effort. Otherwise, the Reserve Bank should use its own assumptions. In general, absent reasonable appraisals of market, the undiscounted amount calculated in step three will be used for those assets that will be disposed of within five years. If applied to an asset that will be held for longer than five years such as a building, use the applicable Treasury rate for a security of that duration as of the impairment date. The impairment loss should be recorded as an adjustment to the asset account (proportionately to assets in a group) and a charge to the same account that would have been charged if the asset was sold.

Fair Value

After adjusting the carrying value for an impairment loss, consider adjusting the remaining useful life and salvage value assumptions from the impairment date. Once the adjustment is recorded, subsequent restoration is not permitted. Depreciation should be based on the adjusted values at the impairment date.

Other Costs Associated with Exit Activities

All other exit costs, such as relocating employees and equipment, and costs associated with closing facilities should be recognized in the period the goods or services are received (see FAM 11.56).

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[16] Estimating cash flows for assets, especially those that support non-priced services areas is problematic. The basis for this proxy is the idea that the result of the pricing process is to match cash flows with costs and that the historical depreciation during full cost recovery is a reasonable proxy for the cash flows. If, a Reserve Bank has another, more accurate method, for computing true cash flows from an asset class, that may be used.

[17] By applying the thresholds at this point rather than after calculating the impairment loss that would be recognized, some administrative costs associated with valuing the asset (group) may be avoided.

30.96 Sale or Transfer of Assets to Another Office

If an asset will be transferred to another office in same District, the depreciation continues and the cost to relocate and reinstall the equipment is charged to expense.[18]

If an asset will be sold to another Reserve Bank, the deprecation will cease when production ceases and the sale should be recorded at book-value (no gain or loss).[19] The receiving Reserve Bank should record the asset at the transferring Reserve Bank's book-value, capitalize the installation and transportation costs and begin depreciation when the equipment is placed into production and continue over the asset's remaining useful life.

30.97 Other Real Estate

This account should be debited upon acquisition of real estate to be held for future Bank use or when Bank property is classified as held for sale. All costs associated with the purchase of real estate should be capitalized. Generally, buildings carried in this account should not be depreciated. When the site is approved for construction, Other real estate should be transferred to the appropriate Bank premises accounts (in most cases, Land).

In some cases, other real estate will include buildings with tenants. Income and expenses involved in operating buildings purchased after 1976 should be functioned through current expenses. If the real estate contains a building that will eventually be razed, depreciation should be discontinued upon acquisition.

The carrying amount of other real estate that is held for sale should not exceed its fair value. The carrying value of other real estate held for sale should be evaluated by the end of the calendar year, at a minimum, to determine if adjustments are necessary (see paragraph 30.95). This does not necessarily require an annual formal appraisal; however, valuation methodologies should be consistent.

31.00 Real Estate Reporting Requirements

Paragraph 60.39 provides instructions for the preparation and submission of required accounting reports FR 612 and FR 892.

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[18] Although relocation costs benefit future periods, the accounting principles require such costs to be charged to expense causing a lack of symmetry in treatment between assets transferred inter- and intra-district.

[19] An impairment loss is unlikely in this case as the "undiscounted cash flow" will include the transfer at book value to the other Reserve Bank.

4 System Open Market Account

Contents

40.01 General

The FRBNY has been authorized and directed by the FOMC to execute open-market transactions on behalf of the Reserve Banks. The FRBNY holds the resulting securities and agreements in the SOMA.

U.S. Treasury, federal agency, and GSE debt securities, Federal agency and GSE MBS, investments denominated in foreign currencies and commitments to buy or sell related securities, comprising the SOMA are recorded at amortized cost, on a settlement-date basis. Rather than using the fair value presentation, amortized cost more appropriately reflects the Bank's securities holdings given the System's unique responsibility to conduct monetary policy. Differences between fair value and amortized cost have no direct effect on the quantity of reserves available to the banking system, or on the ability of the Reserve Banks, as the central bank, to meet their financial obligations and responsibilities. Accounting for securities held in the SOMA on a settlement-date basis better reflects the timing of the transaction's effect on the quantity of reserves in the banking system.[1] The cost bases of Treasury securities, GSE debt securities, and foreign government debt instruments are adjusted for amortization of premiums or accretion of discounts on an effective interest method.

Both the domestic and foreign components of the SOMA portfolio may involve transactions that result in gains or losses when holdings are sold prior to maturity. Decisions regarding securities and foreign currency transactions, including their purchase and sale, are motivated by monetary policy and financial stability objectives rather than profit. Accordingly, market values, earnings, and any gains or losses resulting from the sale of such securities and currencies are incidental to the open market operations and do not motivate decisions related to policy or open market activities. The Reserve Banks do not present a statement of cash flows because their liquidity and cash position do not affect their ability to meet their financial obligations and responsibilities. The financial statement footnote disclosures, however, include cash flow information for significant categories of Reserve Bank activities, such as open market operations, lending, and capital expenditures. Profit motivated entities provide a cash flow statement to disclose their ability to generate future cash flows and thus the ability to meet their obligations. This does not represent a risk to the Reserve Banks.

40.10 U.S. Treasury, Federal Agency, and GSE Debt Securities

These securities are held in the SOMA at the FRBNY with premiums and discounts recorded separately and amortized (accreted) using the effective interest method. Earnings are accrued daily to the interest accrued account (see paragraph 40.60) and all realized gains and losses are determined by specific issue based on average cost. These assets and related income and the associated gains and losses are participated to each Reserve Bank based on the Bank's designated share of the domestic SOMA portfolio. (See paragraph 40.70.)

40.13 Federal Agency and GSE MBS

Outright Purchases and Sales

MBS are held in the SOMA portfolio at the FRBNY. Interest income on Federal agency and GSE MBS is accrued using the effective interest method and includes amortization

[1] The annual audited financial statements, however, are adjusted to reflect foreign-exchange contracts that are unsettled at year-end, effectively adopting trade-date accounting for the audited financial statements only.

of premiums, accretion of discounts, and paydown gains or losses. The premiums and discounts related to Federal agency and GSE MBS are amortized over the term of the security to stated maturity, and the amortization of premiums and accretion of discounts are accelerated when principal payments are received. Paydown gains and losses represent the difference between the principal amount paid and the amortized cost basis of the related security.

Earnings are accrued daily to the interest accrued account (see paragraph 40.60) and all realized gains and losses are determined by specific issue based on average cost. These assets, related income, and the associated gains and losses are participated to each Reserve Bank based on the Bank's designated share of the domestic SOMA portfolio. (See paragraph 40.70.)

MBS Commitments

MBS commitments can result from outright purchases or sales of Federal agency and GSE MBS, and from MBS dollar roll and coupon swap transactions. MBS transactions may be executed as specified pools or "to-be-announced" (TBA) transactions. TBA transactions are agreements between a buyer and a seller with regards to type of security, coupon, face value, price, and settlement date; however, the actual pools and characteristics of the underlying mortgage collateral are not known until allocation day. Allocation day is two business days before settlement date. The Securities Industry and Financial Markets Association releases a monthly schedule that indicates specific days that settlement is expected to occur. The FRBNY requires the posting of cash collateral for commitments as part of the risk management practices used to mitigate counter-party risk, and the resulting cash collateral held by the FRBNY is recorded in Federal Agency MBS Related Liabilities account. (See paragraph 11.94.) Interest expense on the margin balance held for TBA exposure is calculated daily and recorded monthly. Counterparties to MBS commitment transactions incur a daily charge when they fail to deliver the securities on settlement date. The fails charge is calculated daily and accrued monthly. The margin expense and fails charge are participated to each Reserve Bank based on the Bank's designated share of the domestic SOMA portfolio on a monthly basis. (See paragraph 40.70.)

Dollar Roll Transactions

A dollar roll is a transaction in which the investor sells or purchases MBS or TBA securities for delivery in the current month and simultaneously contracts to repurchase or resell substantially similar (although not necessarily the same) securities on a specified future date. Transfers of MBS upon settlement of the initial TBA MBS transactions are accounted for as purchases or sales in accordance with FASB ASC Topic 860, *Transfers and Servicing,* and the related outstanding commitments are accounted for on a settlement-date basis.

Coupon Swap Transactions

A coupon swap is a trade with a single counterparty in which the investor agrees to simultaneously sell one TBA or MBS and to buy an equal amount of a different type TBA or MBS with a different coupon. Based on the terms of the coupon swap transactions, transfers of MBS upon settlement of the initial TBA MBS transactions are accounted for as purchases or sales in accordance with ASC 860 and the related outstanding commitments are accounted for on a settlement-date basis.

40.15 Securities Purchased under Agreements to Resell (Repurchase Agreements)

The FRBNY is authorized by the FOMC to acquire U.S. Treasury, Federal agency, and GSE debt securities, as well as Federal agency and GSE MBS, under agreement with a primary dealer to repurchase the securities at an established point in time (securities purchased under agreements to resell). The FRBNY may engage in tri-party purchases of securities under agreements to resell ("tri-party agreements"). In a tri-party arrangement, commercial custodial banks manage the collateral clearing, settlement, pricing, and pledging, and provide cash and securities custodial services for and on behalf of the FRBNY and counterparty. Acceptable collateral under tri-party agreements is determined by the FOMC. The tri-party agreements are accounted for as financing transactions with the associated interest income accrued over the life of the agreements. Repurchase agreements are participated to each Reserve Bank based on the Bank's designated share of the domestic SOMA portfolio. (See paragraph 40.70.)

40.20 Securities Sold under Agreements to Repurchase (Reverse Repurchase Agreements)

Securities sold under agreements to repurchase are treated as secured borrowing transactions with the associated interest expense recognized over the term of the transaction, generally overnight.

The FRBNY is authorized by the FOMC to sell U.S. Treasury, Federal agency, and GSE debt securities, as well as Federal agency and GSE MBS, under agreements to repurchase. The FRBNY is also authorized and directed by the FOMC to execute reverse repurchase agreements with primary dealers, and with a set of expanded counterparties which includes banks, savings associations, GSEs, and domestic money market funds. These reverse repurchase transactions are settled through tri-party arrangements. The FRBNY also executes reverse repurchase agreements with foreign official and international accounts as part of a service offering to account holders. The par values of securities that are sold under agreements to repurchase are deducted from the SOMA portfolio balance when calculating assets available for collateral for Federal Reserve notes. Reverse repurchase agreements are participated to each Reserve Bank based on the Bank's designated share of the domestic SOMA portfolio. (See paragraph 40.70.)[2]

40.25 Securities Lending

The FRBNY, on behalf of the Reserve Banks, may lend, on an overnight or term basis, U.S. Treasury, Federal agency, and GSE debt securities held in the SOMA to securities dealers and to banks participating in U.S. government clearing arrangements. These securities-lending transactions are fully collateralized by Treasury securities, or Federal agency and GSE debt securities if agency securities are loaned, that have fair value in excess of the securities lent. The FRBNY charges the participating dealer or bank a fee for borrowing securities and a fee if the borrower fails to deliver the borrowed securities at maturity. Securities-lending fees are participated to each Reserve Bank based on the Bank's designated share of the domestic SOMA portfolio. (See paragraph 40.70.)

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[2] The domestic allocation rate is also used for reverse repurchase agreements with foreign officials and international accounts.

40.30 Foreign Currency Denominated Investments

The FRBNY, on behalf of the Reserve Banks, holds foreign currency deposits and foreign government debt instruments denominated in foreign currencies with foreign central banks and the Bank for International Settlements (BIS). The FRBNY may also enter into transactions to purchase Euro denominated government debt securities under agreements to resell; these transactions are treated as financing transactions where the repurchase agreement is recorded as an asset and interest income is accrued on a daily basis. Balances result from the execution of transactions and foreign currency interventions for the purpose of stabilizing fluctuations in international flows and exchange values of various currencies and other needs specified by the FOMC. This balance includes the amortization of premiums and discounts. Foreign currency denominated investments, realized and unrealized gains and losses, and interest are participated to each Reserve Bank based on the Bank's designated share of the foreign SOMA portfolio. (See paragraph 40.70.)

Investments denominated in foreign currencies are accounted for at cost on a settlement-date basis, adjusted for amortization of premiums and accretion of discounts using the effective interest method. These investments are backed by the full faith and credit of the issuing foreign governments, or are contracts with the foreign central banks or the BIS. Foreign currency denominated investments of the Reserve Banks are revalued daily at current market exchange rates, with any translation gains or losses recognized in profit and loss. Interest income is recorded on the accrual basis. Any negative interest associated with these foreign currency denominated investments is included in interest income and also recorded on the accrual basis. Gains and losses resulting from sales of securities are determined by specific issue based on average cost.

40.35 Euro Reverse Repurchase Agreements

The FRBNY, on behalf of the Reserve Banks, may enter into euro reverse repurchase agreements, under which foreign currencies are sold under agreements to repurchase. The FRBNY pays interest at a specified interest rate. These transactions are treated as financing transactions where the currency received is treated as a liability and interest payable is accrued on a daily basis. The liability for euro reverse repurchase agreements, as well as the related accrued interest and interest expense is participated to each Reserve Bank based on the Bank's designated share of the foreign SOMA portfolio. (See paragraph 40.70.)

40.40 SOMA Portfolio Holdings—Impairments

The FRBNY evaluates SOMA securities holdings for impairment resulting from credit risk. The periodic allowance for credit loss evaluation should be reviewed by RBOPS Financial Accounting Policy and Reporting Section. Separately, if SOMA securities are determined to be impaired, the impact of recording and disclosing the credit impairment requires RBOPS Financial Accounting Policy and Reporting Section approval.

40.50 Central Bank Liquidity Swaps

Central Bank liquidity swaps, which can be structured as either U.S. dollar liquidity or foreign currency liquidity swap arrangements, are short-term currency arrangements, generally for up to one year, between two parties, the FRBNY, on behalf of the Reserve Banks, and an FOMC authorized foreign central bank. The parties mutually agree to exchange their currencies up to a prearranged maximum amount and for an agreed-upon period of time. These arrangements give the Federal Reserve temporary access to the foreign currencies that it needs to support its international operations and gives the authorized foreign central bank temporary access to dollars.

Subject to the swap agreement provisions, the FRBNY may invest the foreign currencies received under the swap arrangements in interest-bearing instruments, and the interest income on these holdings is accrued and included in interest income on investments denominated in foreign currencies. Each day the swap commitments (both the foreign currency received and the obligation) are revalued at current exchange rates. Any gains or losses resulting from the revaluation of the resulting foreign currency holdings are participated among the Reserve Banks based on the Bank's designated share of the foreign SOMA portfolio. (See paragraph 40.70.)

U.S. dollar liquidity swaps

At the initiation of each U.S. dollar liquidity swap transaction, the foreign central bank transfers a specified amount of its currency to a restricted account for the FRBNY in exchange for U.S. dollars at the prevailing market exchange rate. Concurrent with this transaction, the FRBNY and the foreign central bank agree to a second transaction that obligates the foreign central bank to return the U.S. dollars and the FRBNY to return the foreign currency on a specified future date at the same exchange rate as the initial transaction. The foreign currency amounts the FRBNY acquires is reported as an asset. The foreign central bank compensates the FRBNY based on the amount outstanding and the rate under the swap agreement. The compensation received during the term of the swap transaction is reported as interest income.

Foreign currency liquidity swaps

The structure of foreign currency liquidity swap transactions involves the transfer by the FRBNY, at the prevailing market exchange rate, of a specified amount of U.S. dollars to an account for the foreign central bank in exchange for its currency. The foreign currency amount received is reported as a liability. The FRBNY compensates the foreign central bank based on the amount outstanding and the rate under the swap agreement. The compensation paid during the term of the swap transaction is reported as interest expense.

40.55 Warehousing Agreement

The FOMC has an agreement to "warehouse" foreign currencies for the U.S. Treasury and the Exchange Stabilization Fund (ESF). This is an arrangement under which the FOMC agrees to exchange, at the request of the Treasury, U.S. dollars for foreign currencies held by the Treasury or ESF for a limited period of time. The purpose of the warehousing facility is to supplement the U.S. dollar resources of the Treasury and ESF for financing purchases of foreign currencies and related international operations. In general, this transaction is similar to the swap; however, the parties are the FRBNY and the Treasury. Warehousing agreements are valued daily at current market exchange rates. Amounts are participated to each Reserve Bank based on the Bank's designated share of the foreign SOMA portfolio. (See paragraph 40.70.)

40.60 Interest Earnings and Expense

Net interest earnings and expenses on securities are accrued daily. Consistent with market convention, interest accruals and the amortization of premiums and discounts are recognized beginning on the day that securities purchases settle and ending the day before securities mature or sales settle.

40.70 SOMA Participation

Participated Accounts

The following accounts are those for which activity is allocated to each Reserve Bank consistent with the appropriate participation ratios.[3]

Domestic portfolio:

- Federal agency and GSE obligations bought outright
- U.S. Treasury securities bought outright
- MBS, related short-term investments, fail assets and liabilities, and cash margin accounts
- Interest accrued and interest payable—includes fees on securities lending
- Interest income and interest expense
- MBS fails charge income
- Premium and discount on securities
- Reverse repurchase agreements
- Repurchase agreements
- SOMA domestic other assets
- Realized gains and losses

Foreign portfolio:

- Investments denominated in foreign currencies
- Central bank liquidity swaps
- Foreign deposits
- Interest income and interest expense
- Realized gains and losses

Domestic Participation

All domestic securities activity is participated to each Reserve Bank using the Interdistrict Settlement Account. (See paragraph 5.00.) The participation includes the related interest accrued and premium amortization or discount accretion. Specific securities are not participated to the individual Reserve Banks and the amounts on each Bank's books reflect an undivided interest. Related interest income and gains and losses are participated to each Bank according to its current domestic allocation rate. Allocation is made on the basis of percentages that are derived from an annual settlement of interdistrict clearings and equalization of gold certificate holdings as explained below. The percentages that are used for allocating the account are calculated as follows:

[3] All activity is participated daily, except acceptances, margin balances, interest expense on margin balances, and MBS fail charge income, which are participated monthly.

- In April of each year the Board calculates the average daily balance on each Bank's Interdistrict Settlement account during the preceding 12 months. The average daily settlement account balance (plus or minus) is applied to each Bank's gold certificate account total.
- A calculation is then made of the amount each Bank should have in its gold certificate account to equal the System average of gold certificates to Federal Reserve notes outstanding. In this calculation, an amount is set aside in the FRBNY's account to accommodate future gold sales by the U.S. Treasury.
- The adjustment that would be required in each Bank's gold certificate total is applied by the FRBNY against each Bank's holdings in the SOMA. Thus, a desired decrease in a Bank's gold certificate account is achieved by increasing the Bank's holdings of securities.
- The resulting percentage of each Bank's participation in the SOMA portfolio is used, until the next reallocation, as the basis for allocating the daily SOMA transactions.
- The following is a simplified illustration of the procedure that is performed each April: Assume that Reserve Bank A has gold certificates balance of 105, securities of 2,000, outstanding Federal Reserve notes of 2,000, and during the 12 months ending in March, its ISA settlement account averaged -5. The gold certificate total of all Banks combined is 10 percent of the combined Federal Reserve notes.
  1. The ISA settlement account will be adjusted by debiting it for 5.
  2. The offset to the above ISA entry is to credit the gold certificate account for 5.
  3. The gold certificate account will be adjusted to equal ten percent of the outstanding notes total (2,000 x 10% = 200), increasing the gold account by 100 (200 – 100 = 100).
  4. The offset to the final change to gold account (100) is deducted from the SOMA securities account (2,000 – 100 = 1,900).

Example:	Gold		ISA		SOMA	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Balance before the annual adjustment	105			10	2,000	
1. ISA			5			
2. Gold		5				
3. Gold	100					
4. Securities						100
Balance after adjustment	200		–	5	1,900	

Foreign Participation

All foreign currency denominated activity is participated based on the ratio of each Reserve Bank's capital and surplus to the Reserve Banks' aggregate capital and surplus using the preceding December 31 balances. Specific securities are not participated to the individual Reserve Banks and the amounts on each Bank's books reflect an undivided interest. The accounts are reallocated annually.

5 Federal Reserve Notes

Contents

50.01 General

This chapter discusses special accounting and reporting procedures applicable to Federal Reserve notes. The Federal Reserve Act requires that Federal Reserve notes be issued to a Reserve Bank through the Federal Reserve Agent, or through an Assistant Federal Reserve Agent appointed by the Agent, upon pledge of adequate collateral security by the Bank. Until 1977 the local assistant agents held stocks of unissued notes as a source of supply for the cash departments and issued the notes to the Banks upon receipt of application for specific amounts. The procedure was changed beginning in 1978 and the local stocks were discontinued along with the need for the Reserve Banks to apply for specific amounts or to earmark specific collateral. As part of the new procedure the Federal Reserve Agents designated a member of the Board of Governors' staff in Washington as Assistant Federal Reserve Agent to control the issuance of notes and to monitor the adequacy of collateral that is pledged by each Bank under a continuing agreement. The agreement, executed by each Bank and Agent, results in the pledge of specified assets that the Bank may own at any time plus whatever amount may be required out of the Bank's other eligible assets, including its participation in Treasury, Federal agency, and GSE debt securities held in the System Open Market Account. The specified assets consist of the Bank's gold and SDR certificates, loans under Section 13 of the Federal Reserve Act, and assets acquired under the provisions of Section 14. In December 1990, the Board revised procedures for collateralizing Federal Reserve notes, whereby assets denominated in foreign currencies that have been acquired under the provisions of Section 14 of the Federal Reserve Act may be pledged as collateral by the Federal Reserve Agent or Assistant Federal Reserve Agent in instances where other eligible assets are insufficient to secure Federal Reserve notes fully. In December 1999, the Federal Reserve Act was amended to broaden the range of discount window loans that may be used as collateral for Federal Reserve notes to include all loans to depository institutions. In October 2003, the Federal Reserve Act was further amended to allow all assets of the Federal Reserve Banks to be eligible as collateral for Federal Reserve notes and to specify that collateral is not required for currency held off-site on behalf of Federal Reserve Banks. A statement showing the amount of notes outstanding to each Bank, the notes requiring collateralization, and the various assets pledged as System collateral security is published weekly in the Board's H.4.1 release.

General procedures for handling the cost of procuring Federal Reserve notes are addressed in the Federal Reserve Act, Section 16, which states, "The expenses necessarily incurred in executing the laws relating to procuring of such notes, and all other expenses incidental to their issue and retirement, shall be paid by the Federal Reserve Banks, and the Board of Governors of the Federal Reserve System shall include in its estimate of expenses levied against the Federal Reserve Banks a sufficient amount to cover the expenses herein provided for." The costs incurred by the Bureau of Engraving and Printing (BEP) for printing Federal Reserve notes are invoiced monthly to the Board in accordance with their agreement. On a scheduled basis, the Board assesses the Reserve Banks for these costs based on each Bank's share of the total number of Federal Reserve notes outstanding on December 31st of the previous year. The Board collects the assessment from the Banks in the same month that it remits payment to the BEP. The Reserve Banks record these payments to the Assessment by Board of Governors—F.R. Currency Costs Account (330-150) as described in paragraph 12.45. See *Accounting for Currency Costs* at Appendix A.3 for additional discussion.

50.05 Denominations

Seven denominations of Federal Reserve notes are issued currently. Before 1963 the issuance was limited to denominations of $5 and up. The $1 notes were authorized in

1963 as a replacement for $I silver certificates that were being discontinued because of the need for silver coinage; $2 notes were authorized at the same time but were not printed and issued until 1976. Larger denominations ($500, $1,000, $5,000, and $10,000) were first authorized primarily for interbank transactions by an amendment to the Federal Reserve Act in 1918. With demand for them shrinking, printing of these denominations was discontinued in 1946. The remaining inventories were delivered to Treasury for destruction in 1969 when it was determined that transactions for which the notes had previously been used could be met by other means, such as checks or $100 notes. Currently, circulating large denomination notes received in the normal course of business are destroyed.

50.10 Printing

The BEP Director, under the direction of the Secretary of the Treasury, is responsible for the printing of Federal Reserve notes. Each year, the Board places a printing order with the BEP Director based on the estimated need for new currency and inventory requirements. After newly printed Federal Reserve Notes pass quality control testing, they are delivered to a special vault pending shipment.

50.20 Shipments

The Board's RBOPS Division arranges for the shipments of Federal Reserve notes from the BEP to Federal Reserve offices in amounts sufficient to maintain inventories at agreed upon levels. The notes are shipped from the BEP in the most economical quantities that can be arranged, considering the following: the facilities and the rates of the carrier, the capacity of the Federal Reserve offices to handle the shipments, the amount of insurance that can be provided, the printing schedule and availability of new notes at the BEP, and unusual circumstances that sometimes warrant special shipments (such as armored carrier and airline strikes or the servicing of Reserve Banks moving into new buildings).

50.30 Application for Notes

The law requires that a Federal Reserve Bank make application to the Federal Reserve Agent for the notes required by the Bank. Unless otherwise instructed, the Reserve Bank may make such application on a continuing basis as set forth in the ordering system.

50.40 Issuance

The notes are issued by the Assistant Federal Reserve Agent, normally on the day of shipment from Washington or Ft. Worth. When the Assistant Agent issues notes to the Bank through shipment from the Washington or Ft. Worth facility, the automated ordering system indicates the denomination, dollar amount, District of issuance, and receiving office. The shipments should be taken into Bank cash on the date shown in the ordering system, which is normally the day the shipment will be received. The notes should be credited to the account on FR 34 for Federal Reserve notes outstanding with the offset being reflected in Federal Reserve notes on hand or in transit. Amounts that are in transit at the close of business—i.e., have not been delivered by the courier—should be carried in a general ledger account entitled “Federal Reserve notes in transit.”

Each Reserve Bank's notes outstanding must agree with the records of the Assistant Federal Reserve Agent. The Cash Department of the head office should originate the credit to Federal Reserve notes outstanding for BEP currency shipments based on the date shown in the ordering system, and the contra entry should be made to the Bank's clearing account.

For shipments of notes between Districts, only the receiving office should use the in transit account when notes are not received the day they are shipped. The sending office should debit SDS and credit notes held by Bank or Branches (210-050) on the day shipped. The SDS debit will automatically create a debit to the interim in-transit account (210-075) at the receiving office based on the Inter-FRB account set-up in the Enterprise Accounting System (EASy). The receiving office should clear the interim in-transit account (210-075) with a credit and debit either their standard in-transit account (210-075) or held by Banks or Branches (210-050).

The fact that a shipment may be taken in and pouches not opened until the following day should not affect the general ledger entries. In the event of error in the contents of the pouches or, in exigent circumstances, the return by the courier of a shipment to BEP or Ft. Worth, or rerouting to another Federal Reserve office, adjusting entries may be necessary. These situations, though, are unusual and the Assistant Federal Reserve Agent should keep the Reserve Bank fully informed.

50.43 Sales of Notes by the Bureau of Engraving and Printing

Under a program initiated in 1981, the BEP purchases Federal Reserve notes from Reserve Banks for sale to the public. The currency is sold in uncut sheets of 16 and 32 notes, over-the-counter and by mail, to meet demands for souvenirs of visits to the BEP and for paper money collections. When purchasing the notes, the BEP authorizes the Reserve Banks to charge Treasury's general account for the face value of the notes plus the cost of printing. The authorization is contained in a modified Letter of Advice of Shipment (BEP Form 1907).

On the release date contained in the Letter of Advice, the Reserve Bank debits Treasury's account for the total, credits the face value of the notes to Federal Reserve notes outstanding and credits the amount received for printing costs to the profit and loss account. (See paragraph 12.40.)

50.45 Retirement

Any Federal Reserve Bank may retire its Federal Reserve notes by returning them to the Federal Reserve Agent. The amount of notes that are retired should be debited on the balance sheet to Federal Reserve notes outstanding and removed from the amount of notes on hand. The notes may be reissued to the Bank as determined by the Assistant Agent in Washington D.C. However, it is not the practice to retire notes.

50.50 Redemption

The law requires that unfit Federal Reserve notes be canceled, destroyed, and accounted for under procedures prescribed and at locations designated by the Secretary of the Treasury and that the credit for the unfit notes be apportioned among the Federal Reserve Banks as determined by RBOPS. The Cash departments commonly refer to the process of destroying Federal Reserve notes as "shreds." Shredding currency is one of the destruction methods permitted by the Treasury Currency Operations Manual (TCOM).

All of the present size unfit currency in the \$1–\$100 denominations are to be regarded for initial accounting purposes as Federal Reserve notes. No sort is made of the Bank of issue. The amount of silver certificates and United States notes that are included in unfit currency are identified by formulae after the currency has been destroyed. After deducting such amounts and charging Treasury, redemption credit for the Federal Reserve notes is allocated among the Reserve Banks on the basis of percentages derived from the application of the following formula:

> A Federal Reserve Bank's share of unfit notes in the $1–$100 denominations delivered for destruction shall be the result of the division of (a) the net amount of the denomination outside the Bank at the beginning of the year by (b) the amount of the denomination outside all Federal Reserve Banks at the beginning of the year.

Daily, as part of District cash office operations, unfit notes should be debited to Federal Reserve notes outstanding on the day the notes are destroyed. Branches should arrange for prompt advice to the head office of amounts that they process in order that reduction may be made currently on the head office books. Thus, all unfit currency processed within a particular District should be charged initially against that District"s outstanding notes effective on the accounting day of destruction.

50.60 Large Denomination Notes

The large denominations, consisting of $500–$10,000 Federal Reserve notes, are sorted by Bank of issue and are eventually charged to the issuing Bank for debiting against Reserve notes outstanding. To minimize the number of accounting advices and facilitate control over amounts outstanding, however, all such notes delivered for verification and destruction by a Reserve Bank should be charged initially against that Bank's outstanding notes. Generally, large denomination notes are sent to the Treasury for destruction and initially charged against the outstanding FR Notes of the Federal Reserve Bank of Richmond. RBOPS will thereafter arrange for settlements between Reserve Banks. Such settlements will normally be scheduled in June and December. The Cash Departments will be informed of the settlement at least a week in advance and should enter data on the "Large note clearing" screen in the FR5 system by the deadline indicated in the electronic mail notification provided by RBOPS staff. If there were no large denomination notes redeemed during the period, zeroes should be entered in the total columns on the screen. FRB Richmond processes one combined entry for all Districts to Federal Reserve notes outstanding to adjust for the allocation.

50.65 Currency Destroyed by Treasury

Unfit and mutilated currency processed by the Treasury in Washington, D.C., is functioned through the books of the Richmond Reserve Bank. On the day of redemption, Treasury will advise the Richmond Reserve Bank of the amount for each denomination, including the Bank of issue for $500–$10,000 notes. The Richmond Reserve Bank will credit the Treasury's General Account for the total and debit (reduce) notes outstanding.

The Federal Reserve Banks are responsible for reimbursement for Treasury's destruction of Federal Reserve currency. Each quarter the Treasury forwards to the Board a voucher, indicating the actual cost for services performed for the destruction of Federal Reserve currency during the previous quarter. RBOPS staff calculates the pro rata amount of each Reserve Bank's assessment based on the Bank's share of the number of notes comprising the System's net liability for Federal Reserve notes outstanding on December 31 of the previous year. Reserve Bank assessment entries will be processed via Same Day Settlement by the Richmond Reserve Bank according to information reported on to RBOPS.

50.70 Monthly Note Allocations

The amount of the unfit $1–$100 denominations charged against outstanding Federal Reserve notes during a month will be reallocated by RBOPS in the following month, using percentages prescribed by Treasury for determining silver certificates and United States notes and the formula adopted by RBOPS for allocating Federal Reserve note redemption credit.

Cash Departments report the number and face value (amount) of unfit notes destroyed by denomination each day to RBOPS by entering information in the FR5 System. The amount of the unfit notes destroyed is charged to Federal Reserve notes outstanding. After month-end, but no later than the fifth business day of the following month, a Reserve Bank cash department officer certifies the number and amount of notes destroyed reported on the “Monthly Notes Redeemed” screen in the FR5 system. Consistent with the TCOM requirements for daily destruction certification, the Reserve Bank cash department officer may designate other individuals in management to certify monthly notes redeemed by issuing a memo to the file and notifying the RBOPS Financial Accounting Policy and Reporting Section. To maintain adequate separation of duties, certifying officers or their designees should not have BPS 3000 supervisory access. Data reported must agree with the total of the daily amounts reported destroyed by the cash departments for that month. Following the verification, the FR 5 system will combine the reports and subtract out the Treasury currency portion. The resulting totals for each denomination will be allocated to the Reserve Banks and an electronic mail advice will be sent to each Reserve Bank instructing them to retrieve the entries to be made to their books in the FR5 system. The Richmond Reserve Bank will make one combined entry for all Districts to Federal Reserve notes outstanding to adjust for the allocation.

51.01 Notes Missing from New Packages of Currency

New currency is delivered by the BEP in 4000-note packages. Losses resulting from notes missing from these packages are borne by the BEP. When the BEP reaches a determination regarding missing currency, the BEP remits funds to the Reserve Bank or sends replacement notes covering the amount. The Letter of Advice accompanying the check will be addressed to the Vice President in charge of the Cash Department at the Reserve Bank and will include a listing of the serial numbers and denominations of the notes. The BEP will send copies of the letter to (1) the Assistant Federal Reserve Agent in Washington, D.C. and (2) the Deputy Assistant Commissioner, Banking and Cash Management, Financial Management Service. The Assistant Federal Reserve Agent in Washington, D.C. and the Reserve Bank will make entries on their respective records depending on the circumstances, as outlined below. In each case the offsetting entry will be reflected in the charge against Treasury’s General Account for the BEP’s check.

- *Deficient packages shipped to depository institutions*: For notes that were reported missing in the new packages received by depository institutions, the Reserve Bank will credit the institution and debit profit and loss. A credit will then be made to profit and loss.
- *Deficient packages held by Bank*: For deficient packages that are in Reserve Bank cash, the Reserve Bank will credit Federal Reserve Notes: Held by Bank and Branches and debit profit and loss. A credit will then be made to profit and loss.
- *Deficient packages held by Agent*: For notes that are missing in packages held by the Assistant Federal Reserve Agent, the packages will be issued to the Reserve Bank at the face value as if all notes were present. Upon receipt of such packages, the Reserve Bank will credit Federal Reserve Notes: Held by Bank and Branches by the amount of the shortage and debit profit and loss. A credit will then be made to profit and loss.
- *Notes missing from inventory at Bureau of Engraving and Printing*: For all unissued notes (in either note or sheet form) which the BEP determines to be missing from its inventories, the Assistant Federal Reserve Agent will issue the notes as shown on the BEP’s Letter of Advice. The Reserve Bank will record two entries: first, credit Federal Reserve notes outstanding and debit profit and loss; and second, credit profit and loss and debit to Treasury general account.

51.50 Statements of the Federal Reserve Agent

Section 16 of the Federal Reserve Act requires that each Federal Reserve Agent make daily reports to the Board of Governors on issues and withdrawals of Federal Reserve notes; in addition, the Board requires a monthly report in considerable detail. The reports are prepared by the Assistant Federal Reserve Agent in Washington. The daily report, conforming to FR 5, should show the amount of Federal Reserve notes received from Treasury, on hand, and outstanding, and the classification of collateral security held against Federal Reserve notes. The Assistant Agent should communicate to each Bank daily, for verification by the Bank against its balance sheet, the amount of Federal Reserve notes outstanding as shown on the FR 5 database. The District balance for Federal Reserve notes outstanding is computer-generated upon acceptance of all head office and Branch data.

The monthly report, conforming to FR 44, should show by denomination the cumulative data for issues of notes, notes on hand, notes returned for destruction and credit, and amount outstanding at the end of the month. The amounts reported should agree where applicable with data reported on form FR 5 after taking into account large and small notes clearings, which are reflected on the FR 44, but are not reflected on form FR 5. The report is sent by the Assistant Federal Reserve Agent to Treasury, Financial Management Service, Government-wide Accounting, Cash Accounting Division and to the Office of Compliance.

51.65 Reports to the Assistant Federal Reserve Agent

The Assistant Agent in Washington receives information daily from Board Divisions, from Treasury and from the Reserve Banks. The data from the Reserve Banks include the amount of unfit notes redeemed for the day by denomination and office, and must be received by RBOPS by 10:00 p.m. ET daily. Other reported information is covered by instructions from the Assistant Agent. These include a report by RBOPS of changes in the gold and SDR certificate accounts, a report by the FRBNY of changes in holdings of securities in the System Open Market Account, and letters of advice of purchases of uncut sheets of notes by the BEP and of purchases of notes by the U.S. Treasurer.

51.70 Accountability Records

Under an agreement with and at the request of the Treasury, RBOPS maintains the official accounts for Federal Reserve notes that are held in Washington by the BEP, at Federal Reserve offices, by Federal Reserve Agents and that are outstanding to the Reserve Banks. Records with respect to notes printed and delivered to vaults at BEP are derived from advices received from the Production Division of the BEP; records on currency released to Federal Reserve Agents or the Banks from shipment advices; and records on currency destroyed from the FR 5 database as reported by each cash department followed by a certified monthly summary. The monthly summary should be reported by each Office by the fifth business day of the month following the end of the report period to permit early verification and subsequent certification by RBOPS to the Treasury. RBOPS also uses these records as a basis for certifying Federal Reserve note accounts to the Audit Departments at Reserve Banks and others.

6 Reporting Requirements

Contents

60.01 General

This chapter contains reporting instructions arranged according to the frequency of each report. A summary of all reporting requirements is contained in Table 60.99.

60.10 Daily Reporting

60.11 Daily Preparation

A balance sheet, form FR 34, for each Federal Reserve Bank should be prepared for each day. (See paragraph 60.52 for the standard holiday schedule.) Balance sheet data for each District should be transmitted to the Board daily. Technical procedures for the transmission of FR 34 data may be found in Technical Memorandum No. 15. Preliminary FR 34s are transmitted daily after completing the end-of-day closing process. Final FR 34 data should be transmitted to reach the Board no later than 1:30 p.m. eastern time on standard business days and 5:00 p.m. eastern time on non-standard business days. Standard business days are defined as Monday through Friday, excluding the Federal Reserve System holidays outlined in paragraph 60.52. Non-standard business days are defined as Saturday through Sunday, including Federal Reserve System holidays.

Adjustments to prior day balances may be made before final balance sheets are submitted; however, adjustments to prior day Treasury and depository institution account balances require special procedures and should be rare. Notify the RBOPS Financial Accounting Policy and Reporting Section Manager of all prior day adjustments to Treasury and depository institution accounts.

Special procedures are required for Wednesday, month-end, and year-end balance sheets.

1. When Wednesday is not the first day of the month and is a holiday, or when the last day of the month is a holiday, the balance sheet for the preceding business day should reflect accruals of earnings, expenses, and dividends through the Wednesday holiday or the last day of the month. (See accrual instructions beginning with paragraph 11.56.)
2. At the end of each day, no amount should be reported in the undistributed net income account on the balance sheet. (See paragraph 60.55 for additional discussion.)

60.12 Confidential Daily Summary (L.6.1)

The balance sheet data are consolidated daily and, together with figures from other sources, are used in preparing a confidential daily statement, which is furnished to the Board and various members of its staff, certain Treasury officials, and the Federal Reserve Banks.

60.15 Weekly Reporting

60.16 Factors Affecting Reserve Balances of Depository Institutions and Condition Statement of Federal Reserve Banks (H.4.1)

Section 11(a) of the Federal Reserve Act provides that the Board of Governors shall publish once each week a statement showing the condition of each Federal Reserve Bank and a consolidated statement for all Federal Reserve Banks. This section of the Act further provides that “such statements should show in detail the assets and liabilities of the Banks, single and combined, and shall furnish full information regarding the character of the money held as reserve and the amount, nature, and maturities of the paper and other investments owned or held by Federal Reserve Banks."

The Board's weekly statement is published each Thursday and is compiled from the previous Wednesday's data.

60.20 Monthly Reporting

60.21 Monthly Report

The reverse side of the District balance sheet, FR 34 (FR 34-Back), should be made available in the EASy application and balances that are recorded in Collateral Management System and Fedwire Securities Service applications should be retained and provided to RBOPS Financial Accounting Policy and Reporting Section upon request.

60.22 Currency Held by Federal Reserve Banks

Form FR 415 shows each type of paper money and coin held by the Reserve Bank at the end of the month. The report combined for the District is due at the Board no later than the 6th business day of the following month. The data is used for calculating currency in circulation and must agree with the appropriate FR 34 accounts and figures reported to Treasury on form TFS 4133–Paper Currency On-Hand Report.

60.25 Quarterly Reporting

60.26 Quarterly Report

The Board publishes the *Federal Reserve Banks Combined Quarterly Financial Report*, which presents the Federal Reserve Banks' combined financial statements and is prepared using data that the Reserve Banks make available.

60.27 Income Report—General

Reference paragraph 12.20 for the detailed listing of current income items reported as interest income or total other items of income or loss in the Combined Statements of Operations in both the *Federal Reserve Banks Combined Quarterly Financial Report* and *Federal Reserve System Audited Annual Financial Statements*. The data should be made available to the RBOPS Financial Accounting Policy and Reporting Section through submission of the working trial balance (WTB) for the period. The WTB must be submitted by the date indicated in instructions issued by the RBOPS Financial Accounting Policy and Reporting Section for each period.[1] If an error is found in the amount of income reported for the current year, the necessary correcting entries should be made to the accounts in which the error occurred.

In any calculation of average rates of earnings on assets, use holdings as of the close of business for each day included in the period under consideration in computing average daily holdings.

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[1] Reserve Banks should ensure that current income items reported as interest income or total other items of income or loss in quarterly and annual Combined Statements of Operations agree with the FR 34 balance of account 330-025. If, however, reconciliation to the FR 34 balance is necessary, the reconciliation should be provided to the RBOPS Financial Accounting Policy and Reporting Section.

60.28 Profit and Loss Statement

Reference paragraph 12.40 for the detailed listing of profit and loss items reported as interest expenses, operating expenses, or other items of income or loss in the quarterly and annual Combined Statements of Operations. The data should be made available to the RBOPS Financial Accounting Policy and Reporting Section through the WTB for the period, which must be submitted by the date indicated in instructions issued by the RBOPS Financial Accounting Policy and Reporting Section for each period.[2] Amounts reported on the detailed listing of profit and loss items should reflect the net for each category except that recoveries of losses on shipments of money and losses on shipments of money should be reported in “Other Items of Income or Loss.”

A brief description of the profit and loss account is given in connection with the discussion of the Balance Sheet in chapter 1. The profit and loss account is intended primarily to cover items for which no provision is made in current income or expenses. These include realized gains and losses on sales of securities and on foreign currencies, profit or loss on the sale of real estate (originally acquired for potential Bank use), the write-off of stale officers' and certified checks (paragraph 10.80), losses that are sustained in the handling or transportation of currency, recoveries and unrealized losses on the value of other real estate (originally acquired for potential Bank use) held for sale, and gains or losses on works of art. The account should not normally be used to adjust prior year income or expenses except for the correction of prior year accounting errors when the amount would seriously distort income or expenses of the current year. Entries to the account for prior year items may be made only with the prior approval of the RBOPS Financial Accounting Policy and Reporting Section.

The profit and loss account should not include dividends and rebates on insurance policies or any additional premium payments on worker’s compensation or other insurance regardless of the year for which the refunds or additional payments apply. Such amounts should be entered to current year income or expenses. Other items from the previous year, which should normally be applied to current year income or expenses rather than profit and loss, are receipts from vending machines, refunds from courier contracts, adjustments for the difference between accounts payable and the actual billings, and adjustments for the difference between accrued income from services and actual billings.

The profit and loss account should also exclude losses arising from the ongoing operations of the Reserve Banks. Any such losses should be charged to current expense.

60.35 Annual Reporting

60.36 Annual Report

The Board publishes the *Annual Report of the Board of Governors of the Federal Reserve System,* which provides the Board’s financial statements, the Reserve Banks’

[2] Reserve Banks should ensure that the profit and loss items reported as interest expenses, operating expenses, or other items of income or loss in the quarterly and annual Combined Statements of Operations, as appropriate, agree with the FR 34 balance of profit and loss account 330-100. If, however, reconciliation to the FR 34 balance is necessary, the reconciliation should be provided to the RBOPS Financial Accounting Policy and Reporting Section.

combined financial statements, and pro forma financial statements for Federal Reserve priced services. The Annual Report is prepared using data that the Reserve Banks make available.

60.37 Financial Results of Operations

Preliminary financial results of operations for each annual period should be made available to the RBOPS Financial Accounting Policy and Reporting Section as follows:

1. Profit and loss items reported in the annual Combined Statements of Operations–Reserve Banks should make data, which agree to the FR 34 as of November 30 of each year, available in the WTB for retrieval by the RBOPS Financial Accounting Policy and Reporting Section by the fifth business day subsequent to November 30. Each Reserve Bank should inform the RBOPS Financial Accounting Policy and Reporting Section of any large or unusual deductions that are anticipated during the last month of the calendar year.
2. Estimated annual Combined Statements of Operations–Reserve Banks should make data that agrees to the FR 34 as of December 31 available in the WTB for retrieval by the RBOPS Financial Accounting Policy and Reporting Section by 1:00 p.m. eastern time on the third business day of the year.

Financial Results of Operations
INTEREST INCOME
Loans
Loans to depository institutions
Other loans
System Open Market Account:
Securities purchased under agreements to resell
Treasury securities, net
Federal agency and government-sponsored enterprise mortgage-backed securities, net
Government-sponsored enterprise debt securities, net
Foreign currency denominated investments, net
Central bank liquidity swaps
Total interest income
INTEREST EXPENSE
System Open Market Account:
Securities sold under agreements to repurchase
Other
Deposits:
Depository institutions
Term Deposit Facility
Other
Total interest expense
Net interest income
System Open Market Account:
Treasury securities gains (losses), net
Government-sponsored enterprise debt securities gains (losses), net
Federal agency and government-sponsored enterprise mortgage-backed securities gains (losses), net
Foreign currency translation gains (losses), net
Other
Provision for credit loss
Income from services
Reimbursable services to government agencies
Other components of net benefit costs
Other
Total other items of income (loss)

Financial Results of Operations—*continued*

OTHER ITEMS OF INCOME (LOSS)

OPERATING EXPENSES
Salaries and benefits
System pension service cost
Occupancy
Equipment
Cost of unreimbursed Treasury services
Other
Assessments:
Board of Governors operating expenses and currency costs
Bureau of Consumer Financial Protection
Total operating expenses

RESERVE BANK AND CONSOLIDATED VARIABLE INTEREST ENTITIES
Total Reserve Bank net income from operations
Consolidated variable interest entities: income (loss), net
Consolidated variable interest entities: non-controlling interest (income) loss, net
Reserve Bank and consolidated variable interest entities net income before providing remittances to the Treasury

EARNING REMITTANCES
Earnings remittances to the Treasury, net
Net income (loss) after providing for remittances to the Treasury

COMPREHENSIVE INCOME
Change in prior service costs related to benefit plans
Change in actuarial gains (losses) related to benefit plans
Total other comprehensive income (loss)
Comprehensive income (loss)

Changes in Capital

RESERVE BANK CAPITAL AND NON-CONTROLLING INTEREST
Dividends on capital stock
Transfer to (from) surplus
Consolidated variable interest entities: non-controlling interest – capital contribution (distribution)

60.38 Expense Report

Annual expense information is reported in the Combined Statements of Operations, classified by expense categories. This annual information should be made available in the WTB for retrieval by the RBOPS Financial Accounting Policy and Reporting Section by the designated January date as specified in special instructions from the Board. This report is used to prepare the statement of income and expenses of the Federal Reserve Banks in the Board's Annual Report. The amount reported for net expenses should agree with the same item reported in annual Profit and Loss information in the WTB.

60.39 Real Estate Reporting Requirements—Annual and Special

This section provides instructions for the preparation and submission of accounting reports FR 612 and FR 892.

Book Value of Bank Premises or Other Real Estate

Form FR 612 is a summary of changes in the book value of Bank premises and other real estate and should be submitted to the RBOPS Financial Accounting Policy and

Reporting Section by the date specified within the RBOPS provided year-end instructions. The annual FR 612 is the primary source of data for completion of the Annual Report table, Acquisition Costs and Net Book Value of Premises (including vaults) of the Federal Reserve Banks and Branches. An FR 612 report should also be submitted whenever property is purchased or sold.

Bank-Owned Property Leased to Outside Tenants and Non-Bank-Owned Property Leased for Bank Use

Form FR 892 is dual purpose because it is used to report either the lease of Bank-owned property to outside tenants or the lease of non-Bank-owned property (outside space) for Bank use. Each office should submit an annual report, indicating lease or rental agreements in effect on December 31. A report should be submitted whether or not the office is leasing or renting space. In addition to operations and office space, the report should identify leases for functions such as warehouse, storage, screening, etc. If there are no leases in effect at the end of the calendar year, this should be indicated in the body of the report. Form FR 892 should reach the RBOPS Building Planning Section by January 20 or the next business day of the year following the reporting period. In addition, a report should be submitted whenever a change occurs in a lease or rental agreement including identifying new and/or terminated leases.

The reporting form is designed to accommodate information concerning several leases or rental agreements. In submitting the data, each lease or agreement should be shown on a separate line of the report. If an office is both leasing Bank-owned property to outside tenants and leasing non-Bank-owned property for Bank use, separate reports should be submitted covering each type of transaction, rather than combining them on the same report.

Financial accounting and facility management staff are encouraged to collaborate to provide the appropriate information to complete the reports. Following are specific instructions concerning the data to be reported as of December 31 under the various columns of this report.

1. Bank-owned Property Leased to Outside Tenants
    a. *Location of space*—Identify the location of the leased space within the building (e.g., third floor).
    b. *Effective date of lease*—The contractual date the lease begins (may not correspond to the date the first lease payment is due such as if rent abatement is part of the lease terms). Indicate if the lease amount is on a month-to-month basis.
    c. *Expiration date of lease*—The contractual date the lease expires (typically the date the last lease payment covers).
    d. *Annual rental income*—The annual rent due from the tenant for the reporting period for the base rent amount. Exclude additional rent to recover items such as reimbursement of increased operating cost (utilities, real estate taxes, etc.) or rent derived from the use of Bank spaces (auditoriums, training or conference rooms, etc.). Exclude amortization of leasehold improvements in the rent figure.
    e. *Rented square feet*—The amount of space rented that serves as the basis for the base rent in the lease agreement (defined in terms of rentable square feet).
    f. *Tenant name and use of space*—The name of the tenant on the lease documents and the function(s) for which the tenant intends to use the space.

g. *Bank-owned space available for lease*—The total amount of space defined in terms of rentable square feet that is either currently leased or currently on the market for lease.

h. *Bank-occupied space*—The total amount of space the Bank occupies for its use defined in terms of rentable square feet.

i. *Bank-unoccupied space*—The total amount of space held in reserve for Bank use defined in terms of rentable square feet, while currently unoccupied, is not available for lease to outside tenants.

j. *Shared conference space*—The amount of general conference space including conference center and auditorium spaces (general conference spaces typically included in "building common" category). Exclude conference, meeting, or training space dedicated to a specific Bank department or functional area.

k. *Comments*—Any supplemental information that might be useful to the Board such as additional amounts to be paid over and above rental charge, fit-out allowances provided to the tenant, and special conditions of lease agreements such as amendments or early termination provisions.

2. Non-Bank-Owned Property Leased for Bank Use

   a. *Location of space*—Identify the property street address and the location of the leased space within the building (example: third floor).

   b. *Effective date of lease*—The contractual date the lease begins (may not correspond to the date the first lease payment is due such as if rent abatement is part of the lease terms). Indicate if the lease amount is on a month-to-month basis.

   c. *Expiration date of lease*—The contractual date the lease expires (typically the date the last lease payment covers).

   d. *Annual rental cost*—The annual rent due from the Bank for the reporting period for the base rent amount. Exclude additional rent to recover items such as reimbursement of increased operating cost (utilities, real estate taxes, etc.). Exclude amortization of leasehold improvements in the rent figure.

   e. *Rented square feet*—The amount of space rented that serves as the basis for the base rent in the lease agreement (defined in terms of rentable square feet).

   f. *Use of space*—The function(s) for which the Bank intends to use the space.

   g. *Number of Bank employees*—The number of Reserve Bank employees that occupy the leased space.

   h. *Comments*—Any supplemental information that might be useful to the Board such as additional amounts to be paid over and above rental charge, fit-out allowances provided to the Bank and special conditions of lease agreements such as amendments or early termination provisions.

60.40 Small and Disadvantaged Business Procurement Information

Until May 1999 when the Board issued S-letter 2593, which rescinded S-2492, each Federal Reserve Bank was required to submit an annual form FR 1425, a report of total contract dollars attributed to acquisitions from small and disadvantaged businesses and the proportion of contract dollars assigned to such businesses. The Reserve Banks are still required to maintain records suitable to provide ad hoc reports to the Board; however, the submission of an annual Form FR 1425 is no longer required.

Summary Information should be captured as follows:

1. *Total Contract Awards*—All contracts awarded and commitment dollars for the year, except for those awarded for personal services. The full liability of all purchase orders and contracts should be reported in the year in which they are executed, including the liability associated with all years of a multi-year contract. For any blanket or retainer type contracts that have an “open-ended” or “not-to-be-exceeded” dollar value, actual expenditures rather than commitment dollars should be reported.

2. *Small Business Awards*—Contract awards, commitment dollars, and purchase orders to firms qualifying as a small business concern under the Small Business Act of 1953, as amended. Further, “small business” means a small business concern under Section 3 of the Small Business Act (15 U.S.C. Section 632) and the regulation promulgated thereto defining size standards for government procurement purposes, by SIC industry (13 CFR Section 121.601 et seq.).

3. *Disadvantaged Business Awards*[3]—Contract awards to firms that qualify as economically disadvantaged (minority) business concerns eligible for assistance under Section 8(a) of the Small Business Act. “Small Disadvantaged Business” is small as defined above, and in addition meets the criteria stated in section 8(A) of the Small Business Act; that is a business that is: (1) at least 51 percent owned, and (2) managed and operated on a daily basis, by one or more socially and economically disadvantaged individuals. Such individuals are defined as those who have been subjected to racial or ethnic prejudice or cultural bias because of their identity as a member of a group without regard to their individual qualities. African Americans, Hispanic Americans, Native Americans, and Asian Pacific Americans are among those considered socially disadvantaged. Women-owned businesses should not be reported in this category unless they are a small disadvantaged business as defined above.

4. Supplemental Information should be captured as follows, if applicable.

   Set Asides—All contracts under $10,000 and any contracts over $10,000 for which proposals or bids were restricted to small and disadvantaged businesses. For proposals or bids to be restricted to small and disadvantaged businesses means that the list of vendors to which the proposal or bid is sent must be comprised of small and disadvantaged businesses only. If large businesses competitively bid on an item under or over $10,000 that is subsequently awarded to a small and disadvantaged business, the dollar value of this award should be reported as either a small business award or a disadvantaged business award.

60.50 Other Topics

60.52 Effect of Holiday on Clearings

The Federal Reserve System observes the following holidays:

- New Year's Day–January 1
- Birthday of Martin Luther King, Jr.–Third Monday in January
- Washington’s Birthday–Third Monday in February
- Memorial Day–Last Monday in May

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[3] The Reserve Banks may, in appropriate circumstances and with advice from its General Counsel, institute a disadvantaged business program, so long as that program does not include provisions that would be unlawful if included in a disadvantaged business program of a federal agency.

- Juneteenth National Independence Day–June 19
- Independence Day–July 4
- Labor Day–First Monday in September
- Columbus Day–Second Monday in October
- Veterans' Day–November 11
- Thanksgiving Day–Fourth Thursday in November
- Christmas Day–December 25

Transactional activity related to Fedwire Funds, Fedwire Securities, National Settlement Service, ACH, Check and Cash Service only takes place on standard business days, and as a result, any related clearings for those services will not be processed on the above holidays. For holidays falling on Saturday, Federal Reserve Bank offices will be open the preceding Friday. For holidays falling on Sunday, Federal Reserve Bank offices will be closed the following Monday. When a Federal Reserve Bank closes for a non-standard holiday or unexpectedly, such as in the event of a local disaster, and is unable to participate in the clearing, the debits/credits for that office should be included with the debits/credits for the following business day and reported on the balance sheet in the line item “Due to Other FR Banks—Collected Funds” (220-075).

60.55 Earnings Remittances to Treasury Calculations

Since 1947, the Board of Governors has required that the Reserve Banks remit to Treasury, as interest on Federal Reserve notes, all net earnings after providing for dividends and the amount necessary to equate surplus with capital paid-in. Effectively, this policy sets Reserve Banks surplus levels and requires, as a nondiscretionary expense, each Reserve Bank to remit all residual net earnings to the Treasury. Effective January 1, 2021, the Federal Reserve Act limits the Reserve Banks’ aggregate surplus funds to $6.785 billion (see paragraph 12.60).

The amount of the remittances to the Treasury that were required under the Board of Governor’s policy is reported as “Earnings remittances to the Treasury, net” in the Combined Statements of Operations. The amount of remittances to the Treasury that are required by the Federal Reserve Act is reported as “Earnings remittances to the Treasury, net” in the Combined Statements of Operations.

Before the implementation of the FAST Act, the Board of Governors, under authority of Section 16 of the Federal Reserve Act, had established the following described rate of interest on the outstanding Federal Reserve notes of each Bank less the amount of gold certificates pledged with the Federal Reserve Agent:

> The interest rate on Federal Reserve notes not covered by gold certificates pledged with the Federal Reserve Agent as collateral security for such notes shall be the result of the division of (a) the net earnings of the Federal Reserve Bank after provision for dividends on its outstanding Capital Paid In and for adjustments necessary to equate the amount of its Surplus with the amount of its Capital Paid In, by (b) the daily average amount of Outstanding Federal Reserve Notes of the Bank after deducting the daily average amount of gold certificates pledged with the Federal Reserve Agent as collateral security for such notes.

Daily Accrual

Earnings remittances to Treasury are accrued each day at an amount equal to the end-of-day balance in the Retained Earnings – Current Year account 330-275. Additionally, the Reserve Bank’s surplus balance must be adjusted to ensure it does not exceed the Bank's portion of the aggregate surplus limitation. After recording this daily accrual and the surplus adjustment, if needed, the balance in the Retained Earnings – Current Year account 330-275 should be zero.

Weekly Remittances

The remittance to Treasury should be made each Wednesday. The amount of the remittance should be equal to the lower of the liability (credit) balance in the Accrued Remittances to Treasury / Deferred Asset account 240-925:

1. For the previous Wednesday, or
2. For the day preceding the remittance

If, however, either of the two balances described above is zero or if the balance is a debit, no remittance should be made. In such cases, remittances to Treasury should not resume until sufficient net earnings have been realized to return the balance in the Accrued Remittances to Treasury / Deferred Asset account 240-925 to a liability (credit).

A Reserve Bank should consult the RBOPS Financial Accounting Policy and Reporting Section if it is aware of a significant entry on the remittance day that would have affected the remittance amount had it been recorded on the previous day.

Each Wednesday, Reserve Banks will transfer to the FRB Richmond the amount owed to the Treasury. If the Wednesday is a holiday, the FRB Richmond will remit the amounts owed to the Treasury on the next business day.

Special procedures exist for the first remittance of each calendar year.

Year-End Procedures

The income, expense, and other capital accounts on the year-end FR 34 should include all amounts applicable to the year up to and including December 31, based on the best data available to the Reserve Bank on December 31. The net income on the FR 34 on December 31 should be fully distributed; the surplus should be adjusted to the level of the Bank's portion of the aggregate surplus limit. The necessary entries to adjust surplus are described in paragraph 12.10.

A credit balance in the Accrued Remittances to Treasury / Deferred Asset account 240-925 represents the amount of the first remittance to Treasury in January, which will be made on the first Wednesday in January or on the next business day if Wednesday is a holiday. Similar to the weekly procedures described above, losses or other circumstances that occur in the intervening week may require adjustment to the remittance amount. RBOPS Financial Accounting Policy and Reporting Section should be contacted if the Bank determines that this remittance will be different than the amount recorded in FR 34 account 240-925 as of December 31.

A debit balance in the Accrued Remittances to Treasury / Deferred Asset account 240-925 represents the amount of net earnings that a Reserve Bank will need to realize before remittances to Treasury resume. In this case, the Bank will not make a remittance to Treasury on the first Wednesday in January.

On the January year-end closing date designated by the Board, the previous year's income, expense, and other capital account balances except for capital paid in and surplus are removed from the balance sheet. The amounts removed should be final data for the year as determined by the Reserve Bank and should agree dollar for dollar with the results for the year, which are reported elsewhere, such as in the annual CASPR reports and the reports on income from services.

In some instances, due to the availability of additional information, adjustments to year-end balances may be identified subsequent to December 31 but prior to removing the previous year's income and expenses and other capital accounts data from the balance sheet. Such adjusting entries should be functioned to December 31 balances during the closing process when they serve to more accurately and completely reflect the financial condition of the Reserve Bank. Communication of these adjustments should be made to RBOPS Financial Accounting Policy and Reporting Section through submission of the WTB. As a practical matter, the annual year-end accounting instructions (that include the financial statement shell including footnotes) are sent to the Banks during the year-end process to provide additional detailed reporting instructions.

60.95 RBOPS Financial Accounting Reports System (RFARS)

Reserve Banks are required to submit certain financial accounting reports to the Board electronically using RFARS, the WTB, or email.[4] The reports in RFARS include the following:

FR 415—Currency Held by Federal Reserve Banks (monthly)

FR 612—Book Value of Bank Premises and Other Real Estate (annually, and as property is purchased/sold). Note: RFARS was modified in 2007 to include construction in progress balances as part of the FR 612.

A link to RFARS is located on RBOPS webpage on the Board's website under "Reserve Bank Oversight" and "Financial Management." It can be accessed by clicking on "Financial Accounting Reporting System."

[4] The earnings credits program was eliminated in July 2012. All earnings credits expired by July 2013; therefore, the FR 1217 was discontinued after the second quarter of 2013.

60.99 Reporting Requirements

Daily	Monthly	Quarterly	Semi-Annually	Annually	Special
All Districts					
FR 34-Front	FR 34-Back[1] FR 415[2]	Current income and profit and loss items reported in the Combined Statements of Operations[3]	Large Notes Re-deemed (FR5)	Annual expense information and profit and loss items reported in the Combined Statements of Operations[1] Estimated annual Combined Statements of Operations[1] WTB[1]	
All Offices					
FR 5	Monthly Notes Redeemed (FR5)			FR 34-Front FR 34-Back[1] FR 612 [1] Report on either the lease of Bank-owned property to outside tenants or the lease of non-Bank-owned property (outside space) for Bank use[4]	FR 612-When property is purchased or sold [1] FR 892-Upon changes to lease/rental agreements[1]

All reports are to be filed electronically unless otherwise indicated.

1 Reference paragraph 60.20 to satisfy the reporting requirements.

2 Submitted via RFARS.

3 Reserve Banks should make current income items data available in the WTB for retrieval by the RBOPS Financial Accounting Policy and Reporting Section to satisfy the reporting requirements.

4 Submit report, whether or not space is leased or rented, to RBOPS Building Planning Section.

7 Funding, Credit, Liquidity, and Loan Facilities

Contents

70.01 General

In response to the COVID-19 pandemic, the Federal Reserve created a number of facilities to support the economy during the downturn. The following sections provide information on the background and accounts of each facility program.

70.20 Term Asset-Backed Securities Loan Facility (145-400, 145-415, 145-430, 145-445, 145-460, 145-515, 145-530, and 145-575)

In March 2020, the Federal Reserve Board announced a program to support the credit needs of consumers and businesses by facilitating the issuance of asset-backed securities (ABS) and improving the market conditions for ABS more generally. Under the TALF II LLC, the FRBNY provides loans to eligible issuers of ABS. The loans purchased by the TALF II are not designated as held for sale and therefore are held for investment under FASB ASC Topic 310, *Receivables*. The loans will be recorded at the cost basis. The FRBNY is the primary beneficiary of the TALF II, and its assets and liabilities are consolidated for financial reporting purposes with those of the FRBNY. The primary asset accounts related to the loan facility and the TALF II are described below.

145-400	TALF—loans extended to borrowers
145-415	TALF—ABS held by FRBNY at FV
145-430	TALF—assets, discounts
145-445	TALF—other investments
145-460	TALF—assets, face
145-515	TALF—FV adjustment to ABS held by LLC
145-530	TALF—interest receivable
145-575	TALF—FV adjustment of loans

70.30 Paycheck Protection Program Liquidity Facility

In April 2020, the Federal Reserve Board announced an emergency lending program to facilitate lending to small businesses. The Paycheck Protection Program Lending Facility (PPPLF) bolstered the Small Business Administration's (SBA) Paycheck Protection Program (PPP Loans) of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). Under the PPPLF, the Federal Reserve Banks will lend to eligible borrowers on a non-recourse basis, taking PPP loans as collateral. The covered PPP loans are fully guaranteed as to principal and accrued interest by the SBA, the amount of each being determined at the time the guarantee is exercised. However, these loans still must be evaluated for collectability on at least a quarterly basis. Per ASC Topic 860, *Transfers and Servicing*, the borrower's pledge of collateral will, therefore, be accounted for as a collateral-secured loan by both the borrower and the Reserve Banks.

70.50 Main Street Lending Program

In April 2020, the Main Street Lending Program (Program) was established to support lending to small and medium-sized businesses under the CARES Act. The Program will operate through five facilities: the Main Street New Loan Facility (MSNLF), the Main Street Priority Loan Facility (MSPLF), the Main Street Expanded Loan Facility (MSELF), the Nonprofit Organization New Loan Facility (NONLF), and the Nonprofit Organization Expanded Loan Facility (NOELF). The Federal Reserve authorized the FRBB under section 13(3) of the Federal Reserve Act to lend to MS Facilities LLC (an SPV) through which these facilities will operate. The FRBB is the primary beneficiary of this SPV, and its assets and liabilities are consolidated for financial reporting purposes into the

FRBB. Loan participations purchased under each of the five facilities described below are recorded at the cost of purchase and treated as loans under ASC 310, *Receivables*.

70.51 Main Street Lending Program—Main Street New Loan Facility (145-660 and 145-662)

The Main Street New Loan Facility (MSNLF) was set up to enhance support for small and medium-sized businesses through the provision of credit. The availability of additional credit is intended to help companies that were in sound financial condition prior to the onset of the COVID-19 pandemic maintain their operations and payroll until conditions normalize. Eligible lenders extend new five-year term loans to eligible borrowers ranging in size from $100,000 to $35 million. The maximum size of a loan made in connection with the MSNLF cannot, when added to the eligible borrower's existing outstanding and undrawn available debt, exceed four times the eligible borrower's adjusted 2019 earnings before interest, taxes, depreciation, and amortization (EBITDA). Certain primary asset accounts related to the loan facility are listed below.

145-660	Loan Participation—MSNLF
145-662	Investments—MSNLF

70.52 Main Street Lending Program—Main Street Expanded Loan Facility (145-675 and 145-677)

The Main Street Expanded Loan Facility (MSELF) is intended to facilitate lending to small and medium-sized businesses through the provision of credit. The availability of additional credit is intended to help companies that were in sound financial condition prior to the onset of the COVID-19 pandemic maintain their operations and payroll until conditions normalize. Eligible lenders increase an eligible borrower's existing term loan or revolving credit facility. The upsized tranche is a five-year term loan ranging in size from $10 million to $300 million. Certain primary asset accounts related to the loan facility are listed below.

145-675	Loan Participation—MSELF
145-677	Investments—MSELF

70.53 Main Street Lending Program—Main Street Priority Loan Facility (145-678 and 145-680)

The Main Street Priority Loan Facility (MSPLF) is intended to enhance support for small and medium-sized businesses through the provision of credit. The availability of additional credit is intended to help companies that were in sound financial condition prior to the onset of the COVID-19 pandemic maintain their operations and payroll until conditions normalize. Eligible lenders extend new five-year term loans to eligible borrowers ranging in size from $100,000 to $50 million. The maximum size of a loan made in connection with the MSPLF cannot, when added to the eligible borrower's existing outstanding and undrawn available debt, exceed six times the eligible borrower's adjusted 2019 EBITDA. Certain primary asset accounts related to the loan facility are listed below.

145-678	Loan Participation—MSPLF
145-680	Investments—MSPLF

70.54 Main Street Lending Program—Nonprofit Organization New Loan Facility (145-681 and 145-683)

The Nonprofit Organization New Loan Facility (NONLF) is designed to provide support to small and medium-sized nonprofit organizations and their employees across the United States during the current period of financial strain by supporting the provision of credit to such organizations. Eligible lenders extend new five-year term loans to eligible borrowers ranging in size from $100,000 to $35 million. The maximum size of a loan made in connection with the NONLF cannot exceed the eligible borrower's average 2019 quarterly revenue. Certain primary asset accounts related to the loan facility are listed below.

145-681	Loan Participation—NONLF
145-683	Investments—NONLF

70.55 Main Street Lending Program—Nonprofit Organization Expanded Loan Facility (145-684 and 145-686)

The Nonprofit Organization Expanded Loan Facility (NOELF) is designed to provide support to small and medium-sized nonprofit organizations and their employees across the United States during the current period of financial strain by supporting the provision of credit to such organizations. The NOELF was designed to meet the needs of borrowers with existing loan arrangements, particularly those with larger and more complex existing loans, where pre-existing loan documentation can be used. Eligible lenders increase an eligible borrower's existing term loan or revolving credit facility. The upsized tranche is a five-year term loan ranging in size from $10 million to $300 million. Certain primary asset accounts related to the loan facility are listed below.

145-684	Loan Participation—NOELF
145-686	Investments—NOELF

70.60 Municipal Liquidity Facility (145-700, 145-701, and 145-702)

In April 2020, the Federal Reserve established the Municipal Liquidity Facility (MLF). The Federal Reserve authorized the FRBNY under section 13(3) of the Federal Reserve Act to lend to a SPV through which the MLF will operate. The FRBNY is the primary beneficiary of the MLF, and its assets and liabilities are consolidated for financial reporting purposes with those of the FRBNY. The assets purchased by the SPV are designated as held-to-maturity under ASC 320, *Investments—Debt and Equity Securities*. The municipal notes will be recorded at amortized cost in accordance with ASC 820, *Fair Value Measurement*, subject to analysis for impairment. Cash generated from facility fees may be invested in assets that are valued at fair value.

145-700	Investments at Par—MLF
145-701	Investments Discounts & Premiums—MLF
145-702	Other Investments—MLF

70.70 Bank Term Funding Program (140-057)

On March 12, 2023, each Federal Reserve Bank established and commenced operation of the Bank Term Funding Program (BTFP), pursuant to section 13(3) of the FRA. The BTFP was established to support American businesses and households by making additional funding available to eligible depository institutions to help assure banks have the ability to meet the needs of all their depositors. The BTFP offers loans of up to one year in length to banks, savings associations, credit unions, and other eligible depository institutions pledging any collateral eligible for purchase by the Federal Reserve Banks in open market operations, such as Treasury securities, federal agency and GSE mortgage-backed securities, and GSE debt securities. These assets pledged as collateral will be valued at par.

70.90 Treasury Equity Contribution (240-475)

The U.S. Treasury has made preferred equity investments in each of the credit facilities operated through LLCs through the Exchange Stabilization Fund (ESF). The U.S. Treasury is using the ESF as a backstop to cover any losses the Federal Reserve may incur through lending programs. The preferred equity / deposit contribution for each facility is recorded within the account.

8 Special Topics

Contents

80.01 General

This chapter addresses the accounting for financial assets and liabilities for which the accounting policies are not specified in other FAM chapters. This chapter provides general accounting guidance for the unique aspects of these assets and liabilities, including SOMA assets. Financial assets and liabilities that are not part of the SOMA should be accounted for in accordance with GAAP. Reserve Banks should work with RBOPS Financial Accounting Policy and Reporting Section to determine the appropriate accounting treatment for the transactions described in this chapter and to obtain approval for the accounting analysis and related conclusions.

81.01 Allowance for Credit Losses

The Federal Reserve offers lending facilities to help provide liquidity and funding to the financial markets. Under each facility, a Federal Reserve Bank (Bank) provides credit either to special purpose vehicles (SPVs) created to administer the provision of liquidity to third parties or directly to eligible borrowers. When credit is provided to SPVs, the Banks' lending is secured by the assets of the SPV and, in some cases, by credit protection provided by the Treasury. Loans made directly by the Banks to eligible borrowers and by SPVs to borrowers may be collateralized by pledged assets. These facilities include the following:

1. Primary, secondary, seasonal, and other credit
2. Main Street Expanded Loan Facility (MSELF)
3. Main Street New Loan Facility (MSNLF)
4. Main Street Priority Loan Facility (MSPLF)
5. Municipal Liquidity Facility (MLF)
6. Nonprofit Organization Expanded Loan Facility (NOELF)
7. Nonprofit Organization New Loan Facility (NONLF)
8. Paycheck Protection Program Lending Facility (PPPLF)
9. Term Asset-Backed Securities Loan Facility (TALF)
10. Bank Term Funding Program (BTFP)

Loans extended by the Reserve Banks to consolidated limited liability companies (LLCs) are not considered in the following paragraphs because the loans are eliminated in consolidation. In addition, loans extended to consolidated LLCs that are recorded at fair value do not require an allowance for credit loss.

FASB ASC Topic 326-20 establishes the general expectation of the recognition of lifetime expected allowance for credit losses on financial assets measured at amortized cost, commonly referred to as the Current Expected Credit Loss (CECL) model, regardless of whether the risk of credit loss is deemed to be remote. The following paragraphs discuss key considerations for accounting for credit losses: (1) recognition of an allowance for credit losses, (2) measuring credit losses, (3) recording credit losses, and (4) interest income recognition.

If however, the measure of expected credit losses on a financial asset (or pool of financial assets) in which historical credit loss experience information, adjusted for current economic conditions and reasonable and supportable forecasts, results in a conclusion that the risk of non-payment is zero, an estimate for credit losses is not required to be recognized, so called the "zero loss expectation" exception. Significant judgment is required whether the exception can be applied to a specific class of financial assets with consideration provided to all reasonably available information when evaluating historical loss experience, whether the assets are issued or guaranteed by a government entity, and evaluation of assets secured by collateral. Further, for financial assets secured by collateral provided by the borrower and whose collateral coverage is being used to arrive at a “zero loss expectation” on the asset, FASB ASC Topic 326-20 requires the consideration of potential future changes in value and historical loss information for assets secured with similar collateral, rather than based solely on the assessment of the current coverage. Given the complexity and judgement required in concluding that the “zero loss expectation” exception is appropriate for a given asset class, Reserve Banks should contact RBOPS Financial Accounting Policy and Reporting Section for guidance when considering such plans.

81.02 Recognizing an Allowance for Credit Losses

The credit loss standard codified in FASB ASC Topic 326 requires recognizing lifetime expected credit losses immediately upon the purchase or origination of the loan, even if the likelihood of a loss is remote. The estimate of expected credit losses is based on historical loss information, adjusted to reflect current economic conditions and reasonable and supportable forecasts.

FASB Topic ASC 326-20 requires that upon initial inception or purchase of the loan, and subsequently at each reporting date, the recognition of an allowance for credit losses generally in a consistent manner over the lifetime (in most cases the contractual maturity) of the loan. A comparison of the current estimate of expected credit losses with the previously recorded amount should be performed at each reporting date, with the amount necessary to adjust the allowance for credit losses reported in net income as a bad debt expense or reversal of bad debt expense.

FASB ASC Topic 326-20-30 establishes the presumption of estimating credit losses on financial assets with similar risk characteristics on a collective (pool) basis when similar risk characteristics exist. FASB ASC Topic 326-20 provides guidance on evaluating credit losses for loans in homogenous pools with similar risk characteristics. Only in instances where financial assets are determined not to share risk characteristics with other financial assets in a pool should an evaluation for expected credit losses be performed on an individual basis. Judgement would be required in making this determination, but the estimation method used would need to be supportable qualitatively or quantitatively and consistently applied. Under the current expected credit loss methodology, assets evaluated on an individual basis should not also be included in the collective evaluation. A loan is defined under FASB ASC Topic ASC 326-20 as the contractual right to receive money on demand or on fixed or determinable dates that is recognized as an asset in the creditor’s balance sheet.

Under FASB ASC Topic 326-20, the estimation timeframe for credit losses is over the life of the financial asset. In practice, the estimate should cover the duration of the contractual term of the financial asset. Specific consideration should be given to estimated prepayments as a separate input in the overall credit loss estimate—both in the magnitude and timing of those prepayments. Consistent with FASB ASC Topic 326-20, expected extensions, renewals and modifications would not affect the estimation timeframe unless the extension/renewal options are included in the contract and are not unconditionally cancellable.

81.03 Measuring Credit Losses

Due to the subjective nature of the estimate, FASB ASC Topic 326-20 does not prescribe one method for measuring credit losses. Rather a discounted cash flow method, loss-rate method, roll-rate method, probability-of-default method, or methods that utilize an aging schedule are all appropriate methodologies. Judgment is required to develop an approach that captures expected credit losses for financial assets that can be consistently applied and should take into account the complexity of the asset portfolio under consideration and availability of information. It is acceptable to select different measurement methods for different loan programs, based on a documented rationale as to the choice of the measurement method, including the Bank's reasonable expectations for the recovery of the investment in the loan. Whereas legacy GAAP generally considered past loss experience and current conditions, FASB ASC Topic 326-20 also requires consideration over reasonable and supportable forecasts of future conditions over the lifetime of the asset. Note, while there is latitude provided by the new standard as to what model methodology may be best to estimate credit losses, given the oftentimes complex nature of the estimate, consultation with RBOPS Financial Accounting Policy and Reporting Section is required to ensure consistent application of accounting policy. Further, once the estimate approach has been determined, RBOPS Financial Accounting Policy and Reporting Section should be consulted if a change in measurement methodology is being considered by the Reserve Bank.

Historical loss experience (both internal or external loss information) generally serves as a starting point for estimating expected credit losses under FASB ASC Topic 326-20. The standard details the need to consider adjustments to the historical loss information for differences in current asset specific risks, such as portfolio mix or asset term, and also both the current economic conditions and reasonable and supportable future forecasts of economic conditions. Adjusted loss information should be specific for each asset pool for which expected credit losses are being estimated.

While FASB ASC Topic 326-20 does not prescribe one specific method of measuring credit losses, three of the more common methods are detailed below. The Reserve Bank should select and apply its method consistently and a change in method should be justified by a change in circumstances.

1. The present value of expected cash flows discounted at the loan's effective interest rate
2. The fair value of the collateral if the loan is nonrecourse
3. Probability of default/loss given default

1. Present Value of Expected Cash Flows Method

The discounted cash flow method estimates an allowance for credit losses by calculating the difference between the carrying value of the loan and the present value of the principal and interest cash flows expected to be collected. Based on reasonable and supportable assumptions and projections, the Bank must exercise significant judgment to develop the best estimates of expected future cash flows. All available inputs, including estimated selling costs if those costs are expected to reduce the cash flows available to repay or otherwise satisfy the loan, should be considered in developing the estimate of expected future cash flows. The weight given to the inputs should be commensurate with the extent to which the factors can be verified objectively. If the Bank estimates a range for either the amount or timing of possible cash flows, the likelihood of the possible outcomes shall be considered in determining the best estimate of expected future cash flows.

Other considerations may exist such as loan-specific credit protection in the form of a guarantee or credit insurance feature.[1] In the case of a non-derivative credit enhancement that is separable from the loan such that its benefits do not follow with or are extinguished with the loan, any expected recoveries from credit enhancements cannot be used to offset the recorded amount of the allowance for credit loss for the impaired loan.

If the credit enhancement is attached to the loan, such that it always follows the loan upon its sale, the proceeds of such enhancements may be considered in the loss estimation. The Bank should consider potential recovery from third-party guarantors such as FDIC, other government agencies, or bond insurance. Additional recourse to consider is the ability to debit the borrower's account with the Federal Reserve. The Bank should consider all the cash flows associated with the loan and its specific credit protections when measuring the incurred loss in impaired loans and in determining the adequacy of the loss.

In addition, the basis for the cash flow estimates must be documented and subject to appropriate review procedures.

2. Collateral-Dependent Measurement Approach (as a practical expedient)

The Bank can also measure the impairment of a loan by reference to the fair value of the collateral if the loan is nonrecourse, for example, if the repayment of the loan is expected to be provided solely by the underlying collateral.[2] In accordance with FASB ASC Topic 326-20, the collateral-dependent measurement approach must be applied when default is probable. Furthermore, this method may be elected as a practical expedient when default is not probable but (1) repayment is expected to be provided substantially through the operation or sale of the collateral, and (2) the borrower is experiencing financial difficulty based on the entity's assessment as of the reporting date. The estimated costs to sell, on a discounted basis, should be considered in the measure of impairment if those costs are expected to reduce the cash flows available to repay or otherwise satisfy the loan. Selling costs should be adequately documented and supported.

3. Probability of Default Method

For pool loans that exhibit similar risk characteristics and other loans not individually identified as impaired, a primary determination of the loss accrual under a lender's policy is often the historical loss experience ratio adjusted for current trends and conditions. The Bank can use available historical information adjusted for differences in current asset specific risks, such as portfolio mix or asset term, and also both the current economic conditions and reasonable and supportable future forecasts of economic conditions to develop a range of expected losses.

Expected loss is the estimate of the current amount of loans for which the Bank will be unable to collect over the life of the loan given facts and circumstances as of the evaluation date. Based on historical experience and adjusted for asset specific risks, current economic conditions, and reasonable supportable future forecasts, evaluate the degree of likelihood that the borrowers will not pay, the amount of funds lost when

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[1] As defined for accounting purposes in accordance with FASB ASC Topic 460-10. This may differ from the legal definition of a guarantee. See paragraph 84.01 for further discussion on Guarantees.

[2] Collateral value method does not apply to loans with recourse. Present value of expected cash flows or market price methods are more representative of the impairment since the lender has recourse to additional assets of the borrower.

the borrowers default, and the total amount the Bank may lose, or the Bank's financial exposure to at the time of default. Loss information should be applied to pools that are defined in a manner that is consistent with the pools for which the historical credit loss experience was observed. Note, if a reasonable and supportable forecast for future economic conditions is unable to be estimated, no economic adjustment should be made for those periods. The calculation is based on a formula commonly used in practice to develop a credit loss allowance:

$Expected Loss = PD% * LGD% * $EAD[3]

PD—Probability of default[4]

LGD—Loss given default

EAD—Exposure at default [5]

As a general practice, PD is based on the borrower's risk rating or credit rating and LGD/EAD is based on the underlying collateral and other recourse for each individual loan. The specific approach should be suitably developed for each program given the nature of underlying portfolio and data availability as discussed below.

The loans extended by the Banks under each facility are collateralized. They differ, however, in that some loans are with recourse while others are extended on a nonrecourse basis to the borrowers. As a result, the loss calculation for each differs. For example,

1. For nonrecourse loans, this calculation should be based on the underlying collateral of the individual loan rather than the loan counterparty, because the pledged collateral is the only source of recovery in the event of the borrower's default on the loan.
2. For recourse loans, this calculation should be based on the credit quality of the loan counterparty as well as the underlying collateral, because the Bank can recover by liquidating the underlying collateral as well as from the borrower itself.

For some loan programs, there may be insufficient historical loss experience to use to estimate the PD and LGD. Alternatives methods include

1. default and recovery rates based on historical studies of similar loans, as applicable; and
2. default and recovery rates based on structured finance rating or corporate default study (e.g., S&P, Moody's)

The Bank should also consider factors that might cause the loss experience for the current loan portfolio to differ from historical experience or from a comparison to other default and recovery rates, such as current market conditions, credit concentration, extraordinary portfolio characteristics, other environmental factors, asset-specific risk characteristics, and expectations of future market conditions.

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[3] The percentage of loans (%) expected to default, multiplied by the loss per loan (%) applied to the dollar value ($) of the total loans outstanding.

[4] Default occurs when the debtor cannot pay all or some of the amounts due according to the contractual terms of the loan agreement, including contractual principal and contractual interest amounts.

[5] Exposure at default includes total investment including principal, interest, and unamortized fees.

Subsequent Measurement

Subsequent to the initial measurement of an impairment, if there is a significant change in the amount or timing of the expected future cash flows of an impaired loan, the Bank should recalculate the impairment by applying the principles described above and adjust the valuation allowance.

If using the pooling methodology for estimating credit losses, an evaluation of whether the loans in the collective pool continue to exhibit similar risk characteristics with others in the pool should be performed.

If the Bank measures impairment based on the fair value of the collateral of an impaired nonrecourse loan, it should adjust the valuation allowance if there is a significant change in either the fair value of the collateral at measurement date or expectations of the future fair value of the collateral over the life of the loan. The net carrying amount of the loan should at no time exceed the recorded investment in the loan.

Periodic evaluations should be performed, but no less than quarterly. When performing the review, the Bank should evaluate whether the actual amount and timing of cash flows received from the borrower are consistent with the Bank's previous expectations. The review should take into account any information, events, or other developments as of the reporting date that may affect the Bank's previous estimate of impairment.

81.04 Recording Credit Losses and Charge-Offs

Recording the Credit Loss

If the estimated realizable amount of a pool of homogenous loans or a specific loan is less than the recorded investment in the loan(s), the Bank should recognize the credit loss by creating a valuation allowance with a corresponding charge to bad debt expense account or by adjusting an existing valuation allowance for the loans with a corresponding charge or credit to bad debt expense account. The valuation allowance should be recorded to FR 34 Account 145-360, *Allowance for Credit Losses* (credit); the expense provision should be recorded to Account 330-080, *Provision for Credit Loss Expense* (debit).

The amount of the required valuation allowance is equal to the difference between the loan's *impaired value* (expected realizable value) and the *recorded investment.* The required charge or credit to bad debt expense is equal to the difference between the required valuation allowance and any existing valuation allowance related to that loan.

The recorded investment in the loan includes the outstanding loan balance (net of any charge-offs), accrued interest, deferred loan fees or costs, and unamortized premium or discount.

The net carrying amount of the loan is equal to the recorded investment in the loan less the valuation allowance, or the impaired value. When the Bank determines that a portion of the loan or the entire loan will be uncollectable, the recorded investment in the loan is written down by recording a charge-off against the loan and the valuation allowance. In no circumstances should the net carrying amount of the loan exceed the recorded investment in the loan.

The allowance for credit losses on either a homogeneous pool of loans or individual loans, both evaluated under FASB ASC Topic 326-20, effectively adjusts the loan portfolio or individual loan to its realizable value. Recoveries on previously charged-off amounts will reduce this allowance account.

Charge-Offs

When the loans become uncollectible, a charge-off will be recorded by reducing both loan balance (credit) and allowance for credit losses (debit). If the previously recorded valuation allowance is not sufficient to cover the charge-off, the difference should be recognized as an adjustment to the bad debt expense (debit) and allowance for credit losses (credit) in the current period.

81.05 Interest Income Recognition

Accrual of Interest on Impaired Loans

When the Bank does not have a reasonable expectation of collection of all or some of the amounts due, including both the contractual interest and principal payments under the loan agreement, the individual loan is considered to be impaired and the accrual of interest income on that loan should be suspended.

The recognition of interest income based on the contractual terms of the loan agreement should be discontinued while the loan is considered impaired because any such interest will not be earned (i.e., the Bank does not expect to collect all of the interest and principal in accordance with the contractual terms of the loan agreement).

Subsequent Payments on Impaired Loans

Two accounting practices exist for recording cash payments that are periodically received on the impaired loans: the cash basis method and the modified cost recovery method. The Banks should apply the modified cost recovery method to recover the investment in the loan prior to recognizing interest income, unless contract terms specify treatment. This method is more conservative because it defers income recognition until the principal is recovered.

Cash Basis Method

Under the cash basis method, payments of interest received are recorded as interest income provided the amount does not exceed that which would have been earned at the historical effective interest rate.

Modified Cost Recovery Method

Under the modified cost recovery method, any interest or principal received is recorded as a direct reduction of the recorded investment in the loan. When the recorded investment has been fully collected, any additional amounts collected are recognized as interest income. This method may result in the recorded investment being less than the present value of the loan because the recorded investment excludes interest income and the present value includes interest.

81.06 Valuation Allowance Adjustments

For impairment models leveraging the present value of future cash flow approach, at the end of the reporting period, changes in the loan's impaired basis due to the passage of time (changes in discounted present value) are reflected in the income statement using either the interest method or the bad debt expense method. Because it is more consistent to apply across the spectrum of programs offered by Reserve Banks, the Banks should apply the bad debt expense method.

Interest Method

The change in the present value of a loan should be assessed to identify the changes because of the passage of time and the changes that are because of the amount or timing of expected future cash flows. The increase in present value attributable to the passage of time can be reported as interest income accrued on the net carrying amount of the loan. The change in present value, if any, attributable to changes in the amount or timing of expected future cash flows can be reported as bad debt expense or as a reduction in the amount of bad debt expense that otherwise would be reported.

Bad-Debt Expense Method

The entire change in present value can be reported as bad debt expense or as a reduction in the amount of bad debt expense that otherwise would be reported.

81.07 Program Specific Analysis

Loans and relevant financing receivables should be evaluated quarterly, in accordance with the process described below. Each Reserve Bank should establish appropriate oversight of the review process, including review by the Chief Financial Officer and other Reserve Bank senior management, as appropriate. Based on a Reserve Bank's daily monitoring, if a loan is deemed to be impaired, the RBOPS Financial Accounting Policy and Reporting Section should be notified immediately. The quarterly process includes the following:

1. Identification of loans and relevant financing receivables that need to be evaluated under FASB ASC Topic 326, Financial Instruments—Credit Losses.
2. For loans and relevant financing receivables for which an allowance for credit loss estimate was determined to be necessary under FASB Topic ASC 326 in previous periods, review key inputs, methodology, and assumptions into the allowance for credit loss to ensure that any requisite changes to the estimate are updated and properly reviewed. For loans and relevant financing receivables (for newly originated or purchased financial assets), determine the appropriate estimate methodology, and key inputs and assumptions to develop an allowance for credit loss for instances where the Bank has concluded that there is an expected credit loss (even when considered remote). See paragraph 81.03 for guidance on developing an allowance for credit loss estimate.
3. For loans and relevant financing receivables for which the "zero-loss expectation" exception has been elected, review previous facts and circumstances supporting that conclusion to ensure the "zero loss" assertion is still appropriate.
4. On a quarterly basis, the Bank should submit its quarterly credit loss evaluation and the relevant supporting documentation to RBOPS Financial Accounting Policy and Reporting Section by the 20th of the month following quarter-end, or the next business day if the 20th is a weekend or holiday. The analysis should be prepared in a format acceptable to the RBOPS Financial Accounting Policy and Reporting Section.

Primary, Secondary, and Seasonal Credit; and Emergency Credit

The Federal Reserve Banks' lending serves as a backup source of liquidity for depository institutions. At times when the normal functioning of financial markets is disrupted, Federal Reserve Banks' lending can become a principal channel for supplying liquidity to depository institutions and other entities.

Regulation A, Extensions of Credit by Federal Reserve Banks, governs borrowing by depository institutions and provides terms and conditions for several lending programs, detailed below. The terms under which a depository institution may obtain advances from, incur obligations to, or pledge collateral to a Federal Reserve Bank in borrowing are set forth in Operating Circular No. 10, which is issued by each Reserve Bank.

- Primary credit is only available to depository institutions in generally sound financial condition for periods as long as 90 days, prepayable and renewable by the borrower on a daily basis.[6] Primary credit is generally priced at a rate above the FOMC's target for the federal funds rate.
- Secondary credit is available to depository institutions not eligible for primary credit.[7] It is extended on a very short-term basis, typically overnight, at a higher rate than the primary credit rate. Secondary credit is available to meet backup liquidity needs when its use is consistent with a timely return by the borrower to a reliance on market sources of funding or the orderly resolution of a troubled institution. Secondary credit may not be used to fund an expansion of the borrower's assets. The secondary credit program entails a higher level of Reserve Bank administration and oversight than the primary credit program. A Reserve Bank must have sufficient information about a borrower's financial condition and reasons for borrowing to ensure that an extension of secondary credit would be consistent with the purpose of the facility.
- Seasonal credit is a lending program that is available to assist small depository institutions with demonstrated liquidity pressures of a seasonal nature and will not normally be available to institutions with deposits of $500 million or more.[8] Depository institutions that experience fluctuations in deposits and loans—caused by seasonal types of business—frequently qualify for the seasonal lending program. The interest rate applied to seasonal credit is a floating rate based on market rates.
- Emergency credit is available only in unusual and exigent circumstances under section 13(3) of the Federal Reserve Act, as amended by the Dodd-Frank Act. In addition to being subject to other requirements, such extensions of emergency credit may be made only pursuant to a program or facility authorized by the Board of Governors and approved by the Secretary of the Treasury.

Federal Reserve Banks extend credit on a secured basis. Satisfactory collateral generally includes United States government and federal-agency securities, foreign debt, municipal and corporate debt, commercial paper and bank-issued assets, and commercial and consumer obligations, including real estate related loans. Collateral must be of acceptable credit quality to the Reserve Bank and performing under its terms and conditions. In accordance with Operating Circular No. 10, the borrower assigns to the lending Reserve Bank a continuing security interest in and lien on the collateral as collateral security for the timely and complete payment and performance

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[6] "Generally sound" refers to depository institutions assigned a composite CAMELS or CAMEL ratings of 1, 2, or 3 that are at least adequately capitalized. At the discretion of the Reserve Bank, however, depository institutions that otherwise meet these criteria may be deemed ineligible for primary credit because of supplementary information regarding their financial condition.

[7] Depository institutions assigned a composite CAMELS or CAMELS rating of 4 or 5 or depository institutions that are less than adequately capitalized are not eligible for primary credit. At the discretion of the Reserve Bank, other depository institutions may also be deemed ineligible for primary credit because of supplementary information regarding their financial condition.

[8] Seasonal credit may be extended to depository institutions that are assigned a CAMELS or CAMEL rating of 1, 2, 3, or 4 and are at least adequately capitalized. At the discretion of the Reserve Bank, however, depository institutions that otherwise meet these criteria may be deemed ineligible for seasonal credit because of supplementary information regarding their financial condition.

when due. Reserve Banks take additional steps to perfect their security interest under the provisions set forth in the Uniform Commercial Code.

Assets accepted as collateral are assigned a lending value (market or face value reduced by a margin) deemed appropriate by the Reserve Bank.[9] The financial condition of an institution and the impairment of any collateral are considered when assigning value. The lending Reserve Bank may request the borrower to replace any item of collateral or pledge additional collateral at any time.

Operating Circular No. 10 specifies that, in the event of a default, the Bank may pursue remedies including debiting (or causing to be debited if the borrower is acting through a correspondent) the borrower's account.

Loans are accounted for on the books of the Reserve Bank with which the borrower has the agreement to borrow. The Reserve Bank is required to evaluate credit losses on loans extended through the primary, secondary, and seasonal credit and emergency credit lending programs.

Allowance methodology

1. *Determine whether loans should be evaluated on a collective (pool) or individual basis*

   Factors to consider in determining whether the loans can be evaluated collectively or individually to develop an estimate for expected credit losses are discussed below:

   a. Primary and seasonal credit:

      (1) While generally overnight, the term for primary credit loans may be up to 90 days; under the seasonal credit program loans can be extended for up to 9 months during a calendar year;

      (2) These loans are made to depository institutions deemed to be in generally sound financial condition; and

      (3) The loans require similar types of collateralization and are recourse loans as specified in Operating Circular 10.

   Assessment: Although some loans may warrant individual assessments in consideration of the risk characteristics outlined under FASB ASC Topic 326-20, these loans are generally homogenous in nature and share similar risk characteristics and should be evaluated in aggregate.

   b. Secondary and emergency credit:

      (1) The nature and terms of these loans are not homogenous.

      (2) For both the secondary and emergency loan programs, the financial institutions involved are in some degree of financial distress.

   Assessment: These loans are not homogenous in nature and do not share similar risk characteristics to the extent that it would not be appropriate to evaluate them on a collective basis. These loans should be evaluated individually in accordance with FASB ASC Topic 326-20.

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[9] To calculate the collateral (lendable) value, a margin is applied to either the market price of the securities or the theoretical price of assets that do not receive market values. Market prices are used as the basis for collateral valuation whenever active markets exist. Market prices are obtained from a vendor that prices CDOs and another vendor that prices all other types of securities and updates the prices frequently. If the Reserve Bank is unable to obtain a market price for pledged assets (e.g., consumer loans) from its vendor(s), a theoretical price is calculated for asset categories based on various characteristics of the asset type, including credit quality, interest rate, maturity, liquidity, and the current interest rate environment. A margin is then applied to the theoretical price.

Emergency credit offered through specifically defined targeted programs that are administered by a designated Reserve Bank likely will have a unique profile. Accordingly, specific evaluation and valuation criteria, while consistent with the methodology described herein, should be developed for each program.

2. *Determine allowance for credit loss*

   The Reserve Bank should evaluate the fair value of the collateral to determine if an allowance for credit loss is appropriate.

   a. If the fair value of the collateral is greater than the recorded investment in the loan, there is no loss allowance to be recorded.

   b. If the fair value of the collateral is lower than the recorded investment in the loan and foreclosure is probable, or foreclosure is not probable but the debtor is experiencing financial difficulty and repayment is expected to be provided substantially through the sale or operation of the collateral (i.e., falling under the collateral-dependent practical expedient), calculate the allowance for credit losses under the collateral-dependent measurement approach outline under FASB ASC Topic 326-20 and FAM paragraph 81.03.

   c. If applicable to the specific loan, review any coverage provided by the indemnity agreement between the FDIC or National Credit Union Administration and the Reserve Bank. Refer to FASB Topic ASC 326-20-30 for further guidance on credit enhancements within the loss allowance estimate process.

81.08 Unfunded Commitments

Identify unfunded commitments that are to be evaluated for likelihood of occurrence

For secured lending facilities, the Bank specifies the maximum amount of funding it will provide. The remaining amounts available to borrow under each facility are the “unfunded commitments.” Unfunded commitments, such as loan commitments or financial guarantees, represent off-balance sheet credit exposures and should be evaluated for impairment. See paragraph 84.01 *Accounting for Guarantees* for additional discussion. A liability for expected credit losses on unfunded commitments is recognized if (1) there is a currently a contractual obligation to extend the credit, and (2) the obligation is not unconditionally cancellable. Expected credit losses should be estimated over the contractual life of the unfunded commitment and should consider the probability that the funding will occur.

81.09 Modifications to Debtors Experiencing Financial Difficulty

When a Reserve Bank revises the terms of a loan, this may qualify as a loan modification. The following are types of typical loan modifications:

- Reduction of the stated interest rate
- Extension of the maturity date at a stated interest rate lower than the current market rate for new debt with similar risks
- Reduction of the principal amount of the debt
- Reduction of the accrued interest.

The effect of most loan modifications provided to borrowers experiencing financial difficulties is already included in the allowance for credit losses under FASB Topics ASC 326-20. Therefore, though most modifications will not result in the measurement of the allowance for credit losses, incremental expected losses that are a result of a loan modification can be captured in the Bank’s allowance estimate. The Bank should refer to the loan refinancing and restructuring guidance in FASB Topic ASC 310-20 to determine whether a modification represents a new loan (i.e., as the extinguishment of the original debt instrument and issuance of a new loan) or continuation of an existing loan through modification, as well as specific disclosures required. The loan refinancing or restricting should be accounted for as a new loan when *both* of the following occur:

1. The new loan's effective yield is at least equal to the effective yield for similar loans.
2. The modifications are more than minor.

If these conditions are not met, the refinancing or restructuring should be accounted for as a modification of the original debt instrument, not as a new loan. The loan should be periodically evaluated and, if necessary, adjustments should be recorded to the allowance for loan restructuring and provision for credit loss.

If the Bank expects that, after restructuring the loan, it will be able collect all amounts in accordance with the revised terms of the loan agreement, it should continue to record interest income. If, however, the Bank does not expect to collect all amounts in accordance with the revised terms of the loan agreement, it should discontinue recording interest income and follow the procedures described in paragraph 81.05.

82.01 Consolidation

The Federal Reserve offered funding markets access to liquidity by introducing a number of liquidity facilities that were authorized by the Board under Section 13(3) of the Federal Reserve Act. The facilities were structured such that a specific Federal Reserve Bank (Bank) provided funding to a legal entity, which in turn acquired certain targeted assets from third party entities.[10]

1. FASB ASC Topic 810-10 requires consolidation of legal entities that are within the scope of the standard to meet the criteria specified in FASB ASC Topic 810-10 for Voting Interest Entity Model and the Variable Interest Entity Model. Two different assessments are provided because a controlling financial interest may be achieved other than by ownership of shares or voting interests.
    a. **The voting interest entity model**

       Under the voting interest entity model for legal entities other than limited partnerships, the usual condition for a controlling financial interest is ownership by one reporting entity, directly or indirectly, of more than 50 percent of the outstanding voting shares of another entity.

    b. **The variable interest entity (VIE) model**

       Under the VIE model, a controlling financial interest requires both of the following:

       (1) The power to direct the activities that most significantly impact the VIE's economic performance; and

       (2) The obligation to absorb losses or the right to receive benefits from the VIE that could potentially be significant to the VIE.

A reporting entity with a controlling financial interest in a VIE is referred to as the primary beneficiary. The reporting entity could be, but is not limited to being, an equity

[10] Legal entities are legal entities created to fulfill narrow, specific, or temporary objectives. An SPE typically limits the recourse of its creditors to the net assets of the SPE and as a result, the creditors do not have recourse to the general credit or assets of the SPE's beneficiaries.

investor and another capital provider such as a debt holder, or a party with another contractual arrangement such as a guarantor.

82.02 Evaluating Consolidation Based on Variable Interests

To determine if a Bank must consolidate a legal entity's assets, liabilities, and results of operations, it must first determine if the legal entity is a business within the scope of FASB ASC Topic 810-10.[11] If the legal entity in which the Bank has a financial interest is deemed to be a business, it is not subject to consolidation. Paragraph 82.06 contains a framework that can be used in evaluating whether a VIE financial results must be consolidated in the financial statements of the Bank.

Next, the Bank should determine if the legal entity is within the scope of FASB ASC Topic 810-10. The legal entity is within the scope of FASB ASC Topic 810-10 if one or more of the following conditions exist:

1. The Bank, or its related parties, participated significantly in the design of the entity;
2. The entity is designed so that all of its activities either involve or are conducted on behalf of the Bank and its related parties;
3. The Bank and its related parties provide more than half of the total of the equity, subordinated debt, and other forms of subordinated financial support to the entity, based on the fair values of the interests in the entity;
4. The activities of the entity are primarily related to securitizations or other forms of asset-backed financings; or
5. The Bank is able to direct the economic performance of the legal entity, whether through voting rights or otherwise.

If, based on the criteria in the paragraph above, the entity in which the Bank has a financial interest is determined to be within the scope of FASB ASC Topic 810-10, the Bank must then determine if the entity is a VIE. The entity will meet the definition of a VIE if any of the following conditions are met:

1. The total *equity* investment at risk is not sufficient to finance its activities without additional subordinated financial support. Generally, an equity investment at risk of less than 10 percent of the entity's total assets shall not be considered to be sufficient to finance its activities;
2. As a group, the holders of the *equity* investment at risk lack any one of the characteristics of a controlling financial interest, which are
   a. The power to direct the activities that most significantly impact the entity's economic performance;
   b. the obligation to absorb the expected losses of the entity;
   c. the right to receive the expected residual returns of the entity;

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[11] A business is defined as a self-sustaining integrated set of activities and assets conducted and managed for the purpose of providing a return to investors. A business consists of (a) inputs, (b) processes applied to those inputs, and (c) resulting outputs that are used to generate revenues. For a set of activities and assets to be a business, it must contain all of the inputs and processes necessary for it to conduct normal operations, which include the ability to sustain a revenue stream by providing its outputs to customers. All entities, except those defined in paragraph 4(a)-(h) of FASB ASC Topic 810-10 must be evaluated. Exceptions include not-for-profit organizations, employee benefit plans, health insurance entities, and governmental organizations; other GAAP literature should be used to determine if consolidation is required for these entities.

3. The equity investors' voting rights are not proportional to the economics; for example, absorption of gains or losses is not proportional to voting rights.

If the entity meets the definition of a VIE outlined above, then the Bank's financial interest represents a variable interest and the Bank must consider whether it has a controlling financial interest in the VIE and, therefore, should include the assets, liabilities, and results of operations of the VIE in its consolidated financial statements. The Bank has a controlling financial interest and should consolidate the variable interest entity if it meets both of the following conditions:

1. The power to direct the activities of a variable interest entity that most significantly affect the entity's economic performance.
2. The obligation to absorb losses or right to receive benefits of the entity that could potentially be significant to the variable interest entity.

Only one enterprise, if any, is expected to be identified as the primary beneficiary of a variable interest entity. Although more than one entity could have either of the characteristics described above, only one entity, if any, will have the power to direct the activities of a variable interest entity that most significantly affect the entity's economic performance.

In certain circumstances, the Bank may determine that there is no primary beneficiary associated with a VIE. In these, circumstances, while variable interests exist, because there is no primary beneficiary no reporting entity consolidates the VIE.

Senior beneficial interests and senior debt instruments with fixed interest rates or other fixed returns normally would absorb little of the entity's expected variability and, therefore, a holder of the most senior interests of a VIE likely would not be the primary beneficiary of that entity unless the VIE's subordinated interests are not large enough to absorb the VIE's expected losses. Further, senior interests normally are not entitled to any of the expected residual returns. A Bank that holds a senior financial interest in a VIE, however, should perform an evaluation to determine if it is the primary beneficiary.

To determine if it is the primary beneficiary, the Bank must treat the financial interests (i.e., variable interests) held by its related parties as its own interests. For purposes of FASB ASC Topic 810-10, related parties include those parties identified in FASB ASC Topic 850-10, as well other parties that are acting as de facto agents. The following are considered to be de facto agents of the Bank:

1. A party with a financial interest in the VIE that cannot finance its own operations without subordinated financial support from the Bank, such as another VIE in which the Bank is the primary beneficiary;
2. A party with a financial interest in the VIE that received its interests as a contribution or a loan from the Bank;
3. An officer, employee, or member of the governing board of the Bank;
4. A party that has a financial interest in the VIE and has an agreement that it cannot sell, transfer, or encumber its interests in the VIE without the prior approval of the Bank;
5. A party that has a financial interest in the VIE and has a close business relationship with the VIE or other beneficiaries of the VIE, like the relationship between a professional service provider and one of its significant clients.

If the Bank and another interest holder are considered to be related parties, and the combination of their interest would lead to a conclusion that the related party group is the primary beneficiary, then the party within the related group that is most closely associated with the VIE is the primary beneficiary for purposes of consolidation. Determining the primary beneficiary from among a related group requires judgment and consideration of qualitative factors, such as the following (no single factor is necessarily determinative):

1. Existence of a principal-agency relationship between the parties (in this case the principal is the primary beneficiary);
2. The relationship and significance of the activities of the VIE to the parties in the related group;
3. The parties' exposure to the variability associated with the anticipated economic performance of the VIE;
4. The design of the VIE, such as the capital structure and the intentions of the parties that created the entity.

Other Considerations in Evaluating Consolidation of VIEs

A VIE (VIE 1) itself can hold variable interest in another VIE (VIE 2). If, in evaluating the above criteria, the Bank determines that VIE 1 is the primary beneficiary of VIE 2, then VIE 1 must consolidate VIE 2 in its separate financial statements. The effect of this multi-level consolidation is that VIE 1 will report the assets and liabilities of VIE 2, rather than simply the net investment in that entity. If the Bank is the primary beneficiary of VIE 1, it will, in effect, consolidate both VIE 1 and VIE 2.

If the Bank is the primary beneficiary of a VIE that qualifies as an investment company, FASB ASC Topic 810-10; specifies that a reporting entity shall not consolidate a legal entity that is required to comply with or operate in accordance with requirements that are similar to those included in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The following attributes of an investment company are specified in FASB ASC Topic 946:

1. Investment activity. The investment company's primary business activity involves investing its assets, usually in the securities of other entities not under common management, for current income, appreciation, or both.
2. Unit ownership. Ownership in the investment company is represented by units of investment, such as shares of stock or partnership interests, to which proportionate shares of net assets can be attributed.
3. Pooling of funds. The funds of the investment company's owners are pooled to provide owners access to professional investment management.
4. Reporting entity. The investment company is the primary reporting entity.

FASB ASC Topic 946-10 provides additional insight.[12] See paragraph 82.07, definition matrix of investment company, for further discussion.

82.03 Reconsideration of the Primary Beneficiary

A Bank with an interest in a VIE shall reconsider whether it is the primary beneficiary throughout the reporting period or if one of the following events occurs:

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[12] Although use of the guidance in FASB ASC Topic 946-10 was not adopted by the American Institute of Certified Public Accountants (AICPA), it presents helpful additional guidance that is not included in the Audit Guide.

1. The legal entity's governing documents or contractual arrangements are changed in a manner that reallocates between the existing primary beneficiary and other unrelated parties (1) the obligation to absorb the expected losses of the VIE or (2) the right to receive the expected residual returns of the VIE.
2. The primary beneficiary sells or otherwise disposes of all or part of its variable interests to unrelated parties.
3. The legal entity undertakes additional activities, or acquires additional assets beyond those that were anticipated at the inception of the VIE formation, that increase the entity's expected losses.
4. The legal entity issues new variable interests to parties other than the primary beneficiary or its related parties.
5. The legal entity becomes subject to consolidation by financial interest holders because the equity investors, as a group, lose the power (typically represented by voting rights or similar rights) to direct the activities of the entity in a manner that most significantly impact the entity's economic performance.

A variable interest holder does not subsequently become the primary beneficiary simply because the actual losses of the VIE exceed the expected losses.

82.04 Accounting for the Legal Entities

The assets, liabilities, and noncontrolling interests shall be accounted for in consolidated financial statements as if the VIE were consolidated based on voting interests. Any specialized accounting requirements applicable to the VIE's business, assets, and liabilities shall be applied. Intercompany balances and transactions should be eliminated.

82.05 Disclosure

The primary beneficiary of a VIE shall disclose the following:

1. The carrying amounts and classification of the variable interest entity's assets and liabilities in the statement of financial position that are consolidated in accordance with FASB ASC Topic 810-10, including qualitative information about the relationship(s) between those assets and liabilities.
2. Lack of recourse if creditors (or beneficial interest holders) of a consolidated variable interest entity have no recourse to the general credit of the primary beneficiary.
3. Terms of arrangements, giving consideration to both explicit arrangements and implicit variable interests that could require the Bank to provide financial support to the variable interest entity, including events or circumstances that could expose the Bank to a loss.

If the Bank holds a significant variable interest, but is not the primary beneficiary, it should disclose the following:

1. The carrying amounts and classification of the assets and liabilities in the Bank's statement of financial position that relate to the Bank's variable interest in the entity.
2. The Bank's maximum exposure to loss as a result of its involvement with the variable interest entity, including how the maximum exposure is determined and the significant sources of the Bank's exposure to the variable interest entity. If the Bank's maximum exposure to loss as a result of its involvement with the variable interest entity cannot be quantified, that fact shall be disclosed.

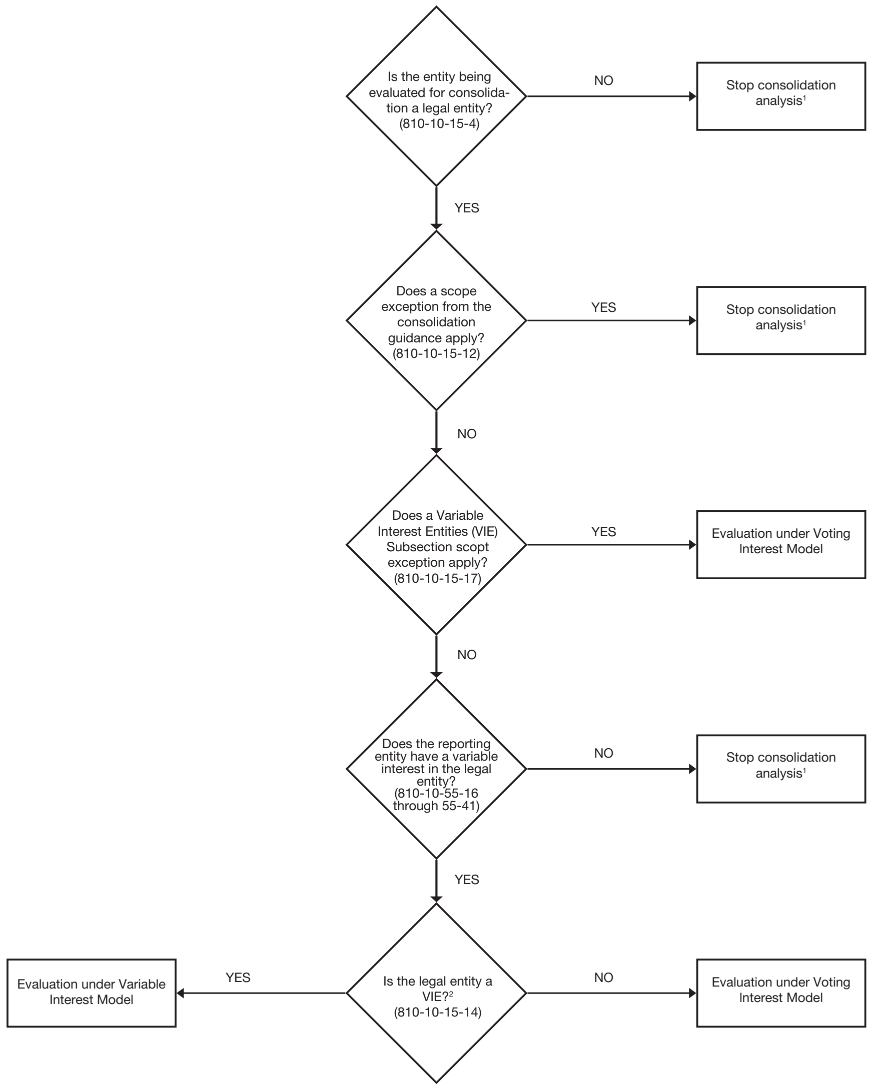
3. A tabular comparison of the carrying amounts of the assets and liabilities, as required by (a) above, and the Bank's maximum exposure to loss, as required by (b) above. A Bank shall provide qualitative and quantitative information to allow financial statement users to understand the differences between the two amounts. That discussion shall include, but is not limited to, the terms of arrangements, giving consideration to both explicit arrangements and implicit variable interests, that could require the Bank to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to the variable interest entity, including events or circumstances that could expose the Bank to a loss.
4. Information about any liquidity arrangements, guarantees, and/or other commitments by third parties that may affect the fair value or risk of the Bank's variable interest in the variable interest entity.
5. If applicable, significant factors considered and judgments made in determining that the power to direct the activities of the variable interest entity that most significantly impact the entity's economic performance is shared.

Information about VIEs may be reported in the aggregate for similar VIEs if separate reporting would not add additional information. Any specialized disclosure requirements applicable to the VIE's business, assets, and liabilities shall be applied.

82.06 Framework for Considering the Consolidation of Legal Entities

Framework for considering the consolidation of legal entities

Consolidation Analysis in Subtopic 810-10



[1]Consolidation not required; however, evaluation of other generally accepted accounting principles (GAAP) may be relevant to determine recognition, measurement, or disclosure.

[2]A legal entity is a VIE if any of the following conditions exist:

a. The equity investment at risk is not sufficient to finance the activities of the entity without additional subordinated financial support provided by any parties.
b. As a group, the holders of the equity investment at risk lack any of the following characteristics of a controlling financial interest:
   1. The power to direct the activities that most significantly impact the entity's economic performance:
      i. For legal entities other than limited partnerships, investors lack that power through voting rights or similar rights if no owners hold voting rights or similar rights (such as those of a common shareholder in a corporation).
      ii. For limited partnerships, partners lack that power if neither (01) nor (02) below exists:
         01. A simple majority or lower threshold of limited partners (including a single limited partner) with equity at risk is able to exercise substantive kick-out rights through voting interests over the genera! partner(s)
         02. Limited partners with equity at risk are able to exercise substantive participating rights overthe general partner(s).
   2. The obligation to abscrb expected losses.
   3. The right to receive expected residual returns.
c. The equity investors' voting rights are not proportional to the economics, and substantially all of the activities of the entity either involve or are conducted on behalf of an investor that has disproportionately few voting rights.

82.07 Definition Matrix of Investment Company FASB ASC Topic 946-10

Guidance—definition matrix of investment company—FASB ASC Topic 946-10

1. Legal entity

   The entity should be organized as a separate legal entity

   a. Corporation,

   b. Partnership,

   c. Limited liability company,

   d. Grantor trust,

   e. REIT, or

   f. Other trust.

2. Business purpose

   For current income, capital appreciation, or both.

3. Entity's activities limited to investment activities

   a. No substantive activities other than investing activities;

   b. No significant assets or liabilities other than those relating to investment activities.

4. Multiple substantive investments

   a. Hold multiple substantive investments simultaneously, either directly or through another investment company.

   b. More than one investment concurrently.

5. Exit strategies

   Identify exit strategies for its investments and the timing (or a range) of when it expects to exit the investments.

6. Not for strategic operating purposes

   Not to obtain benefits as a result of the investments or through relationships with the investee or its affiliates that are unavailable to non-investor entities.

FOLLOWING ARE OTHER FACTORS TO BE CONSIDERED WHEN ASSESSING WHETHER AN ENTITY IS INVESTING FOR STRATEGIC OPERATING PURPOSES

7. Number of substantive investors in the entity (pooling of funds)

   a. The more extensive the pooling of funds (more investors and smaller ownership interests by the investors) to avail owners of professional investment management, the greater the evidence that the entity is investing for current income, capital appreciation, or both.

   b. Related parties as defined should be combined and treated as a single investor for purposes of considering this factor.

8. Level of ownership interests in investees

   a. Significant levels of ownership interests in investees provide significant evidence that the entity is investing for strategic operating purposes. (Conversely, relatively minor levels of ownership interests in investees may provide significant evidence that the entity is investing for current income, capital appreciation, or both.)

   b. Consider the level of ownership interests in investees in relation to the total investment portfolio.

9. Substantial ownership by passive investors

   Substantial ownership by passive investors (as opposed to substantial ownership by principal investors who determine the strategic direction or run the day-to-day operations of the entity) provides evidence of investing for current income, capital appreciation, or both.

10. Substantial ownership by employee benefit plans

    Substantial ownership by employee benefit plans provides evidence that the entity is investing for current income, capital appreciation, or both.

11. Involvement in the day-to-day management of investees, their affiliates, or other investment assets

    The more extensive the involvement in the day-to-day management of investees, their affiliates, or other investment assets, the greater the evidence that the entity is investing for strategic operating purposes.

12. Significant administrative or support services provided to investees or their affiliates

    a. Significant administrative or support services provided to the investees or their affiliates provide evidence that the entity is investing for strategic operating purposes.

    b. Examples of such administrative or support services include legal advice, centralized cash management, or other administrative services that typically are provided by a parent to its subsidiaries or its operating divisions.

13. Financing guarantees or assets to serve as collateral provided by investees for borrowing arrangements of the entity or its affiliates

    a. The more extensive such financing guarantees or assets serving as collateral for borrowing arrangements, the greater the evidence that the entity is investing for strategic operating purposes.

    b. Two exceptions:

       (1) Arrangements in which the entity's ownership interest in an investee serves as collateral for borrowing arrangements of the entity, or

       (2) Arrangements in which the entity guarantees debt of an investee or its affiliates.

14. Provision of loans by noninvestment company affiliates of the entity to investees or their affiliates

    a. Depending on the terms of the loans and other factors, such arrangements may provide evidence that the entity is investing for strategic operating purposes.

    b. Exceptions: such loans are not inconsistent with the definition of an investment company if all of the following exist:

       (1) The terms of the loans are at fair value.

       (2) The loans are not required as a condition of the investment.

       (3) The loans are not made to most of the investees or their affiliates.

       (4) Making the loans is part of the usual business activity of the noninvestment company affiliate.

15. Compensation of management or employees of investees or their affiliates is dependent on the financial results of the entity or the entity's affiliates

    The more extensive such compensation arrangements, the greater the evidence that the entity is investing for strategic operating purposes.

16. Directing the integration of operations of investees or their affiliates or the establishment of business relationships between investees or their affiliates

    a. Directing the integration of operations of investees or their affiliates or establishing business relationships between investees or their affiliates provides evidence that the entity is investing for strategic operating purposes.

    b. Such relationships may include joint ventures or other arrangements between investees, significant purchases or sales of assets or other transactions between investees, investees' participation with other investees in administrative arrangements, investees providing financing to other investees, or investees providing guarantees or collateral for borrowing arrangements of other investees.

In considering the above criteria and their effect on the conclusion about whether an entity is an investment company, some factors may be more or less significant than others, depending on the facts and circumstances, and therefore, more or less heavily weighted in determining whether an entity is an investment company. Criteria 1 through 6 may individually prevent an entity from being classified as an investment company, Criteria 7 through 16 (other factors) are to be evaluated both individually and on a combined basis. Any single criterion of 7 through 16 is not necessarily determinative of whether the entity is an investment company. All of the criteria, however, must be assessed qualitatively, and professional judgment will need to be exercised.

83.01 Valuation of Non-SOMA Financial Assets and Liabilities

This paragraph provides guidance on the valuation of financial assets and liabilities that are not held in the SOMA. The Reserve Banks, largely as a result of liquidity initiatives, have acquired financial assets and liabilities that are not part of SOMA. These financial assets and liabilities should be accounted for in accordance with GAAP applicable to commercial entities. Historically in some cases, the assets were reported by a Reserve Bank through the consolidation of legal entities under the terms of its organization and typically applied GAAP to these assets and liabilities. If appropriate, the Reserve Bank may accept the accounting applied by the VIE, but should review the accounting treatment in consultation with RBOPS Financial Accounting Policy and Reporting Section to ensure consistent accounting for similar Bank assets.

83.02 Evaluating Assets and Liabilities under Relevant Accounting Standards

Financial assets may include commercial paper, mortgage-backed securities, collateralized debt obligations, commercial and residential mortgages, derivative financial instruments, other asset-backed securities, preferred securities, and similar securities. Financial liabilities may include obligations arising under derivative financial instruments and obligations due third-party SPE financial interest holders.[13] The Bank must carefully consider the nature of the financial instrument and the intent of the Bank in holding the instrument to determine the appropriate valuation approach. There are three primary GAAP requirements under which these assets and liabilities should be valued:

[13] Account for derivatives in accordance with FASB ASC Topic 815-20.

1. FASB ASC Topic 320-10 provides general guidance on the valuation of all debt securities and equity securities that have readily determinable fair values. Under FASB ASC Topic 320-10, the debt and equity securities are classified into three categories:

   a. Held-to-maturity securities are reported at *amortized cost*.

   b. Trading securities are reported at *fair value*, with unrealized gains and losses included in earnings.

   c. Available-for-sale securities are reported at *fair value*, with unrealized gains and losses reported in other comprehensive income as a separate component of shareholders' equity.

   Held-to-maturity classification is appropriate in those cases in which the Bank has both the intent and likelihood to hold the securities to maturity. For example, in the case of commercial paper which typically has a relatively short maturity, it may be most appropriate to account for the asset as held-to-maturity. The trading-securities classification is appropriate in cases in which the stated intent with respect to the asset portfolio is an orderly liquidation of assets, since there is no intent to hold the assets to maturity. Available-for-sale securities are generally a residuary category, meeting the definition of neither trading, nor held-to-maturity securities.

   Other real estate assets may be acquired as a result of defaults on the related collateralized asset. Such assets should be recorded at fair value at the date possession is taken of the asset and subsequently should be measured in accordance with paragraph 30.95. The facts and circumstances of each case may need to be evaluated in order to determine when possession occurs.

2. FASB ASC Topic 825-10 allows entities to voluntarily and irrevocably choose, at specified election dates, to measure many financial assets and financial liabilities at fair value. The election is made on an instrument-by-instrument basis. If the fair value option is elected for an instrument, all subsequent changes in fair value for that instrument must be reported in earnings.

   Under FASB ASC Topic 825-10 measuring financial assets and liabilities at fair value is permissible for those assets and liabilities that would otherwise be classified as available-for-sale or held-to-maturity. Electing the fair value option might be appropriate to prevent valuing related assets and liabilities differently. For example, a financial asset and its related derivative, such as a hedging transaction, might be valued differently under FASB ASC Topic 320-10 whereas FASB ASC Topic 825-10 would permit valuing both using fair value. This might reduce volatility in reporting earnings and better reflect the overall economics of the transactions. Another example might be one in which a specific financial liability will be settled from the proceeds of a portfolio of assets; in this case it would be desirable to measure the related assets and liabilities on a similar basis.

   The fair value option can be elected for the following items:

   a. Loan and mortgage receivables

   b. Debt and equity investments (available-for-sale or held-to-maturity securities)

   c. Equity method investments including joint ventures

   d. Loans payable

   e. Debt payable

f. Guarantees[14]

g. Firm commitments that do not qualify as derivatives but involve only financial instruments (e.g., a forward purchase contract for a loan that is not readily convertible to cash. That commitment involves only financial instruments—a loan and cash—and would not otherwise be recognized because it is not a derivative instrument.)

h. Written loan commitments that do not qualify as derivatives

i. The rights and obligations under an insurance contract or a warranty to provide goods or services rather than a cash settlement but whose terms permit the insurer or warrantor to settle by paying a third party to provide those goods or services

j. A host financial instrument resulting from the separation of an embedded non-financial derivative instrument from a non-financial hybrid instrument. An example of such a non-financial hybrid instrument is an instrument in which the value of the bifurcated embedded derivative is payable in cash, services, or merchandise but the debt host is payable only in cash.

The fair value option cannot be elected for the following items:

a. Deposit liabilities, withdrawable on demand

b. An investment in a consolidated entity (a subsidiary or a Variable Interest Entity)

c. Net funding position (liabilities or assets) for pension benefits and other post-employment benefits plans

d. Obligations or assets for employee stock option and stock purchase plans and other forms of deferred compensation arrangements

e. Lease assets or liabilities

f. Financial instruments that are, in whole or in part, classified by the issuer as a component of shareholder's equity

3. Investment Companies—For consolidated SPEs that qualify as investment companies under the criteria of the AICPA Audit and Accounting Guide *Investment Companies,* (Investment Companies Guide), fair value measurement of financial assets is required. If an SPE qualifies as an investment company, then the consolidated financial assets reported by the Bank do not need to be evaluated for classification under FASB ASC Topic 320-10, and no election under FASB ASC Topic 825-10 is necessary. An evaluation of financial liabilities, however, should still be performed to determine if an election under FASB ASC Topic 825-10 is appropriate.

83.03 Fair Value Measurements

For financial assets (or liabilities) to be reported at fair value, the methods for determining the value prescribed in FASB ASC Topic 820-10 should be used. FASB ASC Topic 820-10 defines fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." The best evidence of fair value is the quoted market price in an active market. In the absence of a quoted market price, the bank should estimate fair value using methods applied consistently and determined in good faith. For example, the fair value of a lease at commencement would be its cost, including any acquisition

[14] As defined for accounting purposes in accordance with FASB ASC Topic 460-10. This may differ from the legal definition of a guarantee. See paragraph 84.01 for further discussion on Guarantees.

costs, such as sales taxes and delivery charges. However, if a significant lapse of time occurs between the acquisition of the underlying asset (the lease) and lease commencement, lessors would be required to determine fair value in accordance with ASC 820.

FASB ASC Topic 810-10 establishes a three-level fair value hierarchy that distinguishes between (a) market participant assumptions developed based on market data obtained from sources independent of the reporting entity (observable inputs) and (b) the reporting entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs). Valuation techniques used to measure fair value should maximize the use of observable inputs and minimize the use of unobservable inputs.

Market participant assumptions should include assumptions about the effect of a restriction on the sale or use of an asset if market participants would consider the effect of the restriction in pricing the asset.

83.04 Securities Impairments

For securities classified as either available-for-sale or held-to-maturity under FASB ASC Topic 320-10, the Bank must evaluate the securities for impairment, as outlined in FASB ASC Topic 326. For trading securities or securities accounted for at fair value under FASB ASC Topic 825-10, unrealized holding losses are included in earnings and, therefore, it is not necessary to evaluate such securities for impairment.

For held-to-maturity securities, an approach to testing impairment should follow guidance in FASB Topic ASC 326-20, an approach which is outlined within paragraph 81.03 for financial assets measured at amortized cost.

FASB ASC Topic 326-30 describes the process for recognizing impairment of securities classified as available-for-sale. The model for recognizing impairment is a departure from that outlined for held-to-maturity securities because an entity may realize the value of the securities either through (1) collection of the contractual cash flows by holding the securities, or (2) through the sale of the securities. When evaluating available-for-sale securities for possible impairment, the Reserve Bank should consider the following questions:

Question 1: Is the fair value of the debt security less than its amortized cost basis?

Yes—Generally, an investment is considered impaired if the fair value of the investment is less than its cost. The Bank should determine whether an investment is impaired at the individual security level in each reporting period. FASB ASC Topic 326-30 describes the “individual security level” as the level of aggregation used by the reporting entity to measure realized and unrealized gains and losses on its debt and equity securities. FASB ASC Topic 326-30 also discusses that an investor should not combine separate contracts, such as a debt security and separate guarantee or other credit enhancement, when performing the impairment analysis.

Consider the subsequent question 2 in the available-for-sale decision tree for further consideration regarding recognizing the security’s potential impairment.

No—The security under consideration is not impaired. No further procedures are considered necessary.

Question 2: Is there intent to sell the debt security, or is there a more likely than not possibility that the security will be required to be sold before the recovery of the amortized cost basis?

Yes—As required within FASB Topic ASC 326-30, once there is an intent to sell the debt security, or there is a more likely than not possibility that the security will be required to be sold before the recovery of the amortized cost basis, any previously recognized allowance for credit losses should be written off and the amortized cost basis shall be written down to the security's fair value at the reporting date, with any incremental impairment subsequently reported in income. At subsequent reporting periods, the previous amortized cost basis less the amounts written off (inclusive of non-credit related impairment reported in earnings) is considered to be the new amortized cost basis of the investment and it should not be adjusted for subsequent recoveries in fair value.

No—proceed to question 3 below to consider the underlying reason for the decline in fair value of the security under evaluation for impairment.

Question 3: Is the decrease in fair value below the amortized cost noted in question 1 a result of credit loss, or is it driven by a factor other than credit losses, such as a change in market rates, not related to credit considerations of the underlying issuer of the security?

Yes—A quantitative evaluation of whether a credit loss exists on the security should be performed by the Reserve Bank. As a part of this assessment, the present value of cash flows expected to be collectible from the security should be compared with the amortized cost basis. If the present value analysis results in a fair value that is less than the amortized cost basis, a credit loss exists and an allowance for credit losses should be recognized by the Reserve Bank. Note, as part of this evaluation, the amount of the credit loss recognized should be limited by the difference between the calculated fair value and the amortized cost basis because the Reserve Bank could theoretically sell the securities at fair value to offset the full realization of credit losses.

In accordance with FASB Topic ASC 326-30, the following qualitative factors should be considered when determining whether a credit loss exists:

1. The magnitude of the calculated difference between the fair value and the amortized cost
2. Specific adverse condition factors related to the security, including certain considerations over the industry or geographic area of the issuer of the security
3. The payment structure of the debt security
4. Non-payment of contractually owed interest or principal by the issuer
5. Changes to credit ratings of the security

Note, factors such as length of time a security has been in an unrealized loss position (i.e., the fair value less than the amortized cost basis of the security), the security's historic price volatility, or post balance sheet date increases/decreases in fair value should not be used by themselves, or in combination with others, by the Reserve Bank to conclude that a credit loss does not exist.

In estimating the future cash flows for the purpose of measuring impairment on the available-for-sale security, the amounts should be the Reserve Bank's best estimate based on the historic performance of the security, adjusted for current conditions and reasonable and supportable forecasts. Elements specific to the security, such as the remaining maturity of the security, potential prepayment activity, underlying financial health of the issuer, value/type of collateral, and expected future credit events (i.e., default or bankruptcy), should be used when estimating the amount and timing of collection of expected future cash flows. Available information directly related to the collectability of the security, including industry, economic, or regulatory factors, should also be considered when developing an estimate. Refer to FASB Topic ASC 326-30 for a full list of considerations that the Reserve Bank should review when estimating impairment on an available-for-sale security using expected future cash flows.

Once the measurement of credit loss on the security has been determined by the Reserve Bank, the impairment should be recognized by recording an allowance for credit losses. As stated previously, this amount is limited by the difference between the calculated fair value of the security, less the amortized cost basis. Impairment determined to not be related to credit specific factors (i.e., a change in market rates) should be recorded in the Reserve Bank's other comprehensive income. Refer to the 'No' response below for further details.

An evaluation of impairment of the security should be performed by the Reserve Bank periodically at each reporting date. Any subsequent changes in the impairment of the security related to credit specific factors should be recorded as an adjustment to the allowance for credit losses (and related entry to record the credit loss expense or reversal of credit loss expense). The Reserve Bank should not reverse a previously recognized allowance for credit losses to an amount below zero.

Note also, available-for-sale securities deemed to be uncollectible should be written off in the period of that determination.

No—Impairment determined to be driven by a factor other than credit considerations of the underlying issuer of the security, such as a change in market rates, shall be recorded through other comprehensive income.

84.01 Guarantees

This paragraph provides guidance determine whether certain commitments fall within the scope of FASB ASC Topic 460-10 and how and when to account for a guarantee. While legally a loan commitment, for accounting purposes guarantees are defined in FASB ASC Topic 460-10. For those arrangements that qualify as guarantees under FASB ASC Topic 460-10 a Reserve Bank may be required to record a liability for the fair value of the obligation it assumes under the guarantee, when the guarantee obligation is established.[15]

84.02 Definition of guarantees

FASB ASC Topic 460-10 defines guarantees in terms of certain characteristics. Transactions with the following characteristics are considered to be guarantees and should be evaluated to determine if an obligation requires recognizing a liability at the time the guarantee is issued:

1. Contracts that contingently require the guarantor to make payments (either in cash, financial instruments, other assets, or provision of services) to the guaranteed party

[15] For constructive obligations, see paragraph 84.04 *Determining when to recognize a guarantee.*

based on changes in an underlying[16] that is related to an asset, liability, or equity security of the guaranteed party (e.g., financial and market value guarantees). Following are some examples to which this provision applies:

a. A financial standby letter of credit, which is an irrevocable undertaking (typically by a financial institution) to guarantee payment of a specified financial obligation.

b. A market value guarantee on either a financial asset (such as a security) or a nonfinancial asset owned by the guaranteed party.

c. A guarantee of the market price of the common stock of the guaranteed party.

d. A guarantee of the collection of the scheduled contractual cash flows from individual financial assets held by a special-purpose entity (SPE).[17]

e. A guarantee granted to a business or its owner(s) that the revenue of the business (or a specific portion of the business) for a specified period of time will be at least a specified amount.

2. Contracts that contingently require the guarantor to make payments to the guaranteed party based on another entity's failure to perform under an obligating agreement (performance guarantees).
3. Indemnification agreements that contingently require the indemnifying party (guarantor) to make payments to the indemnified party (guaranteed party) based on changes in an underlying that is related to an asset, a liability, or an equity security of the indemnified party, such as an adverse judgment in a lawsuit or the imposition of additional taxes due to either a change in the tax law or an adverse interpretation of the tax law.
4. Indirect guarantees of the indebtedness of others.

Item 1 above includes most financial standby letters of credit, written put options or market value guarantees on securities (including the common stock of the guaranteed party), and many other financial guarantees. Item 1, however, would not include traditional commercial (non-standby) letters of credit and other loan commitments because they typically do not guarantee payment of an obligation and do not provide for payment in the event of default. Financial standby letters of credit are guarantees because they do not have material adverse change (MAC) clauses or similar provisions that enable the issuing institution (the guarantor) to avoid making a payment. In contrast, many loan commitments contain MAC clauses or other similar provisions that enable the issuing institution to avoid making a loan if the borrower encounters financial difficulties after the commitment is issued.

As an example, if a Reserve Bank provided a guarantee to an entity whereby it would provide loans to that entity if certain asset fair values fell below a predetermined level, the arrangement would probably qualify as a guarantee under FASB ASC Topic 460-10. Because the arrangement may meet the characteristics described in Item 1 above, recognition of a liability at the issuance of the guarantee would be required. The contract contingently requires the Reserve Bank (guarantor) to make payments to the guaranteed party (in the form of loans) based on changes in the fair value of certain

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[16] An underlying is defined in FASB ASC Topic 815-20 as a specified interest rate, security price, commodity price, foreign exchange rate, index of prices, or other variable. The occurrence or nonoccurrence of a specified event is a variable that is considered an underlying under that definition.

[17] See paragraph 82.01 *Consolidation* for additional discussion of SPE.

assets (the underlying). More specifically, the guarantee might qualify under Item 1(a), which refers to a standby letter of letter of credit, or Item 1(b), which refers to a market value guarantee.

84.03 Exclusions from Guarantees

The scope provisions of FASB ASC Topic 460-10 are complex because while certain contracts are fully excluded from its scope, others are excluded from the initial recognition and initial measurement provisions, but are subject to the disclosure provisions.

The following guarantee contracts are fully excluded from the scope of FASB ASC Topic 460-10:

1. A guarantee or an indemnification that is excluded from the scope of FASB ASC Topic 450-20, including vacation pay, pension costs, deferred compensation contracts, and stock issued to employees.
2. A lessee’s residual value guarantee in a capital lease under FASB ASC Topic 460-10.
3. A guarantee (or an indemnification) whose existence prevents the guarantor from being able to either account for a transaction as the sale of an asset that is related to the guarantee's underlying or recognize in earnings the profit from that sale transaction.

The following types of guarantees are not subject to FASB ASC Topic 460-10 for initial recognition and initial measurement, but are subject to its disclosure requirements:

1. A guarantee that is accounted for as a derivative instrument at fair value under FASB ASC Topic 815-20.
2. A guarantee for which the underlying is related to the performance (regarding function, not price) of *nonfinancial* assets that are owned by the guaranteed party (e.g., product warranties).
3. A guarantee issued in a business combination that represents contingent consideration.
4. A guarantee for which the guarantor's obligation would be reported as an equity item (rather than a liability).
5. A guarantee issued either between parents and their subsidiaries or between corporations under common control.
6. A parent's guarantee of its subsidiary's debt to a third party (whether the parent is a corporation or an individual).
7. A subsidiary's guarantee of the debt owed to a third party by either its parent or another subsidiary of that parent.

84.04 Determining When to Recognize a Guarantee

FASB ASC Topic 460-10 requires a guarantor to recognize a liability at the inception of the guarantee. FASB ASC Topic 460-10 does not, however, clarify when the inception of a guarantee occurs. FASB ASC Topic 460-10 states that the provisions of the standard apply to guarantee contracts, implying the existence of an enforceable contract. FASB ASC Topic 460-10 states “…entering into a *contract or agreement* that imposes on the guarantor an ongoing obligation to stand ready to perform over the term of the guarantee warrants immediate recognition of a liability for the obligations under the guarantee, even if it is not probable that the specifying triggering events or conditions will occur." This provision includes the word *agreement* in the definition of a guarantee, whereas paragraph 3 refers only to contracts. In its entirety, FASB ASC Topic 460-10 anticipates that a contract or agreement is required to create a guarantee.

Statement of Financial Accounting Concepts No. 6, *Elements of Financial Statements* (CON 6), paragraph 40 states, "…although most liabilities stem from legally enforceable obligations, some liabilities rest on equitable or constructive obligations. An equitable obligation stems from ethical or moral constraints rather than from rules of common or statute law. A constructive obligation is created, inferred, or construed from the facts in a particular situation rather than contracted by agreement with another entity. Concepts of equitable and constructive obligations must be applied with great care. To interpret them too narrowly will tend to exclude significant actual obligations of an entity, while to interpret them too broadly will effectively nullify the definition by including items that lack an essential characteristic of liabilities."

While FASB ASC Topic 460-10 anticipates the existence of a contract or agreement, CON 6 argues that a constructive obligation under a guarantee might exist even without a legally enforceable obligation. The Reserve Banks should evaluate all of the facts and circumstances in evaluating when a guarantee exists. Consider the following in evaluating whether a constructive obligation exists:

1. The party's expressed intent to seek a guarantee from a Reserve Bank is not sufficient evidence of the existence of an obligation because there is no indication of agreement among the parties.
2. The party's actions that may appear to be in anticipation of Reserve Bank actions, absent any other evidence of agreement between the parties, is not sufficient evidence of the existence of an obligation.
3. A statement by a Reserve Bank that it intends to enter into negotiations with the guaranteed party is not sufficient to indicate the existence of an obligation, since the terms would be indefinite at this point.
4. A Reserve Bank's past practice of entering into similar transactions with other parties cannot be considered as evidence supporting the existence of a constructive obligation in a new arrangement. Each guarantee arrangement is a stand-alone transaction that should be separately evaluated on its merits by the Reserve Bank.
5. Express actions or statements by authorized Reserve Bank representatives that would reasonable lead to an expectation on the part of the party such that the party acts on the expectations might provide evidence that a constructive obligation exists.
6. A joint statement of the Reserve Bank and the guaranteed party that includes important terms of the guarantee might provide evidence that a constructive obligation exists.
7. A term sheet that is agreed to by all parties provides evidence of a constructive and possibly a legal obligation.

If an obligation under a guarantee existed at the balance sheet date, a liability should be recorded in accordance with FASB ASC Topic 460-10. If, subsequent to the balance sheet date but before the issuance of the financial statements, additional information becomes available that affects the obligation that existed at the balance sheet date, the obligation should be adjusted on the balance sheet. If an obligation under a guarantee is material and is issued after the balance sheet date but before the financial statements are issued, the Bank should disclose the guarantee as a subsequent event.

84.05 Initial Measurement of a Guarantee

When the guarantee obligation is established, the guarantors should recognize a liability equal to the fair value of the guarantee on their financial statements under FASB ASC Topic 460-10. If at the inception of the guarantee, it is not probable that a triggering event will occur, then no liability is necessary under FASB ASC Topic 450-20. In the unusual circumstance that it is probable that a liability will occur, a FASB ASC Topic 450-20 contingent liability should be recognized. In such a situation, the liability to be initially recognized for the guarantor's obligation under the guarantee shall be the greater of (a) FASB ASC Topic 460-10 guarantee liability at fair value or (b) FASB ASC Topic 450-20 contingent liability. There are two primary approaches for initially measuring the fair value of the guarantee obligation under FASB ASC Topic 460-10:

1. When a guarantee is issued in a stand-alone arm's-length transaction with an unrelated party and explicit consideration is received, the liability recognized at the inception of the guarantee should be the *premium received* or receivable by the guarantor.
2. When a guarantee is issued as part of a multiple element transaction with an unrelated party (such as in conjunction with selling an asset or entering into an operating lease), the liability recognized at the inception of the guarantee should be an *estimate of the fair value of the guarantee*. In that circumstance, guarantors should consider the premium that would be required by the guarantor to issue the same guarantee in a stand-alone arm's-length transaction with an unrelated party. In the absence of observable transactions for identical or similar guarantees, expected present value measurement techniques will likely provide the best estimate of fair value.

Generally, because of the unique nature of most guarantees, few are valued based upon "observable transactions for identical or similar transactions." The valuation of most guarantees, therefore, will require the use of fair value estimates.

With respect to estimating fair value, FASB emphasizes that the fair value of a guarantee at inception is not equal to the guarantor's single best estimate of what it will be required to pay under the guarantee. It has further clarified that the notion of fair value contemplates the range of probabilities and potential payments that could be required under the guarantee, not merely a point estimate of the most likely outcome.

FASB ASC Topic 460-10 does not prescribe specific accounting for the guarantor's offsetting entry when it recognizes a guarantee liability. That offsetting entry depends on the circumstances in which the guarantee was issued, as illustrated in FASB ASC Topic 460-10:

1. If the guarantee were issued in a stand-alone transaction for a premium, the offsetting entry would be the consideration received (such as cash or a receivable).
2. If the guarantee were issued in conjunction with the sale of assets, a product, or a business, the overall proceeds (such as the cash received or receivable) would be allocated between the consideration being remitted to the guarantor for issuing the guarantee and the proceeds from the sale. That allocation would affect the calculation of the gain or loss on the sale transaction.
3. If the guarantee were issued in conjunction with the formation of a partially owned business or a venture accounted for under the equity method, the recognition of the liability for the guarantee would result in an increase to the carrying amount of the investment.
4. If a guarantee were issued to an unrelated party for no consideration on a stand-alone basis (that is, not in conjunction with any other transaction or ownership relationship), the offsetting entry would be to expense.

In most cases, the Reserve Banks enter into agreements accounted for as guarantees for no consideration. In these cases, the fourth situation listed above would be applicable, and the Banks should charge the initial obligation to profit and loss (FR 34 Account 330-080).

84.06 Subsequent Measurement of a Guarantee

Subsequent to initial measurement, the accounting would depend on the nature of the guarantee and how the Reserve Bank (guarantor) is released from risk. FASB ASC Topic 460-10 provides three possible approaches to the subsequent accounting for the guarantee:[18]

1. Marking the guarantee to fair value at each balance sheet date, so long as the guarantee remains outstanding;
2. Leaving the guarantee at its original amount until either expiration or settlement of the guarantee;
3. A systematic and rational amortization of the value of the guarantee to income over the period of the guarantee.

If the guarantee issued by a Reserve Bank is based on a change in an underlying, such as a change in the fair value of certain assets of the guaranteed party (market value guarantee), then the subsequent measurement of the liability should be based on marking the guarantee to market at each balance sheet date. This approach is especially relevant if the obligation was initially measured using a fair value approach. If a fair value approach is not feasible, then the value of the guarantee may be amortized over the period of the guarantee in a systematic and rational manner.

Any residual liability that remains at the termination of the guarantee should be recorded to profit and loss in the period of the termination. For a guarantee whereby the Reserve Bank agrees to make loans to the guaranteed party based on the occurrence of a future event, the period of the guarantee expires when the maximum amount of loans required under the guarantee have been extended.

84.07 Disclosure

The Reserve Bank must disclose the following information about each guarantee, or each group of similar guarantees in its annual financial statements, even if the likelihood of having to make any payments under the guarantee is remote:

1. The nature of the guarantee, including the approximate term of the guarantee, how the guarantee arose, and the events or circumstances that would require the Reserve Bank to perform under the guarantee.
2. The maximum potential amount of undiscounted future payments the Reserve Bank could be required to make under the guarantee. That maximum potential amount of future payments shall not be reduced by the effect of any amounts that may possibly be recovered under recourse or collateralization provisions in the

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[18] The subsequent measurement of a guarantee liability under FASB ASC Topic 460-10 discussed here does not encompass (and therefore, is separate from) the recognition and subsequent adjustment of the contingent liability under FASB ASC Topic 450-20 relating to the contingent loss for the guarantee. FASB ASC Topic 460-10 in general requires the recognition of a guarantee liability in an earlier stage when it is not probable that the triggering events will occur (and therefore, a FASB ASC Topic 450-20 contingent liability will not be recognized). When it becomes probable that a liability will be incurred, a FASB ASC Topic 450-20 contingent liability needs to be assessed and the greater of (a) FASB ASC Topic 460-10 guarantee liability at fair value or (b) FASB ASC Topic 450-20 contingent liability should be recorded.

guarantee. If the terms of the guarantee provide for no limitation to the maximum potential future payments under the guarantee, that fact shall be disclosed. If the Reserve Bank is unable to develop an estimate of the maximum potential amount of future payments under its guarantee, it shall disclose the reasons why it cannot estimate the maximum potential amount.

3. The current carrying amount of the liability, if any, for the Reserve Bank's obligations under the guarantee (including FASB ASC Topic 450-20 contingency liability), regardless of whether the guarantee is freestanding or embedded in another contract.
4. The nature of (1) any recourse provisions that would enable the Reserve Bank to recover from third parties any of the amounts paid under the guarantee and (2) any assets held either as collateral or by third parties that, upon the occurrence of any triggering event or condition under the guarantee, the Reserve Bank can obtain and liquidate to recover all or a portion of the amounts paid under the guarantee. The Reserve Bank shall indicate, if estimable, the approximate extent to which the proceeds from liquidation of those assets would be expected to cover the maximum potential amount of future payments under the guarantee.
5. The method used for subsequent accounting for the guarantee and an explanation of why the method chosen is appropriate for the guarantee.

Appendixes

These appendixes are intended to be a reference and include previously issued accounting guidance or more detailed information for some topics that are addressed in FAM. For additional information, please contact any member of the RBOPS Financial Accounting Policy and Reporting Section.

A Currency

A.1 Currency Shipments[1]

A.2 BPS 3000 Machine Useful Lives

On September 17, 2012, the Board of Governors' RBOPS Division approved the recommendation of the Cash Product Office to extend the estimated useful life of the BPS 3000 currency processors (CP) and reconciling stations (RS) from December 31, 2017, to December 31, 2022. This change in the estimated useful life is supported by both the BPS 3000 upgrade that was completed in 2010 and by the added functionality to the system. The upgrade introduced technology that will support the currency authentication and verification process over the next 10 years. Further support for the change to the estimated useful life is based on the enhancements to the machine via new and upgraded sensors in 2012 and 2013 and from the extended maintenance terms with Giesecke & Devrient America, Inc. through 2022. The estimated useful life change is effective January 1, 2013.

Useful life history of the BPS 3000 machines:

- In 1992, the BPS 3000 machines were installed with a 10-year useful life.
- In 1997, the useful life was extended 5 years, until 2007.
- In 2004, the useful life was extended an additional 10 years, until 2017.
- In 2012, the useful life was extended an additional 5 years, until 2022.

The machines were originally thought to have a 30-year useful life, but the original 10-year life was based on the collective anticipated life of the System's information technology, data architecture, and computer components. Over time, the machines have continued to operate with new sensors and extended maintenance agreements. The current sensors have useful lives through 2022. Sensors have the capability to authenticate the current currency's design, and up to one additional currency design. The CTO extended the maintenance agreements through 2022 with the maintenance provider, which is confident of the viability of the technology over the extended period.

Per FAM paragraph 30.76, the change in estimate shall be accounted for prospectively such that the remaining net book value is depreciated over the expected remaining useful life of the asset. This extension applies to the BPS 3000 CP and RS and all production sensors. This change in estimate, however, does not affect the accounting for spare sensors because spare sensors are recorded as hardware assets, as of January 1, 2021, and depreciated over the life of the maintenance agreement.[2]

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1 This section was revised in April 2013 and the revision is in Reserve Banks Note Accountability System.

2 Prior to January 1, 2021, spare sensors were recorded as deferred assets and amortization schedule was tied to the maintenance agreement.

A.3 Accounting for Currency Costs

The costs incurred by the Bureau of Engraving and Printing (BEP) for printing Federal Reserve notes are invoiced to the Board. The amount charged is based on the number and denomination of notes that are moved to dedicated storage vaults at BEP facilities ("Fed vault") during that month. When the BEP invoice is received by the Board, it assesses each Reserve Bank a pro rata share of the BEP's printing costs based on each Bank's share of the number of FR notes outstanding at December 31st of the previous year. The Board assesses the Banks for the printing cost, settles the assessment with the Banks, and remits payment to the BEP within the same accounting period. As a result, the Board has no residual asset or liability at any month- or year-end. The Reserve Banks record the scheduled assessment received from the Board directly to expense, in accordance with FAM (see paragraph 12.45).

The following examines from a Reserve Bank perspective whether the inventory of Federal Reserve notes in the BEP vault, the cost of which has been paid by the Board, creates an asset of either the Board or the Reserve Banks. The analysis concludes that the current Reserve Bank accounting for these costs is appropriate.

Federal Reserve Act Provisions

The current accounting treatment by both the Board and the Reserve Banks is based on the relevant provisions of the Federal Reserve Act (the Act). Relevant excerpts are as follows:

- Section 16 (¶1)—Federal reserve notes, to be issued at the discretion of the Board of Governors of the Federal Reserve System for the purpose of making advances to Federal reserve banks through the Federal reserve agents as hereinafter set forth and for no other purpose, are hereby authorized.
- Section 16 (¶2)—Any Federal Reserve bank may make application to the local Federal Reserve agent for such amount of the Federal Reserve notes hereinbefore provided for as it may require. Such application shall be accompanied with a tender to the local Federal Reserve agent of collateral in amount equal to the sum of the Federal Reserve notes thus applied for and issued pursuant to such application.
- Section 16 (¶4)—The Board of Governors of the Federal Reserve System shall have the right, acting through the Federal Reserve agent, to grant in whole or in part, or to reject entirely the application of any Federal Reserve bank for Federal Reserve notes; but to the extent that such application may be granted the Board of Governors of the Federal Reserve System shall, through its local Federal Reserve agent, supply Federal Reserve notes to the banks so applying, and such bank shall be charged with the amount of the notes issued to it.
- Section 16 (¶9)—When such notes have been prepared, the notes shall be delivered to the Board of Governors of the Federal Reserve System subject to the order of the Secretary of the Treasury for the delivery of such notes in accordance with this Act.
- Section 16 (¶10)—The expenses necessarily incurred in executing the laws relating to the procuring of such notes, and all other expenses incidental to their issue and retirement, shall be paid by the Federal reserve banks, and the Board of Governors of the Federal Reserve System shall include in its estimate of expenses levied against the Federal reserve banks a sufficient amount to cover the expenses herein provided for.
- Section 10 (¶3)—The Board of Governors of the Federal Reserve System shall have power to levy semiannually upon the Federal reserve banks, in proportion to their capital stock and surplus, an assessment sufficient to pay its estimated expenses

> and the salaries of its members and employees for the half year succeeding the levying of such assessments, together with any deficit carried forward from the preceding half year.

These provisions establish that the Board is responsible for approving issuance of notes to the Reserve Banks, supplying notes to the Reserve Banks, and assessing the Reserve Banks for the expenses incurred in procuring notes. Section 10 of the Act addresses the general approach to the Board's assessment of expenses.

Discussion

The BEP's practice of invoicing costs on a per-unit basis is not specified in the Federal Reserve Act. Presumably, this convention was developed as a mechanism for systematically charging to the Board its costs related to producing notes. The Federal Reserve Act requires that the Reserve Banks bear the ultimate costs incurred to procure Federal Reserve notes through the Board's assessment mechanism. (Federal Reserve Act Section 16 ¶10). The Board's assessment on the Banks provides the Board with sufficient resources to fund its operations, including the expenses related to procuring notes. The assessment is similar to a tax because it is a statutory obligation, and it is not based on a contractual relationship between the Reserve Banks and the Board. The assessments levied on individual Reserve Banks are not based on which District's notes were produced in that period.

Neither the Board nor the Reserve Banks have regarded the printing costs of notes held at the Fed vault to be assets, such as inventory or prepaid expenses. This is because the Act describes the costs of procuring notes as expenses (Federal Reserve Act Section 16 ¶10). The Board does not regard the notes delivered to the Fed vault to be assets because it does not believe the costs represent a future economic benefit as defined in Statement of Financial Accounting Concept No. 6.[3] While the Board may control the Reserve Banks' access to the notes, the costs incurred to produce the notes do not result in net cash inflows to the Board. The Reserve Banks do not control access to the Federal Reserve notes until such time as they are shipped from the BEP.

Another reason that the Reserve Banks do not consider the assessments to be assets is because the costs do not result in future net cash inflows but, rather are an expense related to carrying out activities that constitute the Banks' ongoing major or central operations, as described in Statement of Financial Accounting Concept No. 6.[4] Statement of Financial Accounting Concept No. 6 recognizes that the character of expenses depends on the nature of the operations involved. Because the Reserve Banks' payment of currency printing costs is an assessment, it is most accurately treated as an expense item similar to other Board assessments, which is also consistent with the provisions of the Federal Reserve Act. The assessments are similar to a tax levied on the Banks by the Board.

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[3] Statement of Financial Accounting Concepts No. 6 states that an asset has three essential characteristics: (a) it embodies a probable future benefit that involves a capacity, singly or in combination with other assets, to contribute directly or indirectly to future net cash inflows, (b) a particular entity can obtain the benefit and control others access to it, and (c) the transaction or other event giving rise to the entity's right to or control of the benefit has already occurred.

[4] Statement of Financial Accounting Concepts No. 6 states that expenses represent actual or expected cash outlays that have occurred or will eventuate as a result of the entity's ongoing major or central operations. The transactions and events from which expenses arise and the expenses themselves are in many forms—for example, cost of goods sold, cost of services provided, depreciation, interest, rent and salaries and wages—depending on the kinds of operations involved and the way expenses are recognized.

Based on the Federal Reserve Act provisions and the discussion of assets and expenses in Statement of Financial Accounting Concept No. 6, treatment of the assessment for the costs to procure Federal Reserve notes as a period expense is appropriate.

Other Considerations

Consideration might be given to treating the costs to procure notes as debt issuance cost. Statement of Financial Accounting Concept No. 6 discusses debt issue cost as follows:

> "Debt issue cost…is either an expense or a reduction of the related debt liability. Debt issue cost is not an asset for the same reason that debt discount is not—it provides no future economic benefit. Debt issue cost in effect reduces the proceeds of borrowing and increases the effective interest rate and thus may be accounted for the same as debt discount. However, debt issue cost may also be considered an expense of the period of borrowing."

We do not believe that the note printing costs are debt issuance costs. Federal Reserve notes differ from typical debt instruments because they are non-interest bearing in a traditional sense and have no stated term. The printing costs do not reduce the proceeds of the Bank's liability related to outstanding Federal Reserve notes and, therefore, are not similar to a debt discount. The issuance of Federal Reserve notes is fundamentally different than the debt issuances described in this section of Concept Statement No. 6 and treating the costs as assessment expense is a more appropriate accounting approach. Further, Concept Statement No. 6 allows for treatment of the costs as a period expense.

Conclusion

The accounting treatment of BEP printing costs that has been followed by the Board and the Reserve Banks remains appropriate. This accounting treatment is based on the requirements of the Federal Reserve Act, and is consistent with the accounting guidance in Statement of Financial Accounting Concept No. 6.

B Dividends

B.1 Payment of Dividends from Surplus

A 1922 opinion from the Board of Governors' Legal Counsel.

To: Federal Reserve Board
From: Mr. Walter S. Logan, General Counsel
Subject: Payment of dividends of Federal Reserve Banks out of surplus
Date: April 11, 1922

You have requested my opinion upon the question of whether a Federal reserve bank, which has accumulated a surplus fund out of earnings of past years, has authority to use a part of this fund to pay to its stockholding member banks the dividend for a subsequent year during which the current earnings of the federal reserve banks are insufficient to pay such dividend.

I am of the opinion that the question should be answered in the affirmative.

The material portions of Section 7 of the Federal Reserve Act read as follows:

> "After all necessary expenses of a Federal reserve bank have been paid or provided for, the stockholders shall be entitled to receive an annual dividend of six per centum on the paid-in capital stock, which dividend shall be cumulative. After the aforesaid dividend claims have been fully met, the net earnings shall be paid to the United States as a franchise tax except that the whole of such net earnings, including those for the year ending December thirty-first, nineteen hundred and eighteen, shall be paid into a surplus fund until it shall amount to one hundred per centum or the subscribed capital stock of such bank, and that thereafter ten per centum of such net earnings shall be paid into the surplus.
>
> "…Should a Federal reserve bank be dissolved or go into liquidation, any surplus remaining, after the payment of all debts, dividend requirements as hereinbefore provided, as the par value of the stock, shall be paid to and become the property of the United States and shall be similarly applied."

This section provides that the earnings of the Federal reserve banks shall be used for the following purposes in the order named:

1. For the payment of or provision for expenses.
2. For the payment to stockholders (who are member banks exclusively) of cumulative dividends at the rate of six percent per annum on paid-in capital.
3. For creating and adding to a surplus fund until such fund equals 100 percent of subscribed capital.
4. The balance to be paid 90 percent to the United States as a franchise tax and 10 percent into surplus.

The question for determination is what are the rights of a Federal reserve bank with respect to the payment of dividends when the bank has already accumulated a surplus out of its past earnings but has failed during some subsequent year to earn a sufficient amount to pay the full dividends for that year.

No payment can be made into the surplus fund unless the earnings for the current year are sufficient to pay in full the dividends for that year and any dividends for past years that may remain unpaid. Thus Congress has directed that the payment of current and past dividends shall take precedence over the accumulation of a surplus fund. In the absence of any indication to the contrary, it would be natural to assume from this that Congress intended also that the payment of current and past dividends should take precedence over the maintenance of a surplus fund already accumulated.

It is to be noted that the provision in the second paragraph of Section 7, regarding the disposition of the surplus fund in the event of the dissolution or liquidation of a Federal reserve bank, makes it clear that the surplus fund of a Federal reserve bank will be available ultimately to pay the cumulative dividends in full.

It is clear also that the payment of dividends out of surplus can result in no loss of revenue to the United States, for no franchise tax can become due until the six percent cumulative dividends have been paid in full. If the surplus should not be used to pay dividends for a year in which the current earnings are insufficient for this purpose, the back dividends would have to be paid out of future earnings before the United States becomes entitled to any franchise tax. In fact, the failure to pay dividends out of surplus in excess of 100 percent of subscribed capital would result in loss of revenue to the United States; because if dividends for any year should remain unpaid, they would have to be paid in full out of the earnings of future years before any franchise tax becomes payable, whereas, if dividends should be paid out of the surplus and the surplus were not thereby reduced below 100 percent of subscribed capital, future payments into the surplus fund would amount to only 10 percent of future earnings over and above current dividend requirements, the other 90 percent being paid to the United States.

It may be argued that, without regard to the questions of the franchise tax, Congress intended that each Federal reserve bank should accumulate a surplus fund for the purpose of protecting such bank against possible future losses and that the fund should be available for no other purpose. It is to be noted in this connection, however, that under the present terms of Section 7 there is no limit to the size of the surplus fund that must be accumulated. All of the earnings, over and above dividend requirements are required to be paid into the surplus fund until such fund equals 100 percent of the subscribed capital (which is equivalent to 200 percent of paid-in capital since under the law only one-half of the subscribed capital is required to be paid in and the balance now remains subject to call), and after a surplus fund equal to 100 percent of subscribed capital has been accumulated, ten percent of all future net earnings over and above dividend requirements must be paid in to the surplus fund. It is hardly reasonable to assume that Congress intended to prevent a Federal reserve bank from paying its current dividends while its surplus fund is far in excess of the amount of its subscribed capital.

Under Section 7 as originally enacted, the argument that the surplus fund of a Federal reserve bank was intended solely as a protection to the bank against possible future losses could have been made with greater force. Prior to the amendment of March 3, 1919, the provisions of Section 7, which correspond to those already quoted form the present Section, read as follows:

> "After all necessary expenses of a Federal reserve bank have been paid or provided for, the stockholders shall be entitled to receive an annual dividend of

> six per centum on the paid-in capital stock, which dividend shall be cumulative. After the aforesaid dividend claims have been fully met, all the net earnings shall be paid to the United States as a franchise tax, except that one half of such net earnings shall be paid into a surplus fund until it shall amount to forty per centum of the paid-in capital stock of such bank.
>
> "…Should a Federal reserve bank be dissolved or go into liquidation, any surplus remaining, after the payment of all debts, dividend requirements as hereinbefore provided, and the par value of the stock, shall be paid to and become the property of the United States and shall be similarly applied."

Thus, the maximum surplus fund which could have been accumulated under the original section was 40 percent of the paid-in capital and it might well have been argued that the purpose of Congress in making provision for this limited surplus was solely to protect the bank against future losses. Even under the original section, however, the question was open to serious doubt, for a Federal reserve bank was required to apply its earnings to the same purposes and in the same order as under Section 7 as amended, and the payment of cumulative dividends therefore took precedence over the accumulation of a surplus fund. Furthermore the payment of dividends out of surplus fund would not have reduced the revenues of the United States. So the same arguments, except that which is based on the unlimited size of the surplus fund, could have been advanced in support of the right of a Federal reserve bank, under the terms of the original Section 7, to pay dividends out of surplus. In my judgment Congress in amending Section 7 so as to require the accumulation of a surplus fund of unlimited size must be considered to have recognized that under both the original section and the section as amended the surplus fund could be used for the payment of the cumulative dividends. Otherwise, it is only reasonable to assume that Congress would have required or permitted some part of the earnings, which must now go into the unlimited surplus, to be paid into a fund of "undivided profits" out of which the dividends could be paid currently in a year of small earnings.

This leads to the observation that under the terms of Section 7 a Federal reserve bank is not permitted to accumulate a fund of "undivided profits". It is the usual custom of commercial banks to show among their liabilities an item of "undivided profits", in addition to their liabilities on account of capital and surplus. From this fund of "undivided profits", dividends are customarily paid and from it also transfers are made from time to time to increase the surplus fund. No banks, so far as I am aware, are prohibited from paying dividends out of this fund of "undivided profits" even though such dividends are in excess of the earnings for the current year. Consequently, by accumulating a fund of "undivided profits" from year to year a bank may make provision for the continuance, during years when earnings are small, of dividend payments without reducing its surplus fund. A Federal reserve bank cannot make provision for the continuance of dividends in this particular manner, because the law absolutely requires Federal reserve banks to dispose of earnings, over and above the amount paid as dividends, either by payment into the surplus fund or by payment of the franchise tax to the United States.

The continuity of dividends is fully as desirable in the case of Federal reserve banks as it is in the case of commercial banks, and Congress, having precluded the Federal reserve banks from making provision for such continuity by setting up "undivided profits", may reasonably be assumed, in my opinion, to have contemplated that the surplus funds, which are required to be accumulated without limit as to size, would be available for the purpose of paying dividends as well as for the purpose of protecting the banks again possible future losses.

From the statement heretofore made that the dividends of commercial banks are customarily paid out of undivided profits, it is not to be inferred that the payment of dividends out of the surplus of commercial banks is prohibited. As I shall now attempt to show, the general rule is that banks may pay dividends out of surplus unless the terms of their charters, or the statutes to which they are subject, prohibit them from so doing.

In deciding the specific question now under consideration no great weight can be attached to the general rules of law as to the powers of corporations generally, or banks in particular, with respect to the payment of dividends; for Federal reserve banks are sui generis, and they are governed by the mandatory provisions of Section 7 of the Federal Reserve Act which take away from the directors all discretionary power as to the disposition of any part of current earnings. Nevertheless, I am of the opinion that a consideration of these general rules of law will serve in some slight measure to confirm the conclusion that a Federal reserve bank may use its surplus fund for the payment of dividends for a year in which its current earnings are insufficient for that purpose.

It is a fundamental principle of the law of corporations, that unless otherwise provided by statute, charter or other limitation, the question of whether a corporation which has surplus profits on hand shall declare a dividend, and what part of such profits shall be distributed by means of such dividend, is a question for the determination of the directors in the exercise of their discretion, and the courts will not interfere with action taken by the directors in the exercise of such discretion unless they act fraudulently or in bad faith.

Gibbons v. Mahon, 136 U.S., 549*;*
N.Y. Ry. Co. v. Nickals, 119 U.S., 296*.*

See also 14 Corpus Juris, p. 808-810 and cases there cited.

It is also held generally that dividends may lawfully be declared out of any surplus of corporate assets over corporate debts and capital stock, that is to say, anything remaining after provision for the corporation's capital stock and liabilities is properly available for distribution to stockholders, although as seen above its actual disposition rests with the directors:

Bowers v. Post, 209 Fed. 660,
Hyams v. Old Dominion Copper Co. 82 N.J. Eq. 507
Equitable Life Assurance Co. v. Union Pacific Ry Co.,
212 N.Y. 360;
14 Corpus Juris, 803, and cases there cited.

Furthermore, it is immaterial what may be the amount of such surplus of corporate assets; whatever the surplus may amount to, it is available for dividend purposes. Hyams v. Old Dominion Copper Co. supra.

It has been held specifically that dividends may be paid from surplus accumulated out of the profits of previous years, although there have been no actual profits for the year in which the dividends are paid.

Beers v. Bridgeport Spring Co., 42 Conn. 17
Murray v. Beattie Mfg Co. 7, N.J. Eq. 322, 648
Williams v. Western Union Co., 93 N.Y. 182
Brouty v. Michigan etc. Ry Co., 4 T. & C. 230 (N.Y.)

The authorities cited above clearly confirm the right, which as heretofore stated is customarily exercised by banks, to pay dividends out of its funds of "undivided profits", without regard to the amount of the earnings for the years in which the dividends are paid. The authorities are not controlling upon the right of banks to pay dividends out of their “surplus” funds, because the surplus fund of a bank is peculiar to this special type of corporation. Corporations other than banks and banking institutions are not as a general rule required to set aside any part of the their earnings into special “surplus” funds distinct from “undivided profits”, nor is it their practice to do so, and the surplus of a corporation other than a bank consists of the entire excess of assets over liabilities and capital stock. On the other hand it is universally true, so far as I am aware, that banks in this country are required by their charter or the statutes under which they operate to set aside a certain proportion of their current earnings into a fund designated surplus, until such fund amounts to a certain percentage of the bank’s capital, and in speaking of the surplus of a bank this specific fund is referred to, not including any undivided profits that may represent further excess of assets over liabilities and capital stock.

For this reason banks stand upon a somewhat different basis as regards surplus than do other corporations, but the general rule is nevertheless applicable to banks as well as to other corporations that unless controlled by statue, charter or otherwise, questions relating to the payment of dividends out of the excess of assets over liabilities and capital stock are left to the discretion of the directors. See in re Heaton, 89 Vt. 550, holding that in the absence of any prohibition by charter or otherwise a bank may declare a stock dividend payment out of surplus. See also Morse on Banks and Banking, 5th Ed. Sec. 66.

Unless, therefore, some prohibition is expressed in or implied from the charter of a bank or the statues to which it is subject, the bank may pay dividends out of surplus at the discretion of the directors. Applying this rule to the case now under consideration, I am of the opinion that there is nothing in Section 7 or any other part of the Federal Reserve Act which can reasonably be construed as a prohibition against the payment of dividends out of the surplus of a Federal reserve bank, but on the contrary that, for the reasons stated in the early part of this opinion, in order to give a reasonable and consistent purpose to the express provisions of the law, it is necessary to conclude that the law authorizes the payment of dividends out of surplus.

In considering the question of the right of a Federal reserve bank to pay dividends out of surplus, it is natural to look at the provisions of the National Bank Act, and to determine, if possible, what is the right of a national bank in this respect. The relevant provisions of the National Bank Act are contained in Sections 5199 and 5204 of the Revised Statutes of the United States. These sections provide as follows:

> “Sec. 5199. The directors of any association may semiannually, declare a dividend of so much of the net profits of the association as they shall judge expedient; but each association shall before the declaration of a dividend, carry onetenth part of its net profits of the preceding half year to its surplus fund until the same shall amount to twenty per centum of its capital stock.”
>
> “Sec. 5204. No association, of any member thereof, shall during the year it shall continue its banking operations, withdraw, or permit to be withdrawn, either in the form of dividends or otherwise, any portion of its capital. If losses have at any time been sustained by any such association, equal to or exceeding its undivided profits then on hand, no dividend shall be made; and no dividend shall ever be made by any association, while it continues its banking operations, to an amount greater than its net profits then on hand, deducting therefrom its losses and bad debts.”

There do not appear to have been any court cases construing these sections with reference to the right of national banks to pay dividends out of surplus, but the office of the Comptroller of the Currency has always construed them as prohibiting the payment of dividends from any surplus not in excess of 20 percent of capital, but as permitting the transfer of any surplus above 20 percent of capital to undivided profits and the payment of dividends out of the fund thus transferred. Thus, in spite of the express prohibition of Sections 5204 that "no dividend shall ever be made by any association, while it continues its banking operations, to an amount greater than its net profits then on hand, deducting therefrom its losses and bad debts", the surplus fund of a national bank in excess of 20 percent of capital may be used for the purpose of paying dividends, provided only, that the bookkeeping operation is first preformed of making a transfer from surplus to undivided profits; and if it were not for this express prohibition it would seem that dividends could be paid directly out of surplus. There is no express prohibition against the payment of dividends by Federal reserve banks from any sources, and in so far as the Comptroller's construction of Sections 5199 and 5204 of the Revised Statues has any bearing upon the question now under consideration, it tends to confirm the right of a Federal reserve bank to pay dividends out of surplus.

National banks are not expressly prohibited from transferring surplus to undivided profits even when by so doing surplus is reduced to less than 20 percent of capital, or from declaring dividends out of the funds thus transferred; and it may be argued that the office of the Comptroller of the Currency in implying such prohibitions from the express provisions of the sections 5199 and 5204 of the Revised Statues has recognized that a surplus fund, which is required by statute to be accumulated, is for the exclusive purpose of paying possible losses and should not be used for the payment of dividends, and that this principle should be applied in construing Section 7 of the Federal Reserve Act. In my opinion, however, this argument is not sound, because national banks and Federal reserve banks stand upon very different ground as to the payment of dividends and accumulation of surplus.

With respect to national banks, (1) there is no limit as to the size of the dividends that may be paid out of the earnings not carried to surplus, (2) at least 10 percent of all earnings, no matter how small, must be paid into surplus until a surplus equal to 20 percent of capital has been accumulated, and (3) after a surplus of 20 percent of capital has been accumulated no further payments into surplus are required. On the other hand, with respect to Federal reserve banks, (1) dividends are absolutely limited to six percent per annum, (2) no payments can be made into surplus until stockholders have been paid the full amount of the current cumulative six percent dividends, and (3) no matter how large a surplus may have been accumulated out of past earnings it is still mandatory upon the bank to continue making additions to such fund out of future earnings in excess of dividend requirements.

In order to give any effect to the provisions of Section 5199 of the Revised Statutes it is necessary to construe them as prohibiting a national bank from paying dividends out of its surplus fund not in excess of 20 percent of capital, because otherwise the bank could, as fast as it put funds into surplus, pay them out again as dividends, and thus never accumulate any surplus at all, no matter how large its earnings may be. There can be no doubt, therefore, that the office of the Comptroller of the Currency is correct in construing Sections 5199 and 5204 of the Revised Statues as prohibiting a national bank, either directly or indirectly, from paying dividends out of its 20 percent surplus fund, the accumulation of which, on the one hand, need be commenced as soon as the bank makes any earnings at all, and, on the other hand, must not be continued after the fund amounts to 20 percent of capital. It does not follow, however, that a similar prohibition is to be implied with respect to the surplus of a Federal reserve bank, the accumulation of which, on the one hand, cannot begin until all current and past cumulative six percent dividends have been paid, and on the other hand, must continue without limit as to the ultimate size out of earnings in excess of dividend requirements.

The conclusion might be reached that a Federal reserve bank may pay dividends out of a surplus in excess of 100 percent of subscribed capital, but may not pay dividends out of surplus not in excess of this amount. I am of the opinion, however, that this conclusion is not warranted under the terms of Section 7 of the Federal Reserve Act. There is no minimum surplus for a Federal reserve bank, as there is for a national bank. It is just as mandatory upon a Federal reserve bank, after it has accumulated a surplus of 100 percent of subscribed capital, to pay into surplus 10 percent of earnings over and above dividend requirements, as it is to pay into surplus 100 percent of such earnings prior to such accumulation. All of a Federal reserve bank's surplus is required surplus, and while it might have been reasonable for Congress to make such a distinction between surplus above and below 100 percent of subscribed capital, I believe that no such distinction was made or would be justified under the terms of the existing law.

As heretofore indicated my conclusion is that a Federal reserve bank, which has accumulated a surplus fund, has legal authority, under the provisions of Section 7 of the Federal Reserve Act, to pay out of such fund to its stockholding member banks dividends for a year in which the current earnings of the Federal reserve bank are insufficient for this purpose.

Respectfully,

General Counsel
OFFICE OF THE ATTORNEY GENERAL
WASHINGTON, D.C.
April 27, 1922.

The Honorable,
The Secretary of the Treasury.

Sir:

I am in receipt of your letter of the 11th instant relative to the right of a Federal Reserve Bank which has already accumulated a surplus fund to use such fund to pay its regular dividends at the rate of 6 (cents) per annum on paid-in capital stock when its current earnings are insufficient for that purpose. You transmit a copy of an opinion rendered by the General Counsel of the Federal Reserve Board and request to be advised whether the conclusion reached by the General Counsel is concurred in by this Department.

The Federal Reserve Banks are creatures of statute and the rights of such banks must be determined by the statutes creating and governing them. The statutory provisions pertinent to the inquiry are found in section 7 of the Federal Reserve act of December 23, 1913, c. 6, 38 Stat. 258, as amended by section 1 of the Act of March 3, 1919, c. 101, 40 Stat. 1314, which reads in part:

> "After all necessary expenses of a Federal reserve bank have been paid or provided for, the stockholders shall be entitled to receive an annual dividend of six per centum on he paid-in capital stock, which dividend shall be cumulative. After the aforesaid dividend claims have been fully met, the net earnings shall be paid to the United States as a franchise tax, except that the whole of such net earnings, including those for the year ending December thirty-first, nineteen hundred and eighteen, shall be paid into a surplus fund until it shall amount to one hundred per centum of the subscribed capital stock of such bank, and that thereafter ten per centum of such net earnings shall be paid into the surplus.
>
> "...Should a Federal reserve bank be dissolved or go into liquidation, any surplus remaining, after the payment of all debts, dividend requirements as hereinbefore

> provided, and the par value of the stock, shall be paid to and became the property of the United States and shall be similarly applied."

In constructing this statute the purpose is to ascertain the legislative intent. From the language used in the above quoted section, it seems reasonably clear the Congress intended that the dividend of 6 cents per annum on the paid-in capital stock should be considered a charge on the gross earnings of the bank, the same as necessary expenses and the dividend requirements shall any amount be considered "net earnings" to be carried, to the surplus fund.

It is also evident that the Congress, in providing that the net earnings after payment of expenses and dividends, shall be carried, to the surplus fund until such surplus fund "shall amount to one hundred per centum of the subscribed capital stock," intended to provide an adequate surplus fund for the protection of the bank and its stockholders, in order that fixed charges might be paid therefrom, should losses or other exigencies diminish the earnings in any year. In doing this the Congress put into the statute a provision dictated by good business management and followed the practice generally obtaining in well managed banking and other corporations.

While the statute makes no guaranty of the payment of dividends at the rate of 6 on the paid-in capital stock, yet the surplus fund built up from the net earnings, after payment of necessary expenses and dividend requirements in prosperous years, stands as a virtual guaranty to stockholders against failure of dividends in lean years, thereby enhancing confidence in the bank's financial stability.

That the surplus fund is liable for unearned dividends is further shown by the last-quoted paragraph of section 7, which provides that upon liquidation of the bank the surplus fund, after payment of all debts and dividend requirements and the par value of the took, shall be paid to and become the property of the United States. This provision indicates that the dividend requirements are not only a charge upon the gross earnings, but that where the gross earnings are not sufficient to meet the necessary expenses, debts and dividend requirements, such expenses, debts, and dividend requirements become a charge upon the surplus fund and must be paid out of that fund before any amount can be paid to and become the property of the United States.

I, therefore, concur in the conclusion reached by the General Counsel of the Federal Reserve Board, that -

> "A Federal reserve bank, which has accumulated a surplus fund, has legal authority, under the provisions of Section 7 of the Federal Reserve Act, to pay out of such fund, to its stockholding member banks dividends for a year in which the current earnings of the Federal reserve bank are insufficient for this purpose."

Respectfully,

(Sgd) H.M. Daugherty
Attorney General

C FR 34 Accounts

Closed Accounts

Account Name	Account Numbers	Description
Consolidated Maiden Lane II LLC Asset Accounts	(142-025, 142-050, 142-075, 142-100)	Maiden II LLC closed on November 12, 2014.
Consolidated Maiden Lane LLC Asset Accounts	(145-025, 145-030, 145-035)	Maiden Lane LLC closed November 1, 2018.
Consolidated Commercial Paper Funding Facility LLC Accounts	(145-055)	The 2009 Commercial Paper Funding Facility was closed on February 1, 2010.
Commercial Paper Funding Facility II LLC Accounts	(145-060, 145-065, 145-070)	CPFF II was terminated on July 8, 2021.
Consolidated Money Market Investor Funding Facility LLCs Accounts	(145-100, 145-115, 145-130, 145-145, 145-160)	The Money Market Investor Funding Facility was never used and was discontinued on October 30, 2009.
Consolidated Maiden Lane III LLC Asset Accounts	(145-200, 145-215, 145-230, 145-245)	Maiden III LLC closed on November 12, 2014.
AIG Allowance for Loan Modification	(145-345)	As a result of the closing of the AIG recapitalization plan on January 14, 2011, the revolving credit facility was fully repaid.
AIG Loan and Capitalized Interest	(145-375)	As a result of the closing of the AIG recapitalization plan on January 14, 2011, the revolving credit facility was fully repaid.
Term Asset-Backed Securities Loan Facility Account	(145-475)	Account closed effective July 2022.
Term Asset-Backed Securities Loan Facility Accounts	(145-500, 145-545, 145-560)	The 2009 TALF LLC closed on November 26, 2014.
Corporate Credit Facilities—Primary Market Corporate Credit Facility Accounts	(145-630, 145-631, 145-632)	CCF was terminated on December 17, 2021.

(continued on next page)

Closed Accounts—*continued*

Account Name	Account Numbers	Description
Corporate Credit Facilities—Secondary Market Corporate Credit Facility Accounts	(145-645, 145-646, 145-647)	CCF was terminated on December 17, 2021.
AIG Preferred Securities	(145-830, 145-845, 145-860, 145-875)	As a result of the closing of the AIG recapitalization plan on January 14, 2011, the New York Reserve Bank has been paid in full for its preferred interests.
Building Machinery and Equipment	(160-075)	Account closed effective January 1, 2021, with all remaining assets reclassed to Furniture & Equipment (170-025).
Furniture and Equipment—Depreciation	(170-050)	Account closed effective July 1, 2021, with all remaining assets reclassed to Furniture & Equipment (160-125)
Furniture and Equipment, Net	(170-060)	Account closed effective July 1, 2021.
Securities Borrowing	(170-500)	The securities borrowing facility was terminated on December 12, 2008, and all outstanding balances under that facility were repaid in full.
Branches or Head Office—Interoffice Account	(190-025)	In 2014, the accounting for all Branch offices was consolidated to each District's head office; therefore, Branch balance sheets are no longer prepared.
Other Offices Own District	(230-025)	In 2014, the accounting for all Branch offices was consolidated to each District's head office; therefore, Branch balance sheets are no longer prepared.
Earning Credits Due to Depository Institutions	(240-175)	In July 2012, the earning credits program was eliminated and all remaining earning credits expired by July 2013.
Consolidated Maiden Lane LLC Liability Accounts	(240-400, 240-425)	Maiden Lane LLC closed November 1, 2018.
Consolidated Maiden II LLC Liability Accounts	(240-435, 240-440)	Maiden II LLC closed on November 12, 2014.
Consolidated Money Market Investor Funding Facility LLCs Liability Accounts	(240-450, 240-455)	The Money Market Investor Funding Facility was never used and was discontinued on October 30, 2009.
Consolidated Maiden III LLC Liability Accounts	(240-460, 240-465)	Maiden III LLC closed on November 12, 2014.
Accumulated proceeds—AIG	(240–470)	As a result of the closing of the AIG recapitalization plan on January 14, 2011, the revolving credit facility was fully repaid.
Branches or Head Office—Interoffice Account	(240–825)	In 2014, the accounting for all Branch offices was consolidated to each District's head office; therefore, Branch balance sheets are no longer prepared.

(continued on next page)

Closed Accounts—*continued*

Account Name	Account Numbers	Description
TALF Liability	(240-930, 240-940, 240-960)	The 2009 TALF LLC closed on November 26, 2014.
Cost of Earning Credits	(330-075)	In July 2012, the earning credits program was eliminated and all remaining earning credits expired by July 2013.
Assessments by Board of Governors—Office of Financial Research	(330-140)	Reserve Banks are no longer required to fund operations of the Office of Financial Research in 2014.

Note: The detailed accounting guidance related to these facilities or accounts has been removed from FAM.

Expansion Accounts

Account Name	Account Numbers
Total Assets	145-075, 145-175, 145-615, 145-715, 145-730, 145-745, 145-760, 145-775, 145-800, 145-815
Other Assets	170-550, 170-560, 170-570, 170-580, 170-590
Other Liabilities	240-445, 240-480, 240-485
Total Liabilities	242-160, 242-180, 242-200, 242-220, 242-240
Current Net Income	330-082, 330-085
Board Assessments	330-130

Note: These asset and liability accounts are reserved for future use. Reserve Banks are required to report zero balances in these expansion accounts.

D Software

D.1 Accounting Guidance for Internal Use Software and Cloud Computing Arrangements

The following accounting guidance is provided to assist System financial accounting staff in determining the appropriate accounting treatment for internal use software, whether it is purchased from a vendor, internally developed, or significantly modified for use by the Federal Reserve Banks.[1] This guidance will also be used for recording charges associated with a cloud computing arrangement containing a software license element, if certain conditions are met and for the recognition of implementation costs associated with a cloud computing arrangement that does not contain a software license element. This information expands on the requirements in the Financial Accounting Manual (FAM)'s Chapters 1 (Section 4.21) and 3 (Sections 30.72, 30.78, 30.80, and 30.95) and further highlights the underlying accounting principles that relate to software assets and expenses.[2] The accounting treatment of costs incurred to purchase or develop internal use software is influenced by the intangible nature of the resulting assets, and the accounting recognition requirements are frequently different than those for tangible assets.

The costs incurred to develop, purchase, and install software must be carefully analyzed and independently evaluated to establish the proper accounting treatment based on all the relevant factors. The discussion that follows will assist those performing the analysis in using a uniform analytical approach when evaluating the events and related information associated with software development efforts to promote consistency in accounting treatment for like transactions.

In April 2018, the Reserve Banks adopted the Program and Project Management (PPM) Standard, which integrates the prior Technology Project Standard, Enterprise Program Standard, Business Case Justification Standard, Technology Project Management Standard, Software Development Framework, Application Development Estimation Framework, and Requirements Engineering Framework (REF). The single PPM Standard is aligned with industry-based standards and incorporates all aforementioned standards and frameworks. The PPM Standard is organized into three stages: Stage 1: Justification, Stage 2: Planning and Execution, and Stage 3: Transition and Closing.

Integral to performing a thorough analysis and determining the proper accounting treatment for software costs is having the requisite information about the contracts, agreements, and circumstances so that the derived accounting treatment is correct.

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1 This appendix is based on a memo issued by RBOPS FRB Financial Accounting Section on December 27, 2007.

2 As background, information in the FASB ASC Topic 350-40 was reviewed. The accounting principles are: the tangible object or intangible right has economic value to its owners, has continuing benefits for future periods, and can be expressed in terms of its costs; and that costs are matched with the accounting periods that the costs benefit.

This requires that an accounting staff member communicates with business areas and other affected Reserve Banks' accounting departments and vice versa to discuss all the relevant information, including cost data needed to establish the proper accounting for software assets. In cases where software development costs are related to System initiatives, the product and function offices likely will be part of the communications and will have additional relevant information that is needed to determine the proper accounting treatment for internal use software.

Board staff may also be consulted for assistance in the decision making process and considering the implications for financial reporting, or with emerging arrangements that are not addressed in this document. In certain situations, which are identified later, RBOPS Financial Accounting Policy and Reporting Section staff must be contacted for approval of FAM exceptions.

The analysis, conclusions, and rationale for the accounting treatment should be documented.

1. Capitalization thresholds

For an outlay to be capitalized, it should be material in value, which, for purposes of recognizing assets, is defined as equal to or greater than established capitalization thresholds. For software assets, the thresholds are $100,000 or more for internally developed software and implementation costs for cloud computing arrangements that does not contain a software license and $25,000 or more for externally purchased software. These thresholds are discussed in FAM Chapter 1, section 4.20 (Deferred Charges). The capitalization threshold for externally purchased software was lowered in 2005 to make this threshold consistent with other prepaid license fees. For internally developed software, information referenced in sections 3, 4, and 6 further explain what costs are to be capitalized and how to evaluate the asset unit.

2. Ownership of software

Every asset is an asset of some entity and that entity must control future economic benefits and regulate access to the benefit. The contract is usually the primary source for information about ownership. Contracts and agreements usually indicate who will have future economic benefit, and specify who has which legal rights, which enables determining ownership. Absent contracts or agreements that indicate ownership or rights, software ownership is determined by several factors that indicate control such as:

- The entity makes decisions about the software, including but not limited to defining requirements, and establishing implementation and decommission dates.
- The entity operates and provides daily support for the software.
- The entity controls granting rights to use the software.

In the Federal Reserve System, there is a designated entity, such as a Central Business Administrative Function (CBAF), Product Office, or Function Office that controls a software asset, thus the asset would be recorded on the books of the Reserve Bank hosting this entity or, absent the entity, the Reserve Bank that exercises this control over the asset, regardless of physical location of the software. The software may be installed on another Reserve Bank's hardware, a hardware platform that is operated by a third party vendor that was contracted for by a Reserve Bank, or an outside party's hardware.

As a result, software development may occur at one Reserve Bank, the software may be installed on hardware at another Reserve Bank, and a third Reserve Bank, hosting a CBAF for example, may control the software asset.

Software developed for release to an outside party that will be controlled by the outside party (the above ownership factors are met) is not considered internal use software and should be expensed as development occurs. This includes instances when FRB staff makes further modifications to the software at the request of the outside party, but then releases the modifications for support and operation by that third party.

3. Definition of the asset unit for software

The developed or purchased software (purchased software includes acquisition cost, as well as installation/integration costs) that provides economic benefit and otherwise qualifies to be capitalized is recorded as a single asset. When software development occurs over several years, however, and the software will be implemented in phases as elements, each element (a component or module) should be analyzed to determine whether it should be treated as a separate asset. Specifically, the element should provide economic benefit through distinct, substantive functionality; and meet the tests for materiality, ownership, and eligibility for capital treatment. If all the criteria are met, the element should be treated as a separate asset with a unique useful life determined from the analysis performed for section 9 and placed in service when substantially complete and ready for its intended use.

When the majority of elements associated with a long term software development project are treated as separate software assets, but an element costs less than $100,000, the accounting treatment for this element should be discussed with Board staff.

When identical software that is acquired is a bulk purchase of a number of low cost licenses that are licensed per server (for example software to be placed on many servers) or per user and individually are below the capitalization threshold, the bulk purchase can be capitalized as a single asset when it is material in value, that is $100,000 or more, and the license term is longer than one year.[3] A subsequent purchase of the same software that is acquired under the same contract (quantity not originally specified or ‘up to quantity’ is specified) and that does not meet the $100,000 threshold should be charged to current expense.[4] Standard desktop utility software (such as word processing, electronic mail, and anti-virus software) and maintenance should be charged to current expense regardless of amount.

4. Cloud Computing arrangements

Cloud computing arrangements are hosting arrangements in which the customer of the software does not take possession of the software, but instead accesses and uses the software on an as-needed basis or by subscription. A customer that acquires a software license—including in a hosting arrangement that transfers a software license to the customer—recognizes an intangible asset (i.e., the software license) and a corresponding liability to pay for it over time (unless the license is prepaid).

As such, the Reserve Bank will record charges associated with a cloud computing arrangement containing a software license element if both the following conditions are met:

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[3] The $100,000 threshold is not related to the threshold for internally developed software, but is an amount that is deemed a significant or material enough bulk purchase to warrant capitalization.

[4] Some contracts are open ended or may include subsequent orders. If a subsequent purchase does not satisfy the threshold, it would be expensed.

- The Reserve Bank has the contractual right to take possession of the software at any time during the hosting period without significant penalty,[5] and
- It is feasible for the Reserve Bank to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software.

If the arrangement contains a software license, Reserve Banks should account for the fees related to the software license element in a manner consistent with the acquisition of a software license. If the arrangement does not contain a software license, Reserve Banks should account for the arrangement as a service contract—typically by amortizing the service cost over the expected service period.

Certain cloud computing arrangements may have multiple elements such as implementation, set up, training, and data conversion costs in addition to license and service elements. All expenses should be carefully evaluated for capitalization purposes. Appendix D should be reviewed for guidance for costs including those resulting from training, data capture, and conversion activities.

Capitalized implementation costs for an arrangement that does not contain a software license should be amortized on a straight-line basis over the fixed non-cancellable term of the hosting arrangement.[6]

5. Improvements to existing software

Expenditures made to change existing software assets are considered either improvements or maintenance. Expenditures to existing software assets that meet the capitalization thresholds outlined in section 1 should be capitalized if the resulting improvement provides additional capabilities by meeting one of the following criteria:

- the quantity of output or operating efficiency of the asset is significantly increased, and
- the quality of output is significantly increased.

Improvements add functionality that the software previously did not have, incorporate new specifications, or involve a significant change to the original specifications and are typically termed releases or versions. Improvements should be recorded as separate assets with a unique useful life determined from the analysis performed for section 9. Costs incurred for maintenance such as fixes, patches, or updates such as increasing the field width, adding a comment field, and reformatting or adding reports are expensed.

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[5] The term "without significant penalty" contains two distinct concepts: (1) the ability to take delivery of the software without incurring significant cost, and (2) the ability to use the software separately without a significant diminution in utility or value.

[6] In some instances, the Reserve Bank contracting the implementation arrangement may not also contract the hosting arrangement, i.e. the hosting arrangement is contracted by another Reserve Bank. In such cases, analysis from a control perspective (similar to section 2. Ownership of Software) would need to be exercised as to which Reserve Bank should capitalize the associated implementation costs of the cloud-based arrangement. In cases where the Reserve Bank capitalizing implementation costs does not contract the hosting arrangement, the Reserve Bank should ensure it is able to ensure contractual rights through the Reserve Bank contracting the hosting arrangement. The fixed non-cancellable term includes optional periods that the Reserve Bank is reasonably certain to exercise; termination options that the Reserve Bank is reasonably certain not to exercise; and extension or termination options controlled by the vendor.

The following table provides examples of expenditures and how they would be classified:

Capital	Expense
Augmenting existing business functions with new features and functions	Updating of flags and thresholds
Building completely new business functions	Updating field lengths and comment fields
Creating new screens and reports for new features or business functions[1]	Reformatting of reports including the inclusion/exclusion of existing data fields
Converting to a new platform, include converting to the cloud environment (mainframe to distributed platform; see section 6)[2]	Modifying layout of screens
Building a new interface	Changes to facilitate a new operating system version (Windows XP to Windows Vista) Installing fixes and patches

[1] Initial or upgrade work performed during the development phase should be capitalized. Similar work performed during the post-implementation phase should be expensed.

[2] For the conversion to be considered capital, it needs to meet the capitalization criteria in section 5, Improvements to existing software.

A specific software development project may include expenditures for improvements and maintenance that cannot be easily separated. One approach that can be used to separate these costs is a ratio that is based on the projected work hours for development activities for each type of work. Such a ratio can be applied to the development costs to determine the percentage of expenditures that should be capitalized. The basis for allocating costs should be defensible.

6. Replacement of existing software

A replacement is a substitution of the existing asset with a new asset. When the results of efforts to rewrite or improve the software are significant enough to be considered a replacement to the existing software and the expenditures meet the criteria in sections 1, 2, and 5, the costs are capitalized. Conversion of an application from a mainframe to a distributed platform is generally considered a replacement. Even though the application's functionality may not have changed, a significant alteration of the software occurs. The software code is converted to a different programming language, different operating systems and technologies are used, and different tools are used to manage the application.[7] Because the former software asset is significantly altered, the net book value of the former software asset is removed from the books and expensed. The useful life of the replacement, therefore, should be unique based on the analysis performed using section 9.

In addition, if there is a replacement of an element of existing software and the expenditures meet the criteria in sections 1, 2, and 5, then the former element, if previously treated as a separate asset, is removed from the books and expensed. The new element would be capitalized in accordance with section 5.

[7] The above describes the porting of the application software; another approach is hosting, whereby a distributed platform is used to emulate the mainframe so that the mainframe application software can be used without recoding; such an approach would likely not be treated as a replacement.

When the former software asset is replaced by new software whose costs do not meet the capitalization threshold and are expensed, the net book value of the former asset is removed from the books and also expensed.

7. Capitalizable costs

Costs incurred during software development or implementation of a cloud computing arrangement are capitalized or expensed depending on the project stage. These stages are commonly described as preliminary, development, and post-implementation.

The *preliminary stage* includes activities related to

- the conceptual formulation of alternatives
- the evaluation of alternatives
- the determination of existence of needed technology
- the final selection of alternatives
- the selection of vendors and consultants
- and the prototype or proof of concept.

Capitalized: None

Expensed: All costs associated with preliminary stage activities.

The *development stage* includes all the activities related to designing the chosen path including configuration and software interfaces, coding, testing (to include all testing prior to user acceptance testing), installation of software on hardware, preparation of code to convert old data, and development of user guides.

Capitalized:

- external costs of materials and services (for example, consulting fees), salary and retirement and other benefit costs of employees directly associated with the project as outlined in section 8
- preparation of developer guides
- costs associated with time spent specifically to oversee developers (programmers), if determinable
- expenditures for integration materials and services, which include consultant fees and salary and retirement and other benefit costs of employees directly associated with the integration effort. Integration efforts include customizing the infrastructure/operating system software so that the developed application will operate on the infrastructure hardware and within existing network environments. (In some cases integration costs may involve the components, installation, and related interconnectivity of hardware, which may require the allocation of integration costs between hardware and software.)
- travel costs for staff, consultants, or vendors should be capitalized if directly related to the software development and, when required, in conformance with applicable Bank travel policies or contract requirements for consultants and vendors
- implementation costs associated with activities to integrate, configure and/or customize a hosted cloud computing arrangement service
- cost of testing necessary to accept the developed application or validate that the application satisfies the business requirements. (example: functional testing or non-functional testing such as business continuity, capacity, availability, and security)

Expensed:

- general and administrative costs
- parallel testing and parallel processing[8]
- end-user testing
- end-user training
- actual purging, cleansing, and conversion of historical data
- FISMA certification
- cost of testing performed in conjunction with fixes, or periodically performed to ensure the continued integrity and maintenance of the application. (Examples are penetration testing and contingency testing.)

The *post-implementation stage* includes activities such as maintenance to fix problems and training of internal and external users.

Capitalized: Software maintenance contracts that are executed when the software is installed should be capitalized and treated as prepaid expenses or deferred charges in instances when the contract terms indicate a longer maintenance period and costs exceed the FAM thresholds for prepaids and deferred charges. Likewise, software maintenance contracts executed for bulk purchases that exceed FAM thresholds should be capitalized and amortized over the current and prospective periods that benefit from the expenditure.

Expensed: All the costs associated with post-implementation stage activities except maintenance costs as described above. This includes integration costs to reinstall existing software on new hardware.

Purchased software may include costs for multiple services such as training and maintenance in addition to the software license. Because maintenance costs may be capitalized if costs exceed the FAM thresholds for prepaids and deferreds and training costs are expensed, the costs should be allocated among these services based on the value of the services. Vendors may have information that can be provided to assist in determining the costs of these services. The basis for allocation should be defensible.

Because development of internal-use software may not follow the order as stated above (for example, coding and testing are often performed iteratively, or an Agile methodology is used) the accounting treatment should be based on the nature of the costs incurred, not the timing of their occurrence.

8. Software development labor rates

Internally developed software costs that meet the FAM threshold should be capitalized using actual salaries and/or outside agency help (OAH) rate(s).[9] If actual costs are not readily determinable, a Reserve Bank may use either a blended or two-rate approach. Reserve Banks may use different rates based on varying skillsets, salary differentials,

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8 Parallel testing related activities are generally performed by the end-user and take place when the internally developed system is deemed functionally complete. Parallel processing related activities take place when the newly internally developed system is designated as the “system of record” and runs in parallel with the system that has been replaced (designated as the legacy system).

9 Federal Reserve System users should reference the Reserve Banks’ FAM SharePoint site for detailed procedures.

or project structures within a cost pool to help reduce the risk of distorting assets. The rate (blended or two-rate) that a Reserve Bank chooses to use should be consistently applied for all District assets.

Rates should be calculated based on budgeted annual employee salaries (including all types of variable compensation) and budgeted benefit costs, and/or the budgeted annual OAH costs divided by the total applicable annual work hours (AWH). The rates should be adjusted to account for employee turnover, organizational changes, or changes in retirement and other benefits (ROB) rates that have occurred since final budget submission.

Two-rate approach:

$$\frac{\text{[Total budgeted employee salary and ROB]}}{\text{[Total employee AWH hours]}}\text{, and/or}$$

$$\frac{\text{[Total budgeted annual OAH costs]}}{\text{[Total annual budgeted OAH hours]}}$$

Blended-rate approach:

$$\frac{\text{[Total budgeted employee salary and ROB + Total budgeted annual OAH costs]}}{\text{[Total employee AWH hours + Total budgeted OAH hours]}}$$

9. Assigning a useful life to the software asset

The estimated useful life over which the costs will be amortized should reflect the circumstances for that specific asset. The circumstances to consider include the type of software (for example, operating software, application software) and the effects of obsolescence, technology, competition, immediate- and long-term plans, and other economic factors should be considered. For example, rapid changes in the availability of alternative software solutions or hardware technology (on which the software will operate) would contribute to a shorter expected useful life. Consultation with the outside party (when appropriate), the product or function office, business areas, other Reserve Banks, and Board staff may be necessary in order to determine the appropriate useful life and should reflect the circumstances for that specific asset. While FAM sets the maximum useful life that should be assigned to any software asset at five years, in unusual situations, a request to establish a longer life may be submitted for Board staff approval. The rationale for any adopted useful life should be defensible.

Each element (a component or module) or improvement should be recorded separately from the underlying software asset and assigned a unique useful life, not to exceed five years. In some cases, the separately recorded element or improvement may be assigned a useful life that ends co-terminously with the underlying software asset if the analysis warrants such treatment. For example, an element or improvement may be recorded separately, but be amortized co-terminously with the original asset because it is known that the software will be decommissioned at a specific future date.

10. Amortization of software

A software asset is amortized over its useful life. For each element or improvement, amortization should begin when the software is ready for its intended use (after all substantial testing is completed and not necessarily when it is placed in production). If the functionality of an element is entirely dependent on the completion of another element, amortization should begin when the functionality of both elements are ready for their intended use.

11. Regular evaluation of assigned useful lives

At a minimum, each Bank should assess annually the useful lives of software. Each Bank should also assess annually the amortization periods assigned to implementation costs for a cloud computing arrangement that does not contain a software license. If there is a need to change the useful life or amortization period due to the effects of obsolescence, technology, and other economic factors, then revisions are made prospectively. As such, the current net book value is amortized over the revised remaining useful life. In cases where this analysis results in an extension of a useful life for software, the extension should not exceed the maximum allowed by FAM, which is five years. In unusual situations, a request to establish a longer life may be submitted for Board staff approval.

12. Impairment and write-off of software development costs or software assets

Significant events or changes in operating circumstances warrant a review to determine whether the carrying value of an existing software asset or capitalized implementation costs for a cloud computing arrangement that does not contain a software license is not recoverable and should be impaired. Tests should be performed consistent with FAM, Chapter 3, section 30.95 (Asset Impairment) and Board staff should be contacted for approval. In the case of software applications developed for Treasury, no impairment typically results because all costs including those associated with software are generally recoverable from the Treasury. The need for a change in estimated useful life, however, should be considered.

Impairment is applicable, for example, when one of the following events or changes in circumstances occurs related to the software being developed or currently in use indicating that the carrying amount may not be recoverable according to ASC Topic 350-40:

- Internal-use computer software or the cloud computing arrangement is not expected to provide substantive service potential.
- A significant change occurs in the extent or manner in which the software or the cloud computing arrangement is used or is expected to be used.
- A significant change is made or will be made to the software program or the cloud computing arrangement.
- Costs of developing or modifying the internal-use computer software significantly exceed the amount originally expected to develop or modify the software.

When it is no longer probable that a software project will be completed, no further costs should be capitalized and any costs that have been capitalized should be written off. Any expected recovery of accumulated costs from third parties, including the U.S. Treasury, should be considered in the write off. Indications that the software may no longer be completed include:

- the lack of commitments to fund further development
- the discontinuance of the business segment the software was designed for
- the inability to resolve programming difficulties timely
- significant cost overruns

- or a decision to obtain third-party software instead and abandon the current software development.

13. Unusual situations

Categorization of some software development may not be as readily ascertainable from the above guidance and may require more analysis and review with the product or support office, business area, and Board staff to determine whether the software costs should be capitalized or expensed.

14. Software Standard Task Description List

Reserve Bank initiatives with a software component must comply with the PPM Standard. The PPM Standard also applies to any Reserve Bank technology initiative, including software development, purchased software (vendor-developed/purchased software applications), infrastructure, and service. Reserve Bank users should reference the standard task list description when determining capitalization or expense classifications for software development or purchased software initiative activities. The standard task list description is found on the Reserve Banks’ FAM SharePoint site.

E Reserved

F Pension

F.1 Employer Accounting for the Retirement Plan for the Employees of the Federal Reserve System and the Consumer Financial Protection Bureau

The purpose of this memorandum is to document the considerations and conclusions relevant to determining how the Federal Reserve's financial statements should reflect the employer accounting for the Retirement Plan for Employees of the Federal Reserve System (System Plan). The System Plan is a defined benefit pension plan that covers employees of the 12 Federal Reserve Banks (Banks), the Board of Governors (BOG), and the Consumer Financial Protection Bureau (CFPB). The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) allows CFPB employees to participate in the System Plan.[1]

The System employers account for their pension obligations in a manner consistent with GAAP. In accordance with FASB ASC Topic 715-30, employer accounting for pension benefits reflects the employer's financial interest for providing pension benefits net of assets held in separate pension entities. Because the System Plan provides for the payment of benefits to retirees from the assets of the plan without regard to the source of the funding, each employer's interest in the plan could not be computed and accounted for as separate financial positions. Instead, each employer's position is computed at a System level and reported on the financial statements of one Reserve Bank. We believe this treatment is the most appropriate and consistent with the intent of GAAP. This interpretation, however, is not clearly contemplated by the applicable accounting standards in that it arises from the unique structure of the Federal Reserve System. That is, the System employers are legally independent and not commonly owned and controlled, yet cooperate financially in the provision of pension benefits in a manner that would not normally exist among independent entities.

The following explains the treatment of the System Plan as a **single** employer plan that was historically reflected on the FRBNY's financial statements, and, effective August 1, 2023, transferred to the Federal Reserve Bank of Atlanta (FRBA) financial statements following the integration of the Office of Employee Benefits of the Federal Reserve System (OEB) into the operations of the FRBA.

Single/Multi-employer Accounting

Much of the authoritative accounting literature on employer pension plan accounting focuses on whether the plan is characterized as a single-employer or a multi-employer plan. Essentially, the resources of single employer plans are incorporated into the employer's net pension asset/liability, the resources of multi-employer plans are not. The System Plan has many characteristics of a multi-employer plan, yet the related

[1] CFPB employees may choose to participate in the System plan and, if they do, they receive the same benefits as those offered to Board employees.

nature of its employers leads to the System's conclusion that it should be treated as a single employer plan. The citations/definitions discussed below present definitions of each term from key sources.

1. FASB ASC Topic 715-30:
    - Single-employer plan—A pension plan that is maintained by one employer. The term may also be used to describe a plan that is maintained by related parties such as a parent and its subsidiaries.
    - Multiemployer plan—A pension plan to which two or more unrelated employers contribute, usually pursuant to one or more collective bargaining agreements. A characteristic of multiemployer plans is that assets contributed by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer.
    - Multiple employer plan—A pension plan where two or more unrelated employers contribute or pool their assets for investment purposes and to reduce plan administration costs. The assets contributed by an employer to a multiple-employer plan may not be used to provide benefits to participants of another sponsoring employer in the multiple-employer plan.
2. FASB ASC Topic 960-10 specifies that administration is the most distinguishing characteristic between single employer plans and multiemployer plans. In a single employer plan, the employer is the plan sponsor. Multiemployer plans are normally negotiated and established pursuant to collective bargaining agreements between an associated group of employers, such as those whose employees are represented by a specific union, and the plan sponsor of a multiemployer plan is a joint employer, union committee, or board.
3. FASB ASC Topic 960-10 addresses the reporting-entity question for affiliated not-for-profit entities. The conclusion of this discussion is that "parent" entity within the group may account for a plan as a single employer plan in its financial statement, while all other entities in the group account for the plan as a multiemployer plan.

A distinguishing characteristic of multiemployer plans is that assets contributed by one employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer. In this respect, the System Plan is similar to a multiemployer plan, as the assets are not divisible among the Banks, BOG, and CFPB, and all assets are available for benefits to employees of each entity. Another distinguishing characteristic, however, is the nature of the relationship among the entities whose employees participate in a plan. The multiemployer definitions frequently refer to collective bargaining relationships, implying that the employers are unrelated parties. If the employers are related parties (for example, through equity interest, management control, or financial control), then the plan would generally be considered a single employer plan. When the entities are unrelated parties, the plan would typically be considered a multiemployer plan.

ASC 715-30 defines a multiple-employer plan as one that is maintained by more than one unrelated employer with plan assets that are severable and maintained in separate accounts for each employer even though the assets are pooled together for investment purposes and to reduce administration costs. Separating the assets allows for the participating employers to have different benefit formulas and to reserve each employer's assets to provide benefits to only its respective employee benefits. Under a multiple-employer plan, therefore, each employer accounts for its respective interest in the plan as a single-employer plan, and the net pension asset/liability of all participating employers is not reported. The System plan is not a multiple-employer plan because the invested assets are not maintained in separate accounts.

Although the Banks, BOG, and CFPB are not related through equity or other beneficial ownership, there is strong evidence that they are related parties for plan aggregation purposes. For example,

1. the BOG appoints three members of each Bank's board of directors,
2. effective August 1, 2023, the OEB became an operating unit of the FRBA under its supervision and control with the OEB retaining its oversight committees that are composed of Bank and BOG representatives,
3. the Banks are the sole funding source for the BOG,
4. the BOG and five Bank presidents compose the Federal Open Market Committee, which directs the investments that provide substantially all of the Banks' income,
5. the Banks rely on each other for the provision of various operational and administrative functions,
6. the legal definition of the CFPB in the Dodd-Frank Act designates it as an independent agency established in the Federal Reserve System,[2]
7. the provisions of the Dodd-Frank Act that designates the CFPB as the "same employer as the Federal Reserve System,"[3] and
8. the requirement that the Board fund the operations of the CFPB.

Based on the discussions above, the System Plan most closely resembles a single employer plan with characteristics of a multiemployer plan. Accordingly, the most appropriate treatment would be single plan accounting on the financial statements of the most appropriate employer. In addition, the governance and administration of the System plan is not changed with CFPB employee participation. In addition, the governance and administration of the System plan is not changed with CFPB employee participation. The Dodd-Frank Act specifically states that the CFPB does not have responsibility or authority to make any plan amendments, administer an existing plan, or ensure the System plan complies with applicable laws.[4]

Determining the Reporting Employer

The assets, liabilities, and costs related to the System Plan are recorded by the FRBA effective August 1, 2023. This decision was based on (1) the conclusion that it was appropriate for one entity among the participating employers to report the System Plan, (2) that the System Plan should be reported by a Reserve Bank so that the income/costs associated with the pension benefits would be incorporated into the Reserve Banks' distribution of excess earnings to the U.S. Treasury, and (3) no one individual Reserve Bank exercises control or undue influence over the System Pension plan as the oversight committees govern the plan. In light of these considerations, it is most appropriate for the FRBA to record the System Plan as subsequent to the transition, the FRBA will have ultimate responsibility for the OEB's operational performance in meeting its assigned responsibilities consistent with direction from the oversight committees.

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[2] U.S.C. § 5491(a).

[3] U.S.C. § 5584(i)(1)(C)(v). This statement was included in the act for purposes of subsections (b), (c), (m), and (o) of section 414 of the Internal Revenue Code of 1986 (26 U.S.C. § 414).

[4] U.S.C. § 5584(i)(1)(C)(ii).

Accounting and Disclosure

FASB ASC Topic 715-30 provides guidance on which employer should account for the plan's funded status. A subsidiary that issues separate financial statements may participate in a defined benefit pension or postretirement plan of a parent company. If the parent's plan covers employees of the subsidiary, the subsidiary should account for its participation in its standalone financial statements as a participation in a multi-employer plan if all criteria are met:

- Each subsidiary is required to contribute to the plan based on a predetermined formula.[5]
- Plan assets are not segregated or restricted on a subsidiary-by-subsidiary basis.
- If a subsidiary withdraws from the plan, the benefit obligations for its employees are retained by the parent's plan (as opposed to being allocated to the withdrawing subsidiary).

The participating subsidiary would not recognize an allocation of the plan's funded status (only the plan sponsor should recognize the plan's funded status on its balance sheet). If a subsidiary doesn't meet the above criteria, it should not follow multi-employer plan accounting. The parent (or the ultimate plan sponsor) should account for the plan as a single-employer defined benefit plan in its consolidated financial statements per ASC 715-30-55-64. In applying this guidance, the subsidiaries would be the 11 Reserve Banks who are not reporting the funded status, while the Reserve Bank who does report the funded status would be considered the parent or the ultimate plan sponsor.

While there is no 'parent' or 'subsidiary' entity within the Federal Reserve System, as noted earlier, the FRBA will now be primarily responsible for development of the OEB's operational strategies, operational performance and delivery, provider of shared services, leadership support, and coordination of benefits governance. These may be thought of as parent responsibilities when it comes to pension accounting. Based on the discussion above, the System Plan should be held with the 'ultimate plan sponsor,' which in this instance, most resembles the FRBA.

Funding

System plan employer contributions are currently determined annually at an aggregate level and the employer funding may be allocated among the participating entities on other than a pro rata basis. FRBA makes employer contributions to the System plan on behalf of all Reserve Banks and the Board. Dodd-Frank Act requires that the CFPB contribute funds to the System plan for each CFPB employee participating in the System plan.[6] The contribution formula for CFPB employees electing to participate is based on the Federal Employee Retirement System contribution formula (not on the cost of benefits to be provided to CFPB beneficiaries at retirement).[7] The addition of CFPB employer contributions to the System plan funding will not change the approach to determine overall employer contributions; they will continue to be determined at an

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5 The Retirement Plan Document Section 27. Contributions by the Employers, the Board and the Bureau states that, "Each Employer…shall contribute to the Trust monthly…, such amounts as are necessary to maintain the Plan…on a sound actuarial basis…"

6 U.S.C. § 5584(i)(1)(A)(iv).

7 U.S.C. § 5584(i)(1)(A)(iv). The Dodd-Frank Act also requires that the CFPB contribute funds for employees that have transferred from the Federal Reserve System to the CFPB (12 U.S.C. § 5584(i)(1)(C)(iv)). Also, the Dodd-Frank Act states that the Board can require the CFPB to supplement the contributions that it provides with additional funding.

aggregate level based on aggregate plan assets and plan obligations. In addition, because the CFPB contribution formula is specifically required by the Dodd-Frank Act and not based on a benefit formula or linked to the participating employee benefits, the amount funded by each employer does not indicate that the assets are severable. The System plan's funded status for each participating employer is not determinable because the plan assets are not severable, and they will not be tracked separately.[8]

Conclusion

Previously, the FRBNY and effective August 1, 2023, the FRBA accounts for the System Plan in a manner that is consistent with the accounting for a single employer plan. System Plan assets, liabilities, costs and all required footnote disclosures are reflected in its financial statements, and net periodic pension costs are presented as a component of its net income from operations. Each of the other participating employers account for the System Plan in a manner similar to a multiple employer plan; no disclosure of plan assets, liabilities, and costs would be made in the financial statements of the other eleven Banks, and BOG as discussed earlier.

Limited disclosure regarding the reporting entity of the System Plan is required. Though the characterization as a single or multiemployer plan affects the accounting and disclosure, there is no requirement to state specifically that a plan is being accounted for as either a single or multiemployer plan. Financial statement disclosures provide users information about the participating employers and the FRBA's role, on behalf of the System, in recognizing the net asset/liability and costs and that the other participating employers do not reimburse the FRBA for the Plan costs. In addition, when they are made, the FRBA discloses the amount of contributions.

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[8] Any internal estimation of the funded status or funding requirement by participating employer is not considered relevant to the treatment as a single-employer plan.

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