Federal Reserve System Audits

Audits of the Federal Reserve System

The Board of Governors, the Federal Reserve Banks, and the Federal Reserve System as a whole are all subject to several levels of audit and review. The Board's financial statements, and its compliance with laws and regulations affecting those statements, are audited annually by an outside auditor retained by the Board's Office of Inspector General. The Office of Inspector General also conducts audits, reviews, and investigations relating to the Board's programs and operations as well as to Board functions delegated to the Reserve Banks.

The Reserve Banks' financial statements are audited annually by an independent outside auditor retained by the Board of Governors. In addition, the Reserve Banks are subject to annual examination by the Board. As discussed in the chapter "Federal Reserve Banks," the Board's examination includes a wide range of ongoing oversight activities conducted on site and off site by staff of the Board's Division of Reserve Bank Operations and Payment Systems.

Federal Reserve operations are also subject to review by the Government Accountability Office. ■

Board of Governors Financial Statements

The financial statements of the Board of Governors for 2009 and 2008 were audited by Deloitte & Touche LLP, independent auditors.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

March 19, 2010

MANAGEMENT'S ASSERTION

To the Committee on Board Affairs:

The management of the Board of Governors of the Federal Reserve System ("the Board") is responsible for the preparation and fair presentation of the balance sheet as of December 31, 2009, and for the related statement of revenues and expenses and changes in cumulative results of operations, and cash flows for the year then ended (the "Financial Statements"). The Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States of America and, as such, include some amounts which are based on management judgments and estimates. To our knowledge, the Financial Statements are, in all material respects, fairly presented in conformity with generally accepted accounting principles and include all disclosures necessary for such presentation.

Board management is also responsible for establishing and maintaining effective internal control over financial reporting as it relates to the Financial Statements. Such internal control is designed to provide reasonable assurance to management and to the Committee on Board Affairs regarding the preparation of the Financial Statements in accordance with accounting principles generally accepted in the United States of America. Internal control includes self-monitoring mechanisms, including, but not limited to, divisions of responsibility and a code of conduct. Once identified, any material deficiencies in internal control are reported to management and appropriate corrective measures are implemented.

Even effective internal control—no matter how well designed—has inherent limitations, including the possibility of human error. Internal control, therefore, can provide only reasonable assurance with respect to the preparation of reliable financial statements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that specific controls may become inadequate because of changes in conditions or that the degree of compliance with policies or procedures may deteriorate.

Board management assessed its internal control over financial reporting reflected in the Financial Statements based upon the criteria established in the *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Based on this assessment, we believe that the Board has maintained effective internal control over financial reporting as it relates to its Financial Statements.

Stephen R. Malphrus	William L. Mitchell
Staff Director for Management	Chief Financial Officer

Deloitte.

INDEPENDENT AUDITORS' REPORT

The Board of Governors of the Federal Reserve System:

We have audited the accompanying balance sheets of the Board of Governors of the Federal Reserve System (the "Board") as of December 31, 2009 and 2008, and the related statements of revenues and expenses and changes in cumulative results of operations, and cash flows for the years then ended. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Board of Governors of the Federal Reserve System as of December 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Board's internal control over financial reporting as of December 31, 2009, based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 19, 2010 expressed an unqualified opinion on the Board's internal control over financial reporting.

In accordance with *Government Auditing Standards,* we have also issued our report dated March 19, 2010, on our tests of the Board's compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte + Touche LLP

McLean, VA
March 19, 2010

Deloitte.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

To the Board of Governors of the Federal Reserve System:

We have audited the internal control over financial reporting of the Board of Governors of the Federal Reserve System (the "Board") as of December 31, 2009, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Board's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Assertion report. Our responsibility is to express an opinion on the Board's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

The Board's internal control over financial reporting is a process designed by, or under the supervision of, the Board's principal executive and principal financial officers, or persons performing similar functions, and effected by the Board's Committee on Board Affairs, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. The Board's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Board; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Board are being made only in accordance with authorizations of management and governors of the Board; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Board's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Board maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on the criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), generally accepted auditing standards as established by the Auditing Standards Board (United States), and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the accompanying balance sheet, statements of revenues and expenses and changes in cumulative results of operations, and cash flows as of and for the year ended December 31, 2009 of the Board and our report dated March 19, 2010 expressed an unqualified opinion on those financial statements.

Deloitte + Touche LLP

McLean, VA
March 19, 2010

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

BALANCE SHEETS

	As of December 31, 2009	As of December 31, 2008
ASSETS		
CURRENT ASSETS:		
Cash	$ 54,792,831	$ 58,255,990
Accounts receivable	2,948,984	2,975,478
Prepaid expenses and other assets	3,693,970	4,817,719
Total current assets	61,435,785	66,049,187
NONCURRENT ASSETS:		
Property, equipment, and software, net (Note 4)	159,267,605	148,875,490
Other assets	1,837,995	2,187,395
Total noncurrent assets	161,105,600	151,062,885
Total assets	$222,541,385	$217,112,072
LIABILITIES AND CUMULATIVE RESULTS OF OPERATIONS		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	$ 20,765,464	$ 13,312,600
Accrued payroll and related taxes	10,940,984	9,313,237
Accrued annual leave	24,821,044	22,234,106
Capital lease payable (Note 4)	533,110	471,266
Unearned revenues and other liabilities	2,982,629	1,843,058
Total current liabilities	60,043,231	47,174,267
LONG-TERM LIABILITIES:		
Capital lease payable (Note 4)	782,357	1,183,466
Accumulated retirement benefit obligation (Note 5)	13,021,387	10,866,659
Accumulated postretirement benefit obligation (Note 6)	9,304,324	8,527,800
Accumulated postemployment benefit obligation (Note 7)	14,463,965	13,900,000
Other long-term liabilities	415,324	648,534
Total long-term liabilities	37,987,357	35,126,459
Total liabilities	98,030,588	82,300,726
CUMULATIVE RESULTS OF OPERATIONS:		
Fund balance	133,677,902	144,085,508
Accumulated other comprehensive income (loss) (Note 8)	(9,167,105)	(9,274,162)
Total cumulative results of operations	124,510,797	134,811,346
Total liabilities and cumulative results of operations	$222,541,385	$217,112,072

See accompanying notes to financial statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

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

	For the years ended December 31, 2009	2008
BOARD OPERATING REVENUES:		
Assessments levied on Federal Reserve Banks for Board operating expenses and capital expenditures	$386,399,900	$352,290,700
Other revenues	9,413,565	9,059,232
Total operating revenues	395,813,465	361,349,932
BOARD OPERATING EXPENSES:		
Salaries	243,664,276	219,752,842
Retirement and insurance	50,458,964	48,394,723
Contractual services and professional fees	40,065,160	29,901,374
Depreciation, amortization, and net losses on disposals	13,885,165	13,782,449
Utilities	8,676,782	9,977,809
Travel	11,346,880	9,414,877
Software	8,699,031	7,277,995
Postage and supplies	8,157,780	5,802,368
Repairs and maintenance	5,115,155	3,214,203
Printing and binding	2,597,982	1,825,119
Other expenses	13,553,896	10,870,638
Total operating expenses	406,221,071	360,214,397
RESULTS OF OPERATIONS	(10,407,606)	1,135,535
CURRENCY COSTS:		
Assessments levied on Federal Reserve Banks for currency costs	502,144,883	500,356,895
Expenses for costs related to currency (Note 9)	502,144,883	500,356,895
CURRENCY ASSESSMENTS OVER (UNDER) EXPENSES	0	0
TOTAL RESULTS OF OPERATIONS	(10,407,606)	1,135,535
CUMULATIVE RESULTS OF OPERATIONS, Beginning of year	134,811,346	141,463,159
OTHER COMPREHENSIVE INCOME (Note 8)		
Prior service credit (cost) arising during the year	(315,842)	(5,059,307)
Amortization of prior service (credit) cost	541,162	73,867
Amortization of net actuarial (gain) loss	353,551	131,578
Net actuarial gain (loss) arising during the year	(471,814)	(3,183,688)
Curtailment effects - prior service credit (cost)	0	250,202
Total Other Comprehensive Income (Loss)	107,057	(7,787,348)
CUMULATIVE RESULTS OF OPERATIONS, End of year	$124,510,797	$134,811,346

See accompanying notes to financial statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

STATEMENTS OF CASH FLOWS

	For the years ended December 31, 2009	2008
Cash Flows from Operating Activities		
Results of operations	$(10,407,606)	$ 1,135,535
Adjustments to reconcile results of operations to net cash provided by (used in) operating activities:		
Depreciation	13,869,221	13,946,960
Net loss (gain) on disposal of property and equipment	15,944	(164,511)
Decrease (increase) in assets:		
Accounts receivable, prepaid expenses and other assets	1,499,641	(2,164,471)
Increase (decrease) in liabilities:		
Accounts payable and accrued liabilities	1,668,788	(7,087,682)
Accrued payroll and related taxes	1,627,747	3,666,184
Accrued annual leave	2,586,938	3,804,505
Unearned revenues and other liabilities	1,139,571	1,140,936
Accumulated retirement benefit obligation	2,154,728	8,664,984
Accumulated postretirement benefit obligation	776,524	555,331
Accumulated postemployment benefit obligation	563,965	5,044,387
Other long-term liabilities	(233,210)	648,534
Accumulated other comprehensive income	107,057	(7,787,348)
Net cash provided by (used in) operating activities	15,369,308	21,403,344
Cash Flows from Investing Activities		
Proceeds from disposals	866	0
Capital expenditures	(18,346,427)	(9,307,059)
Net cash provided by (used in) investing activities	(18,345,561)	(9,307,059)
Cash Flows from Financing Activities—Capital lease payments	(486,906)	1,545,977
Net cash provided by (used in) financing activities	(486,906)	1,545,977
Net Increase (Decrease) in Cash	(3,463,159)	13,642,262
Cash Balance, Beginning of year	58,255,990	44,613,728
Cash Balance, End of year	$ 54,792,831	$58,255,990

See accompanying notes to financial statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

NOTES TO FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

(1) Structure

The Federal Reserve System (the System) was established by Congress in 1913 and consists of the Board of Governors (the Board), the Federal Open Market Committee, the twelve regional Federal Reserve Banks, the Federal Advisory Council, and the private commercial banks that are members of the System. The Board, unlike the Reserve Banks, was established as a federal government agency and is supported by Washington, D.C. based staff numbering approximately 2,100, as it carries out its responsibilities in conjunction with other components of the Federal Reserve System.

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

(2) Operations and Services

The Board's responsibilities require thorough analysis of domestic and international financial and economic developments. The Board carries out those responsibilities in conjunction with other components of the Federal Reserve System. The Board also supervises and regulates the operations of the Federal Reserve Banks, exercises broad responsibility in the nation's payments system, and administers most of the nation's laws regarding consumer credit protection. Policy regarding open market operations is established by the Federal Open Market Committee. However, the Board has sole authority over changes in reserve requirements, and it must approve any change in the discount rate initiated by a Federal Reserve Bank.

The Board also plays a major role in the supervision and regulation of the U.S. banking system. It has supervisory responsibilities for state-chartered banks that are members of the Federal Reserve System, bank holding companies, foreign activities of member banks, and U.S. activities of foreign banks.

(3) Significant Accounting Policies

Basis of Accounting — The Board prepares its financial statements in accordance with accounting principles generally accepted in the United States (GAAP).

Revenues — The Federal Reserve Act authorizes the Board to levy an assessment on the Reserve Banks to fund its operations. The Board levies the assessment based on each Reserve Bank's capital and surplus balances as of December 31 of the prior year.

Currency Costs — The Federal Reserve Board issues the nation's currency (in the form of Federal Reserve notes), and the Federal Reserve Banks distribute currency and coin through depository institutions. The Board incurs expenses and assesses the Reserve Banks for the expenses related to producing, issuing, and retiring Federal Reserve notes. The assessment is allocated based on each Reserve Bank's share of the number of notes comprising the Federal Reserve Bank System's net liability for Federal Reserve notes on December 31 of the prior year. These expenses and assessments are reported separately from the Board's operating transactions in the Board's Statement of Revenues and Expenses and Changes in Cumulative Results of Operations.

Allowance for Doubtful Accounts — Accounts receivable are shown net of the allowance for doubtful accounts. Accounts receivable considered uncollectible are charged against the allowance account in the year they are deemed uncollectible. The allowance for doubtful accounts is adjusted monthly, based upon a review of outstanding receivables.

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

The Board's internally developed software projects are each recorded at cost and capitalized and amortized over the project's useful life as required by the Internal Use Software Topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC).

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

Deferred Rent — The leases contain scheduled rent increases over the term of the lease. As required by the Leases Topic of the ASC, rent abatements and scheduled rent increases must be considered in determining the annual rent expense to be recognized. The deferred rent represents the difference between the actual lease payments and the rent expense recognized.

Estimates — The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recently Issued Accounting Standards — The Retirement Benefits Topic of the ASC provides rules for the disclosure of information about assets held in a defined benefit plan in the financial statements of the employer sponsoring that plan, and additional disclosures about asset categories and concentrations of risk. It is effective for financial statements with fiscal years ending after December 15, 2009. The provisions of the ASC have been reflected in the accompanying footnotes.

The Subsequent Events Topic of the ASC establishes general standards of accounting for and disclosure of events that occur through the balance sheet date but before financial statements are issued or are available to be issued. The ASC sets forth (i) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements; (ii) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements; and (iii) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date, including disclosure of the date through which an entity has evaluated subsequent events and whether that represents the date the financial statements were issued or were available to be issued. The Board adopted the standard for the period ended December 31, 2009.

On June 30, 2009, the FASB issued SFAS No. 168, "The Statement of Financial Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles — a replacement of SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles" (SFAS 168). SFAS 168 establishes the FASB ASC as the source of authoritative accounting principles recognized by the FASB to be applied by entities in the preparation of financial statements in conformity with GAAP. The ASC does not change current GAAP, but it introduces a new structure that organizes the authoritative standards by topic. SFAS 168 is effective for financial statements issued for periods ending after September 15, 2009. In accordance with the requirements of this standard, the ASC is referenced in the Board's financial statements and footnotes.

(4) Property, Equipment, and Software

The following is a summary of the components of the Board's property, equipment, and software, at cost, net of accumulated depreciation and amortization as of December 31, 2009 and 2008:

	As of December 31,	
	2009	2008
Land	$ 18,640,314	$ 18,640,314
Buildings and improvements	155,403,350	150,602,767
Furniture and equipment	66,411,669	56,104,247
Software in use	16,196,241	14,514,315
Software in process	6,276,842	3,832,516
Construction in process	8,100,559	3,818,295
Total	271,028,975	247,512,454
Less accumulated depreciation and amortization	(111,761,370)	(98,636,964)
Property, equipment, and software — net	$ 159,267,605	$148,875,490

Construction in process includes costs incurred in 2009 and 2008 for long-term projects and building enhancements. The Board has accrued liabilities related to property, equipment, and software of $7,131,000 as of December 31, 2009.

The Board entered into capital leases for printing equipment during 2003 that terminated in May 2008. The Board subsequently entered into new capital leases in 2008 and 2009. Under the new commitments, the capital lease term extends through 2012. Furniture and equipment includes $2,086,000 and $1,923,000 in 2009 and 2008, respectively, for capitalized leases. Accumulated depreciation includes $789,000 and $280,000 for capitalized leases as of 2009 and 2008, respectively. The Board paid interest related to these capital leases in the amount of $36,000 and $26,000 as of December 31, 2009 and 2008, respectively. The Board has accrued liabilities related to capital leases of $148,000 as of December 31, 2009.

The Board has leased space in its buildings to other governmental agencies. The revenues collected from these leases are $2,037,000 and $2,034,000 in 2009 and 2008, respectively.

The future minimum lease payments required under the capital leases and the present value of the net minimum lease payments as of December 31, 2009, are as follows:

Years Ending December 31	Amount
2010	$ 978,315
2011	978,315
2012	421,925
Total minimum lease payments	2,378,555
Less amount representing maintenance	(1,026,701)
Net minimum lease payments	1,351,854
Less amount representing interest	(36,387)
Present value of net minimum lease payments	1,315,467
Less current maturities of capital lease payments	(533,110)
Long-term capital lease obligations	$ 782,357

(5) Accumulated Retirement Benefits

Substantially all of the Board's employees participate in the Retirement Plan for Employees of the Federal Reserve System (the System Plan). The System Plan provides retirement benefits only to employees of the Board, the Federal Reserve Banks, and the Office of Employee Benefits of the Federal Reserve System (OEB). The Federal Reserve Bank of New York (FRB NY), on behalf of the System, recognizes the net assets and costs associated with the System Plan in its financial statements. Costs associated with the System Plan are not redistributed to other participating employers.

Employees of the Board who became employed prior to 1984 are covered by a contributory defined benefits program under the System Plan. Employees of the Board who became employed after 1983 are covered by a non-contributory defined benefits program under the System Plan. Contributions to the System Plan are actuarially determined and funded by participating employers. In 2009, the System made $500 million in contributions to the System Plan; the contributions may be adjusted upon completion of the 2010 actuarial valuation. The Board was not assessed a contribution for 2009.

Effective January 1, 1996, Board employees covered under the System Plan are also covered under a Benefits Equalization Plan (BEP). Benefits paid under the BEP are limited to those benefits that cannot be paid from the System Plan due to limitations imposed by Sections 401(a)(17), 415(b) and 415(e) of the Internal Revenue Code of 1986. Activity for the BEP as of December 31, 2009 and 2008, is summarized in the following tables:

	As of December 31,	
	2009	2008
Change in projected benefit obligation:		
Benefit obligation — beginning of year	$4,591,374	$2,201,675
Service cost	712,515	589,094
Interest cost	307,501	213,714
Plan participants' contributions		
Actuarial (gain) loss	(175,635)	1,137,486
Gross benefits paid	(27,649)	(35,016)
Plan amendments	492,461	484,421
Benefit obligation — end of year	$5,900,567	$4,591,374
Accumulated benefit obligation — end of year	$1,245,465	$1,267,005

	As of December 31, 2009	2008
Weighted-average assumptions used to determine benefit obligation as of December 31:		
Discount rate	6.00%	6.00%
Rate of compensation increase	5.00%	5.00%
Change in plan assets:		
Fair value of plan assets — beginning of year	$ -	$ -
Employer contributions	27,649	35,016
Plan participants' contributions		
Gross benefits paid	(27,649)	(35,016)
Fair value of plan assets — end of year	$ -	$ -
Funded status:		
Reconciliation of funded status — end of year:		
Fair value of plan assets	$ -	$ -
Benefit obligations	5,900,567	4,591,374
Funded status	(5,900,567)	(4,591,374)
Amount recognized — end of year	$(5,900,567)	$(4,591,374)
Amounts recognized in the statements of financial position consist of:		
Asset	$ -	$ -
Liability	(5,900,567)	(4,591,374)
Net amount recognized	$(5,900,567)	$(4,591,374)
Amounts recognized in accumulated other comprehensive income consist of:		
Net actuarial loss (gain)	$ 1,708,854	$ 2,031,269
Prior service cost (credit)	714,123	256,919
	$ 2,422,977	$ 2,288,188
Expected cash flow:		
Expected employer contributions — 2010	$ 111,143	
Expected benefit payments:*		
2010	$ 111,143	
2011	149,745	
2012	183,388	
2013	210,792	
2014	232,368	
2015–2019	1,421,730	

*Expected benefit payments to be made from System assets

	2009	2008
Components of net periodic benefit cost:		
Service cost	$ 712,515	$ 589,094
Interest cost	307,501	213,714
Expected return on plan assets	-	-
Amortization:		
Actuarial (gain) loss	146,780	112,474
Prior service (credit) cost	35,257	(5,902)
Net periodic benefit cost (credit)	$ 1,202,053	$ 909,380
Weighted-average assumptions used to determine net periodic benefit cost:		
Discount rate	6.00%	6.25%**
Rate of compensation increase	5.00%	5.00%

**In 2008, amendments to the System Plan were approved. As a result, the actuarially determined net periodic benefit expenses for the year ended December 31, 2008, were remeasured with a discount rate of 7.75% as of November 1, 2008.

	As of December 31, 2009	As of December 31, 2008
*Other changes in plan assets and benefit obligations recognized in other comprehensive income:****		
Current year prior service (credit) cost	$ 492,461	$ 484,421
Current year actuarial (gain) loss	(175,635)	1,137,486
Amortization of prior service credit (cost)	(35,257)	5,902
Amortization of actuarial gain (loss)	(146,780)	(112,474)
Total recognized in other comprehensive income	$ 134,789	$1,515,335
Total recognized in net periodic benefit cost and other comprehensive income	$1,336,842	$2,424,715

***For the Benefit Equalization Plan, other changes to assets and benefits recognized in other comprehensive income will be reflected in net periodic cost.

Estimated amounts that will be amortized from accumulated other comprehensive income into net periodic benefit cost (credit) in 2010 are shown below:

Net actuarial (gain) loss	$114,291
Prior service (credit) cost	12,290
Total	$126,581

On October 30, 2008, the Board approved a non-qualified plan for Officers of the Board. The retirement benefits covered under the Board Officer Pension Enhancement (BOPE), formerly the Supplemental Employee Retirement Plan (BSERP), increases the pension benefit calculation from 1.8% above the Social Security integration level to 2.0%. Activity for the BOPE as of December 31, 2009 and 2008, is summarized in the following tables:

	As of December 31, 2009	As of December 31, 2008
Change in projected benefit obligation:		
Benefit obligation — beginning of year	$ 6,275,285	$ -
Service cost	333,034	37,190
Interest cost	402,680	56,010
Plan participants' contributions		
Actuarial (gain) loss	286,440	1,607,199
Gross benefits paid		
Plan amendments	(176,619)	4,574,886
Benefit obligation — end of year	$ 7,120,820	$ 6,275,285
Accumulated benefit obligation — end of year	$ 5,175,331	$ 4,530,540
Weighted-average assumptions used to determine benefit obligation as of December 31:		
Discount rate	6.00%	6.00%
Rate of compensation increase	5.00%	5.00%
Change in plan assets:		
Fair value of plan assets — beginning of year	$ -	$ -
Employer contributions		
Plan participants' contributions		
Gross benefits paid		
Fair value of plan assets — end of year	$ -	$ -
Funded status:		
Reconciliation of funded status — end of year:		
Fair value of plan assets	$ -	$ -
Benefit obligations	7,120,820	6,275,285
Funded status	(7,120,820)	(6,275,285)
Amount recognized — end of year	$(7,120,820)	$(6,275,285)

	As of December 31, 2009	2008
Amounts recognized in the statements of financial position consist of:		
Asset	$ -	$ -
Liability	(7,120,820)	(6,275,285)
Net amount recognized	$(7,120,820)	$(6,275,285)
Amounts recognized in accumulated other comprehensive income consist of:		
Net actuarial loss (gain)	$ 1,742,746	$ 1,607,199
Prior service cost (credit)	3,774,673	4,482,687
	$ 5,517,419	$ 6,089,886
Expected cash flows:		
Expected employer contributions — 2010	$ 41,829	
Expected benefit payments:****		
2010	$ 41,829	
2011	75,298	
2012	115,587	
2013	161,773	
2014	215,737	
2015–2019	1,967,583	

****Expected benefit payments to be made from System assets

	2009	2008
Components of net periodic benefit cost:		
Service cost	$ 333,034	$ 37,190
Interest cost	402,680	56,010
Expected return on plan assets		
Amortization:		
Actuarial (gain) loss	150,893	
Prior service (credit) cost	531,395	92,199
Net periodic benefit cost (credit)	$ 1,418,002	$ 185,399
Weighted-average assumptions used to determine net periodic benefit cost:		
Discount rate	6.00%	7.75%
Rate of compensation increase	5.00%	5.00%
*Other changes in plan assets and benefit obligations recognized in other comprehensive income:******		
Current year prior service (credit) cost	$ (176,619)	$ 4,574,886
Current year actuarial (gain) loss	286,440	1,607,199
Amortization of prior service credit (cost)	(531,395)	(92,199)
Amortization of actuarial gain (loss)	(150,893)	
Total recognized in other comprehensive income	$ (572,467)	$ 6,089,886
Total recognized in net periodic benefit cost and other comprehensive income	$ 845,535	$ 6,275,285

*****For the Board Officer Pension Enhancement, other changes in assets and benefits recognized in other comprehensive income will be reflected in net periodic cost.

Estimated amounts that will be amortized from accumulated other comprehensive income into net periodic benefit cost (credit) in 2010 are shown below:

Net actuarial (gain) loss	$123,908
Prior service (credit) cost	531,395
Total	$655,303

The total accumulated retirement benefit obligation for both the Benefits Equalization Plan (BEP) and Board Officer Pension Enhancement (BOPE) as of December 31, 2009 and 2008, are as follows:

	As of December 31,	
	2009	2008
Accumulated retirement benefit obligation:		
Benefit obligation — BEP	$ 5,900,567	$ 4,591,374
Benefit obligation — BOPE	7,120,820	6,275,285
Total accumulated retirement benefit obligation	$13,021,387	$10,866,659

A relatively small number of Board employees participate in the Civil Service Retirement System (CSRS) of the Federal Employees' Retirement System (FERS). These defined benefit plans are administered by the U.S. Office of Personnel Management, which determines the required employer contribution levels. The Board's contributions to these plans totaled $329,000 and $305,000 in 2009 and 2008, respectively. The Board has no liability for future payments to retirees under these programs and is not accountable for the assets of the plans.

Employees of the Board may also participate in the Federal Reserve System's Thrift Plan or Roth 401(k). Board contributions to members' accounts were $14,342,000 and $11,815,000 in 2009 and 2008, respectively.

(6) Accumulated Postretirement Benefits

The Board provides certain life insurance programs for its active employees and retirees. Activity as of December 31, 2009 and 2008, is summarized in the following tables:

	As of December 31,	
	2009	2008
Change in projected benefit obligation:		
Benefit obligation — beginning of year	$ 8,527,800	$ 7,972,469
Service cost	169,687	176,450
Interest cost	516,194	505,691
Plan participants' contributions		
Actuarial (gain) loss	361,009	439,003
Gross benefits paid	(270,366)	(315,611)
Curtailments		(250,202)
Benefit obligation — end of year	$ 9,304,324	$ 8,527,800
Weighted-average assumptions used to determine benefit obligation as of December 31 — discount rate	5.75%	6.00%
Change in plan assets:		
Fair value of plan assets — beginning of year	$ -	$ -
Employer contributions	270,366	315,611
Gross benefits paid	(270,366)	(315,611)
Fair value of plan assets — end of year	$ -	$ -
Funded status:		
Reconciliation of funded status — end of year:		
Fair value of plan assets	$ -	$ -
Benefit obligations	9,304,324	8,527,800
Funded status	(9,304,324)	(8,527,800)
Amount recognized — end of year	$(9,304,324)	$(8,527,800)
Amounts recognized in the statements of financial position consist of:		
Asset	$ -	$ -
Liability	(9,304,324)	(8,527,800)
Net amount recognized	$(9,304,324)	$(8,527,800)
Amounts recognized in accumulated other comprehensive income consist of:		
Net actuarial loss (gain)	$ 1,528,733	$ 1,223,601
Prior service cost (credit)	(302,024)	(327,513)
	$ 1,226,709	$ 896,088

	As of December 31, 2009	As of December 31, 2008
Expected cash flows:		
Expected employer contributions — 2010	$ 342,502	$ 321,938
Expected benefit payments:*		
2010	$ 342,502	
2011	361,970	
2012	381,110	
2013	408,919	
2014	436,116	
2015–2019	2,570,408	

*Expected benefit payments to be made from System assets

	2009	2008
Components of net periodic benefit cost:		
Service cost	$ 169,687	$ 176,450
Interest cost	516,194	505,691
Expected return on plan assets		
Amortization:		
Actuarial (gain) loss	55,878	19,104
Prior service (credit) cost	(25,490)	(12,430)
Net periodic benefit cost (credit)	$ 716,269	$ 688,815
Weighted-average assumptions used to determine net periodic benefit cost — discount rate	6.00%	6.25%**

**In 2008, amendments to the Plan were approved. As a result, the actuarially determined net periodic benefit expenses for the year ended December 31, 2008, were remeasured with a discount rate of 7.75% as of November 1, 2008.

	2009	2008
Other changes in plan assets and benefit obligations recognized in other comprehensive income:		
Current year actuarial (gain) loss	$ 361,009	$ 439,003
Amortization of prior service credit (cost)	25,490	12,430
Amortization of actuarial gain (loss)	(55,878)	(19,104)
Curtailment effects — prior service (credit) cost		(250,202)
Total recognized in other comprehensive income	$ 330,621	$ 182,127
Total recognized in net periodic benefit cost and other comprehensive income	$1,046,890	$ 870,942

Estimated amounts that will be amortized from accumulated other comprehensive income into net periodic benefit cost (credit) in 2010 are shown below:

Net actuarial (gain) loss	$76,193
Prior service (credit) cost	(25,490)
Total	$50,703

(7) Accumulated Postemployment Benefits

The Board provides certain postemployment benefits to eligible former or inactive employees and their dependents during the period subsequent to employment but prior to retirement. Postemployment costs were actuarially determined using a December 31 measurement date and discount rates of 4.00% and 2.50% as of December 31, 2009 and 2008, respectively. The accrued postemployment benefit costs recognized by the Board as of December 31, 2009 and 2008, were $1,754,000 and $5,974,000, respectively.

(8) Accumulated Other Comprehensive Income

A reconciliation of beginning and ending balances of accumulated other comprehensive income for the years ended December 31, 2009 and 2008, is as follows:

	Amount Related to Defined Benefit Retirement Plans	Amount Related to Postretirement Benefits Other Than Pensions	Total Accumulated Other Comprehensive Income (Loss)
Balance — January 1, 2008	$ 772,853	$ 713,961	$(1,486,814)
Change in funded status of benefit plans:			
Prior service (credit) cost arising during the year	5,059,307		(5,059,307)
Amortization of prior service credit (costs)	(86,297)	12,430	73,867
Amortization of net actuarial gain (loss)	(112,474)	(19,104)	131,578
Net actuarial (gain) loss arising during the year	2,744,685	439,003	(3,183,688)
Curtailment effects — prior service (credit) cost		(250,202)	250,202
Change in funded status of benefit plans — other comprehensive income (loss)	7,605,221	182,127	(7,787,348)
Balance — December 31, 2008	8,378,074	896,088	(9,274,162)
Change in funded status of benefit plans:			
Prior service (credit) cost arising during the year	315,842		(315,842)
Amortization of prior service credit (costs)	(566,652)	25,490	541,162
Amortization of net actuarial gain (loss)	(297,673)	(55,878)	353,551
Net actuarial (gain) loss arising during the year	110,805	361,009	(471,814)
Change in funded status of benefit plans — other comprehensive income (loss)	(437,678)	330,621	107,057
Balance — December 31, 2009	$7,940,396	$1,226,709	$(9,167,105)

Additional detail regarding the classification of accumulated other comprehensive income is included in Notes 5 and 6.

(9) Federal Reserve Banks

The Board performs certain functions for the Reserve Banks in conjunction with its responsibilities for the System, and the Reserve Banks provide certain administrative functions for the Board. Activity related to the Board and Reserve Banks as of December 31, 2009 and 2008, is summarized in the following table:

	As of December 31, 2009	As of December 31, 2008
Reserve Bank expenses charged to the Board:		
Data processing and communication	$ 776,835	$ 2,368,144
Contingency site	1,171,808	1,265,618
Total Reserve Bank expenses charged to the Board	$ 1,948,643	$ 3,633,762
Board expenses charged to the Reserve Banks:		
Assessments for currency costs:		
Printing	$479,255,288	$477,927,083
Shipping	15,367,546	14,984,564
Retirement	3,608,937	3,722,146
Research and development	3,913,112	3,723,101
Assessments for operating expenses of the Board	386,399,900	352,290,700
Data processing	635,235	601,957
Total Board expenses charged to the Reserve Banks	$889,180,018	$853,249,551
Accounts receivable due from the Reserve Banks	$ 1,071,932	$ 1,016,688
Accounts payable due to the Reserve Banks		295,848

The Board contracted for audit services on behalf of entities that are included in the combined financial statements of the Federal Reserve Banks. The entities reimburse the Board for the cost of the audit services. The Board accrued liabilities of $138,000 and $313,000 in audit services and recorded receivables of $138,000 and $313,000 from the entities as of December 31, 2009 and 2008, respectively.

(10) Federal Financial Institutions Examination Council

The Board is one of the five member agencies of the Federal Financial Institutions Examination Council (the Council), and currently performs certain management functions for the Council. The five agencies that are represented on the Council are the Board, Federal Deposit Insurance Corporation, National Credit Union Administration, Office of the Comptroller of the Currency, and Office of Thrift Supervision. The Board's financial statements do not include financial data for the Council. Activity related to the Board and Council, as of December 31, 2009 and 2008, is summarized in the following table:

	As of December 31,	
	2009	2008
Council expenses charged to the Board:		
Assessments for operating expenses	$ 67,998	$ 164,889
Central Data Repository	1,522,597	1,352,390
Uniform Bank Performance Report	210,293	185,833
Total Council expenses charged to the Board	$1,800,888	$1,703,112
Board expenses charged to the Council:		
Data processing related services	$4,884,868	$4,683,363
Administrative services	245,000	190,400
Total Board expenses charged to the Council	$5,129,868	$4,873,763
Accounts receivable due from the Council	$ 618,861	$ 650,672
Accounts payable due to the Council	209,922	373,466

(11) The Office of Employee Benefits of the Federal Reserve System

The Office of Employee Benefits of the Federal Reserve System (OEB) administers certain System benefit programs on behalf of the Board and the Reserve Banks, and costs associated with the OEB's activities are assessed to the Board and Reserve Banks. The Board was assessed $2,166,000 and $2,867,000 as of December 31, 2009 and 2008, respectively.

(12) Bureau of Engraving and Printing

The Bureau of Engraving and Printing (BEP) is the principal supplier for currency printing and retirement services. The currency costs incurred as of December 31, 2009 and 2008, are reflected in the following table:

	As of December 31,	
	2009	2008
Currency expenses charged to the Board:		
Printing	$479,255,288	$477,927,083
Retirement	3,608,937	3,722,146
Total currency expenses charged to the Board	$482,864,225	$481,649,229

(13) Commitments and Contingencies

Leases — The Board has entered into several operating leases to secure office, training and warehouse space. The Board has subleased space to other governmental agencies. The sublease agreements are annual and the revenue collected was $467,000 and $468,000 for 2009 and 2008, respectively.

Minimum annual payments under the operating leases having an initial or remaining non-cancelable lease term in excess of one year at December 31, 2009, are as follows:

Years Ending December 31	
2010	$ 6,297,594
2011	6,335,714
2012	6,414,807
2013	6,608,976
After 2013	42,414,511
	$68,071,602

Rental expenses under the operating leases were $3,947,000 and $2,207,000 for the years ended December 31, 2009 and 2008, respectively.

Deferred Leases — The change in deferred rent was $1,666,000 and $537,000 for the years ended December 31, 2009 and 2008, respectively.

Commitments — The Board has entered into an agreement with the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency, through the Council, to fund a portion of the enhancements and maintenance fees for a central data repository project through 2010 with an option to extend maintenance through 2013. The estimated Board expense to support this effort is $7.9 million for the base period and $2.6 million for the option period.

In 2007, the Council began a rewrite of the Home Mortgage Disclosure Act processing system, for which the Board provides data processing services. The estimated total expense to the Council of the rewrite is $3.2 million through 2010. The estimated total Board expense to support this effort with the maintenance extension option is $533,000.

Accrued liabilities include a federal tax liability estimated at $494,000 for the Board and its employees. The Board expects to pay the liability during 2010.

Litigation and Contingent Liabilities — The Board is subject to contingent liabilities which arise from litigation cases and various business contracts. These contingent liabilities arise in the normal course of operations and their ultimate disposition is unknown. Based on information currently available to management, it is management's opinion that the expected outcome of these matters, individually or in the aggregate, will not have a materially adverse effect on the financial statements.

One case alleges employment discrimination under Title VII of the Civil Rights Act of 1964, as amended, and the Age Discrimination in Employment Act, and is pending in the United States District Court for the District of Columbia. The second case is an action alleging discrimination on behalf of a class of African American secretaries at the Board. The case was dismissed by the United States District Court for the District of Columbia on January 31, 2007, and the plaintiffs' motion to alter or amend judgment was denied by that court on March 2, 2009. The plaintiffs have appealed the dismissal to the United States Court of Appeals for the District of Columbia circuit. The Board has substantial defenses for both cases and intends to defend the matters vigorously. Management believes that the likelihood of an adverse judgment for both cases is small.

The estimated contingent liabilities related to business contracts were $0 and $69,720 as of December 31, 2009 and 2008, respectively.

(14) Subsequent Events

There were no subsequent events that require adjustments to or disclosures in the financial statements as of December 31, 2009. Subsequent events were evaluated through March 19, 2010, which is the date the Board issued the financial statements.

Deloitte.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Governors of the Federal Reserve System:

We have audited the financial statements of the Board of Governors of the Federal Reserve System (the "Board") as of and for the year ended December 31, 2009, and have issued our report thereon dated March 19, 2010. We conducted our audit in accordance generally accepted auditing standards as established by the Auditing Standards Board (United States), auditing standards of the Public Company Accounting Oversight Board (United States), and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In accordance with standards of the Public Company Accounting Oversight Board (United States) and *Government Auditing Standards,* we have also issued our report dated March 19, 2010, on our tests of the Board's internal control over financial reporting. The purpose of that report is to describe the scope and the results of that testing. That report is an integral part of an audit performed in accordance with standards of the Public Company Accounting Oversight Board (United States) and *Government Auditing Standards* and should be considered in assessing the results of our audit.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Board's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

Distribution

This report is intended solely for the information and use of the Board, management, and others within the organization, Office of Inspector General, the United States Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLP

McLean, VA
March 19, 2010

Federal Reserve Banks Combined Financial Statements

The combined financial statements of the Federal Reserve Banks were audited by Deloitte & Touche LLP, independent auditors, for the years ended December 31, 2009 and 2008.

Deloitte.

INDEPENDENT AUDITORS' REPORT

To the Board of Governors of the Federal Reserve System
and the Board of Directors of the Federal Reserve Banks:

We have audited the accompanying combined statements of condition of the Federal Reserve Banks (the "Reserve Banks") as of December 31, 2009 and 2008, and the related combined statements of income and comprehensive income and changes in capital for the years then ended, which have been prepared in conformity with accounting principles established by the Board of Governors of the Federal Reserve System. These combined financial statements are the responsibility of the Division of Reserve Bank Operations and Payment System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards as established by the Auditing Standards Board (United States) and in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Reserve Banks are not required to have, nor were we engaged to perform, an audit of their internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Reserve Bank's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 4 to the combined financial statements, the Reserve Banks have prepared these combined financial statements in conformity with accounting principles established by the Board of Governors of the Federal Reserve System, as set forth in the Financial Accounting Manual for Federal Reserve Banks, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The effects on such combined financial statements of the differences between the accounting principles established by the Board of Governors of the Federal Reserve System and accounting principles generally accepted in the United States of America are also described in Note 4.

In our opinion, such combined financial statements present fairly, in all material respects, the combined financial position of the Reserve Banks as of December 31, 2009 and 2008, and the combined results of their operations for the years then ended, on the basis of accounting described in Note 4.

Deloitte & Touche LLP

April 21, 2010

FEDERAL RESERVE BANKS
COMBINED STATEMENTS OF CONDITION
(in millions)

	As of December 31, 2009	As of December 31, 2008
Assets		
Gold certificates	$ 11,037	$ 11,037
Special drawing rights certificates	5,200	2,200
Coin	2,053	1,688
Items in process of collection	507	979
Prepaid interest on Federal Reserve notes	-	2,425
Loans to depository institutions	96,618	544,010
Other loans, net (of which $48,183 million is measured at fair value as of December 31, 2009)	69,433	100,082
System Open Market Account:		
Securities purchased under agreements to resell	-	80,000
Treasury securities, net	805,972	481,449
Government-sponsored enterprise debt securities, net	167,362	20,740
Federal agency and government-sponsored enterprise mortgage-backed securities, net	918,927	-
Investments denominated in foreign currencies	25,272	24,804
Central bank liquidity swaps	10,272	553,728
Other investments	5	-
Consolidated variable interest entities:		
Investments held by consolidated variable interest entities (of which $71,648 million and $74,570 million is measured at fair value as of December 31, 2009 and 2008, respectively)	81,380	411,996
Preferred securities	25,106	-
Accrued interest receivable	12,641	7,389
Bank premises and equipment, net	2,624	2,572
Other assets	638	629
Total assets	$2,235,047	$2,245,728
Liabilities and Capital		
Federal Reserve notes outstanding, net	$ 887,846	$ 853,168
System Open Market Account:		
Securities sold under agreements to repurchase	77,732	88,352
Other liabilities	601	-
Consolidated variable interest entities:		
Beneficial interest in consolidated variable interest entities	5,095	2,824
Other liabilities (of which $143 million is measured at fair value as of December 31, 2009)	1,316	5,813
Deposits:		
Depository institutions	976,988	860,000
Treasury, general account	186,632	106,123
Treasury, supplementary financing account	5,001	259,325
Other deposits	36,228	21,671
Deferred credit items	2,103	2,471
Accrued interest on Federal Reserve notes	1,191	-
Interest due to depository institutions	113	88
Accrued benefit costs	2,631	3,374
Other liabilities	290	367
Total liabilities	2,183,767	2,203,576
Capital paid-in	25,640	21,076
Surplus (including accumulated other comprehensive loss of $3,676 million and $4,683 million at December 31, 2009 and 2008, respectively)	25,640	21,076
Total capital	51,280	42,152
Total liabilities and capital	$2,235,047	$2,245,728

The accompanying notes are an integral part of these combined financial statements.

FEDERAL RESERVE BANKS
COMBINED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(in millions)

	For the years ended December 31, 2009	2008
Interest income:		
Loans to depository institutions	$ 990	$ 3,817
Other loans, net	4,519	3,348
System Open Market Account:		
Securities purchased under agreements to resell	13	1,891
Treasury securities	22,873	25,532
Government-sponsored enterprise debt securities	2,048	99
Federal agency and government-sponsored enterprise mortgage-backed securities	20,407	-
Investments denominated in foreign currencies	296	623
Central bank liquidity swaps	2,168	3,606
Other investments	1	-
Investments held by consolidated variable interest entities	9,820	4,087
Total interest income	63,135	43,003
Interest expense:		
System Open Market Account:		
Securities sold under agreements to repurchase	98	737
Depository institution deposits	2,183	817
Beneficial interest in consolidated variable interest entities	267	463
Total interest expense	2,548	2,017
Provision for loan restructuring	(2,621)	-
Net interest income, after provision for loan restructuring	57,966	40,986
Non-interest income (loss):		
Other loans unrealized gains	557	-
System Open Market Account:		
Treasury securities gains	-	3,769
Federal agency and government-sponsored enterprise mortgage-backed securities gains, net	879	-
Foreign currency gains, net	172	1,266
Consolidated variable interest entities:		
Investments held by consolidated variable interest entities losses, net	(1,937)	(9,626)
Beneficial interest in consolidated variable interest entities (losses) gains, net	(1,903)	4,389
Dividends on preferred securities	106	-
Income from services	663	773
Reimbursable services to government agencies	450	461
Other income	443	899
Total non-interest (loss) income	(570)	1,931
Operating expenses:		
Salaries and other benefits	2,802	2,184
Occupancy expense	280	275
Equipment expense	183	200
Assessments by the Board of Governors	888	853
Professional fees related to consolidated variable interest entities	125	80
Other expenses	702	662
Total operating expenses	4,980	4,254
Net income prior to distribution	52,416	38,663
Change in funded status of benefit plans	1,007	(3,159)
Comprehensive income prior to distribution	$53,423	$35,504
Distribution of comprehensive income:		
Dividends paid to member banks	$ 1,428	$ 1,189
Transferred to surplus and change in accumulated other comprehensive income (loss)	4,564	2,626
Payments to Treasury as interest on Federal Reserve notes	47,431	31,689
Total distribution	$53,423	$35,504

The accompanying notes are an integral part of these combined financial statements.

FEDERAL RESERVE BANKS
COMBINED STATEMENTS OF CHANGES IN CAPITAL
for the years ended December 31, 2009 and December 31, 2008

(in millions, except share data)

		Surplus			
	Capital Paid-In	Net Income Retained	Accumulated Other Comprehensive (Loss) Income	Total Surplus	Total Capital
Balance at January 1, 2008 (368,996,413 shares)	$18,450	$19,974	$(1,524)	$18,450	$36,900
Net change in capital stock issued (52,521,054 shares)	2,626	-	-	-	2,626
Transferred to surplus and change in accumulated other comprehensive income (loss)	-	5,785	(3,159)	2,626	2,626
Balance at December 31, 2008 (421,517,467 shares)	$21,076	$25,759	$(4,683)	$21,076	$42,152
Net change in capital stock issued (91,289,192 shares)	4,564	-	-	-	4,564
Transferred to (from) surplus and change in accumulated other comprehensive income	-	3,557	1,007	4,564	4,564
Balance at December 31, 2009 (512,806,659 shares)	$25,640	$29,316	$(3,676)	$25,640	$51,280

The accompanying notes are an integral part of these combined financial statements.

Notes to the Combined Financial Statements of the Federal Reserve Banks

(1) Structure

The 12 Federal Reserve Banks ("Reserve Banks") are part of the Federal Reserve System ("System") created by Congress under the Federal Reserve Act of 1913 ("Federal Reserve Act"), which established the central bank of the United States. The Reserve Banks are chartered by the federal government and possess a unique set of governmental, corporate, and central bank characteristics.

In accordance with the Federal Reserve Act, supervision and control of each Reserve Bank is exercised by a board of directors. The Federal Reserve Act specifies the composition of the board of directors for each of the Reserve Banks. Each board is composed of nine members serving three-year terms: three directors, including those designated as chairman and deputy chairman, are appointed by the Board of Governors of the Federal Reserve System ("Board of Governors") to represent the public, and six directors are elected by member banks. Banks that are members of the System include all national banks and any state-chartered banks that apply and are approved for membership. Member banks are divided into three classes according to size. Member banks in each class elect one director representing member banks and one representing the public. In any election of directors, each member bank receives one vote, regardless of the number of shares of Reserve Bank stock it holds.

In addition to the 12 Reserve Banks, the System also consists, in part, of the Board of Governors and the Federal Open Market Committee ("FOMC"). The Board of Governors, an independent federal agency, is charged by the Federal Reserve Act with a number of specific duties, including general supervision over the Reserve Banks. The FOMC is composed of members of the Board of Governors, the president of the Federal Reserve Bank of New York ("FRBNY"), and, on a rotating basis, four other Reserve Bank presidents.

(2) Operations and Services

The Reserve Banks perform a variety of services and operations. These functions include participating in formulating and conducting monetary policy; participating in the payments system, including large-dollar transfers of funds, automated clearinghouse ("ACH") operations, and check collection; distributing coin and currency; performing fiscal agency functions for the U.S. Department of the Treasury ("Treasury"), certain federal agencies, and other entities; serving as the federal government's bank; providing short-term loans to depository institutions; providing loans to individuals, partnerships, and corporations in unusual and exigent circumstances; serving consumers and communities by providing educational materials and information regarding financial consumer protection rights and laws and information on community development programs and activities; and supervising bank holding companies, state member banks, and U.S. offices of foreign banking organizations. Certain services are provided to foreign and international monetary authorities, primarily by the FRBNY.

The FOMC, in conducting monetary policy, establishes policy regarding domestic open market operations, oversees these operations, and annually issues authorizations and directives to the FRBNY to execute transactions. The FOMC authorizes and directs the FRBNY to conduct operations in domestic markets, including the direct purchase and sale of Treasury securities, federal agency and government-sponsored enterprise ("GSE") debt securities, federal agency and GSE mortgage-backed securities ("MBS"), the purchase of these securities under agreements to resell, and the sale of these securities under agreements to repurchase. The FRBNY executes these transactions at the direction of the FOMC and holds the resulting securities and agreements in a portfolio known as the System Open Market Account ("SOMA"). The FRBNY is authorized to lend the Treasury securities and federal agency and GSE debt securities that are held in the SOMA.

In addition to authorizing and directing operations in the domestic securities market, the FOMC authorizes the FRBNY to execute operations in foreign markets in order to counter disorderly conditions in exchange markets or to meet other needs specified by the FOMC to carry out the System's central bank responsibilities. Specifically, the FOMC authorizes and directs the FRBNY to hold balances of, and to execute spot and forward foreign exchange and securities contracts for, 14 foreign currencies and to invest such foreign currency holdings, while maintaining adequate liquidity. The FRBNY is authorized and directed by the FOMC to maintain reciprocal currency arrangements with two central banks and to "warehouse" foreign currencies for the Treasury and the Exchange Stabilization Fund ("ESF"). The FRBNY is also authorized and directed by the FOMC to maintain U.S. dollar currency liquidity swap arrangements with 14 central banks. The FOMC has also authorized the FRBNY to maintain foreign currency liquidity swap arrangements with four foreign central banks.

Although the Reserve Banks are separate legal entities, they collaborate in the delivery of certain services to achieve greater efficiency and effectiveness. This collaboration takes the form of centralized operations and product or function offices that have responsibility for the delivery of certain services on behalf of the Reserve Banks. Various operational and management models are used and are supported by service agreements between the Reserve Banks. In some cases, costs incurred by a Reserve Bank for services provided to other Reserve Banks are not shared; in other cases, the Reserve Banks are reimbursed for costs incurred in providing services to other Reserve Banks.

(3) Financial Stability Activities

The Reserve Banks have implemented the following programs that support the liquidity of financial institutions and foster improved conditions in financial markets.

Expanded Open Market Operations and Support for Mortgage Related-Securities

The Single-Tranche Open Market Operation Program allows primary dealers to initiate a series of 28-day term repurchase transactions while pledging Treasury securities, federal agency and GSE debt securities, and federal agency and GSE MBS as collateral.

The Federal Agency and GSE Debt Securities and MBS Purchase Program provides support to the mortgage and housing markets and fosters improved conditions in financial markets. Under this program, the FRBNY purchases housing-related GSE debt securities and federal agency and GSE MBS. Purchases of housing-related GSE debt securities began in November 2008 and purchases of federal agency and GSE MBS began in January 2009. The FRBNY is authorized to purchase up to $200 billion in fixed rate, non-callable GSE debt securities and up to $1.25 trillion in fixed rate federal agency and GSE MBS. The activities of both of these programs are allocated to the other Reserve Banks.

Central Bank Liquidity Swaps

The FOMC authorized and directed the FRBNY to establish central bank liquidity swap arrangements, which may be structured as either U.S. dollar liquidity or foreign currency liquidity swap arrangements.

U.S. dollar liquidity swap arrangements were authorized with 14 foreign central banks to provide liquidity in U.S. dollars to overseas markets. Such arrangements were authorized with the following central banks: the Reserve Bank of Australia, the Banco Central do Brasil, the Bank of Canada, Danmarks Nationalbank, the Bank of England, the European Central Bank, the Bank of Japan, the Bank of Korea, the Banco de Mexico, the Reserve Bank of New Zealand, Norges Bank, the Monetary Authority of Singapore, the Sveriges Riksbank, and the Swiss National Bank. The maximum amount that could be drawn under these swap arrangements varied by central bank. The authorization for these swap arrangements expired on February 1, 2010.

Foreign currency liquidity swap arrangements provided the Reserve Banks with the capacity to offer foreign currency liquidity to U.S. depository institutions. Such arrangements were authorized with the Bank of England, the European Central Bank, the Bank of Japan, and the Swiss National Bank. The maximum amount that could be drawn under the swap arrangements varied by central bank. The authorization for these swap arrangements expired on February 1, 2010.

Lending to Depository Institutions

The Term Auction Facility ("TAF") promotes the efficient dissemination of liquidity by providing term funds to depository institutions. Under the TAF, Reserve Banks auction term funds to depository institutions against any collateral eligible to secure primary, secondary, and seasonal credit less a margin, which is a reduction in the assigned collateral value that is intended to provide the Reserve Banks additional credit protection. All depository institutions that are considered to be in generally sound financial condition by their Reserve Bank and that are eligible to borrow under the primary credit program are eligible to participate in TAF auctions. All loans must be collateralized to the satisfaction of the Reserve Banks.

Lending to Primary Dealers

The Term Securities Lending Facility ("TSLF") promoted liquidity in the financing markets for Treasury securities. Under the TSLF, the FRBNY could lend up to an aggregate amount of $200 billion of Treasury securities held in the SOMA to primary dealers secured for a term of 28 days. Securities were lent to primary dealers through a competitive single-price auction and were collateralized, less a margin, by a pledge of other securities, including Treasury securities, municipal securities, federal agency and GSE MBS, non-agency AAA/Aaa-rated private-label residential MBS, and asset-backed securities ("ABS"). The authorization for the TSLF expired on February 1, 2010.

The Term Securities Lending Facility Options Program ("TOP") offered primary dealers, through a competitive single-price auction, to purchase an option to draw upon short-term, fixed-rate TSLF loans in exchange for eligible collateral. The program enhanced the effectiveness of the TSLF by ensuring additional liquidity during periods of heightened collateral market pressures, such as around quarter-end dates. The program was suspended effective with the maturity of the June 2009 TOP options and the program authorization expired on February 1, 2010.

The Primary Dealer Credit Facility ("PDCF") was designed to improve the ability of primary dealers to provide financing to participants in the securitization markets. Primary dealers could obtain secured overnight financing under the PDCF in the form of repurchase transactions. Eligible collateral was that which could be pledged in tri-party arrangements, which primarily includes Treasury securities, federal agency and GSE MBS, other MBS, municipal securities, ABS, and money market equities. The interest rate charged on the secured financing was the Reserve Banks' primary credit rate. Participants paid a frequency-based fee if they accessed the program on more than 45 business days during the term of the program. Secured financing made under the PDCF was made with recourse to the primary dealer. The authorization for the PDCF expired on February 1, 2010.

The Transitional Credit Extension ("TCE") program provided liquidity support to broker-dealers that were in the process of transitioning to the bank holding company structure. Loans were collateralized similar to loans made under either the Reserve Banks' primary credit programs or the PDCF. The authorization for the TCE program expired on February 1, 2010.

Other Lending Facilities

The Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility ("AMLF") provided funding to depository institutions and bank holding companies to finance the purchase of eligible high-quality asset-backed commercial paper ("ABCP") from money market mutual funds. The program assisted money market mutual funds that hold such paper to meet the demands for investor redemptions and to foster liquidity in the ABCP market and money markets more generally. The Federal Reserve Bank of Boston ("FRBB") administered the AMLF and was authorized to extend these loans to eligible borrowers on behalf of the other Reserve Banks. All loans extended under the AMLF were non-recourse and were recorded as assets by the FRBB, and loans extended to borrowers that settle to depository accounts in other Districts were processed through the interdistrict settlement account. The credit risk related to the AMLF was assumed by the FRBB. The authorization for the AMLF expired on February 1, 2010.

The Commercial Paper Funding Facility ("CPFF program") enhanced the liquidity of the commercial paper market in the U.S. by increasing the availability of term commercial paper funding to issuers and by providing greater assurance to both issuers and investors that issuers would be able to roll over their maturing commercial paper. The authorization to purchase high-quality commercial paper through the CPFF program expired on February 1, 2010. The Commercial Paper Funding Facility LLC ("CPFF") is a Delaware limited liability company formed on October 14, 2008, in connection with the implementation of the CPFF program, to purchase eligible three-month unsecured commercial paper and ABCP directly from eligible issuers using the proceeds of loans made to CPFF by the FRBNY. CPFF is a single-member limited liability company, with the FRBNY as the sole and managing member. The FRBNY is the controlling party of CPFF and will remain as the controlling party as long as it retains an economic interest.

All lending to CPFF was made with recourse to the assets of CPFF. The interest rate on each loan to CPFF was the target federal funds rate and was fixed through the term of the loan. If the target federal funds rate was a range, the interest rate was set at the maximum rate within the range. Principal and accrued interest are payable to the FRBNY, in full, at the maturity date of the commercial paper. The FRBNY's loans to CPFF eliminate in consolidation.

To be eligible for purchase by CPFF, commercial paper was required to be (1) issued by a U.S. issuer (which includes U.S. issuers with a foreign parent company and U.S. branches of foreign banks) and (2) rated at least A-1/P-1/F1 by a nationally recognized statistical rating organization ("NRSRO") or, if rated by multiple NRSROs, was rated at least A-1/P-1/F1 by two or more. The commercial paper was also required to be U.S. dollar-denominated and have a three-month maturity. Commercial paper purchased by CPFF was discounted when purchased and carried at amortized cost. The maximum amount of a single issuer's commercial paper that CPFF could own at any time ("maximum face value limit") was the greatest amount of U.S. dollar-denominated commercial paper the issuer had outstanding on any day between January 1 and August 31, 2008. The CPFF did not purchase additional commercial paper from an issuer whose total commercial paper outstanding to all investors (including CPFF) equaled or exceeded the issuer's maximum face value limit.

Each issuer was required to pay a non-refundable facility fee upon registration with CPFF equal to 10 basis points of the issuer's maximum face value limit ("registration fee"). The CPFF program participants that issued unsecured commercial paper to CPFF were required to pay a surcharge of 100 basis points per annum of the face value ("credit enhancement fee"). The CPFF was authorized to reinvest cash in short-term and highly-liquid assets, which included Treasury securities, federal agency debt securities (excluding MBS), money market funds, repurchase agreements collateralized by Treasury securities and federal agency securities, and U.S. dollar-denominated overnight deposits. ABCP issuers that were inactive prior to the creation of the CPFF program were ineligible for participation. An issuer was considered inactive if it did not issue ABCP to institutions other than the sponsoring institution for any consecutive period of three months or longer between January 1 and August 31, 2008.

The Money Market Investor Funding Facility ("MMIFF") supported a private-sector initiative designed to provide liquidity to U.S. money market investors. Under the MMIFF, the FRBNY could provide senior secured funding to a series of special purpose vehicles ("SPV") to facilitate an industry-supported private-sector initiative to finance the purchase of eligible assets from eligible investors. No activity was recorded for the MMIFF in 2008 or 2009. The authorization for the MMIFF expired on October 30, 2009.

The Term Asset-Backed Securities Loan Facility ("TALF") assists financial markets in accommodating the credit needs of consumers and businesses of all sizes by facilitating the issuance of ABS collateralized by a variety of consumer and business loans; it is also intended to improve the market conditions for ABS. The Board of Governors has authorized the offering of TALF loans collateralized by newly issued ABS and legacy commercial mortgage-backed securities ("CMBS") until March 31, 2010 and TALF loans collateralized by newly issued CMBS until June 30, 2010.

Under the TALF, the FRBNY is authorized to lend up to $200 billion to eligible borrowers. Up to $100 billion of the total authorized TALF loans can have maturities of five years to finance purchases of CMBS, ABS backed by student loans, and ABS backed by loans guaranteed by the Small Business Administration ("SBA"). Interest proceeds paid on collateral supporting a five-year TALF loan or a three-year loan collateralized by CMBS may be used toward an accelerated repayment of the principal amount of the loan.

Each TALF loan is secured by eligible collateral, with the FRBNY lending an amount equal to the value of the collateral, as determined by the FRBNY, less a margin. Loan proceeds are disbursed to the borrower contingent on receipt by the FRBNY's custodian of the eligible collateral, an administrative fee, and, if applicable, a margin.

Eligible collateral includes U.S. dollar-denominated ABS that are (1) backed by student loans, auto loans, credit card loans, loans guaranteed by the SBA, loans or leases related to business equipment, leases of vehicle fleets, floor plan loans, mortgage servicing advances, and insurance premium finance loans that have a credit rating in the highest investment-grade rating category from two or more approved rating agencies and do not have a credit rating below the highest investment-grade rating category from a major rating agency, or (2) are newly issued CMBS or certain high-quality CMBS issued before January 1, 2009 ("legacy CMBS"). High-quality newly issued and legacy CMBS must have at least two AAA ratings from the approved ratings agencies and must not have a rating below AAA from any of these rating agencies. As of December 31, 2009, approved credit rating agencies for ABS included Fitch, Moody's Investors Service, and Standard & Poor's. The credit rating agencies for ABS were expanded in February 2010 to include DBRS and Realpoint. As of December 31, 2009, approved credit rating agencies for CMBS included Fitch, Moody's Investors Service, Standard & Poor's, DBRS, and Realpoint. Prior to its acceptance by the FRBNY, pledged collateral must also have met other risk assessment criteria as stipulated in the TALF program's terms and conditions.

The TALF loans are extended on a non-recourse basis. If the borrower does not repay the loan, the FRBNY will enforce its rights in the collateral and may sell the collateral to TALF LLC, a Delaware limited liability company, established for the purpose of purchasing such assets. As of December 31, 2009, the FRBNY had not enforced its rights to any of the collateral and, as a result, TALF LLC did not purchase such assets.

Pursuant to a put agreement with the FRBNY, TALF LLC has committed to purchase assets that secured a TALF loan at a price equal to the principal amount outstanding plus accrued but unpaid interest, regardless of fair value of the collateral. TALF LLC's purchases of these securities are funded first through the fees received by TALF LLC from the FRBNY for this commitment and any interest earned on its investments. The fee represents the spread on the TALF loans, which is the TALF loan interest rate paid by the TALF borrower less the overnight indexed swap ("OIS") rate plus 25 basis points. In the event that such funding proves insufficient for the asset purchases that TALF LLC has committed to make under the put agreement, the Treasury, as a subordinated lender, has committed to lend up to $20 billion to TALF LLC at a rate of the one-month London Interbank Offered Rate ("LIBOR") plus 300 basis points. The FRBNY has agreed to lend up to $180 billion to TALF LLC in the form of senior debt at a rate of the one-month LIBOR plus 100 basis points. Both the senior, when funded, and subordinated loans to TALF LLC are secured by all of the assets of TALF LLC through a pledge to Bank of New York Mellon as the collateral agent. The FRBNY is the managing member and the controlling party of TALF LLC and will remain as the controlling party as long as it retains an interest. After TALF LLC has paid all operating expenses and principal due to the FRBNY, the remaining proceeds of the portfolio holdings will be distributed in the following order, principal due to Treasury, interest due to the FRBNY, and interest due to Treasury. Any residual cash flows will be shared between the FRBNY, which will receive 10 percent, and the Treasury, which will receive 90 percent as contingent interest.

Support for Specific Institutions

Bear Stearns Companies, Inc.

In connection with and to facilitate the merger of The Bear Stearns Companies, Inc. ("Bear Stearns") and JPMorgan Chase & Co. ("JPMC"), the FRBNY extended credit to Maiden Lane LLC ("ML") in June 2008. ML is a Delaware limited liability company formed by the FRBNY to acquire certain assets of Bear Stearns and to manage those assets over time, in order to maximize the potential for the repayment of the credit extended to ML and to minimize disruption to the financial markets. The assets acquired by ML were valued at $29.9 billion as of March 14, 2008, the date that the FRBNY committed to the transaction, and largely consisted of federal agency and GSE MBS, non-agency residential mortgage-backed securities ("non-agency RMBS"), commercial and residential mortgage loans, and derivatives. The FRBNY extended a senior loan of approximately $28.8 billion and JPMC extended a subordinated loan of $1.15 billion to finance the acquisition of the assets through a pledge to State Street as the collateral agent. The interest rate on the senior loan is the primary credit rate in effect from time to time. JPMC bears the first $1.15 billion of any losses associated with the portfolio through its subordinated loan. Residual gains, if any, will be allocated to the FRBNY. The interest rate on the JPMC subordinated loan is the primary credit rate plus 450 basis points. The loans are collateralized by all of the assets of ML. The FRBNY is the sole and managing member and the controlling party of ML and will remain as such as long as the FRBNY retains an economic interest in ML.

American International Group, Inc.

In September 2008, the Board of Governors authorized the FRBNY to lend to American International Group, Inc., ("AIG"). Initially, the FRBNY provided AIG with a line of credit collateralized by the pledge of a substantial portion of the assets of AIG. Under the provisions of the original agreement, the FRBNY was authorized to lend up to $85 billion to AIG for two years at the three-month LIBOR, with a floor of 350 basis points, plus 850 basis points. In addition, the FRBNY assessed AIG a one-time commitment fee of 200 basis points on the full amount of the commitment and a fee of 850 basis points per annum on the undrawn credit line. A condition of the credit agreement was that AIG would issue to a trust, for the sole benefit of the fiscal treasury, preferred shares convertible to approximately 78 percent of the issued and outstanding shares of the common stock of AIG. The AIG Credit Facility Trust ("Trust") was formed January 16, 2009, and the preferred shares were issued to the Trust on March 4, 2009. The Trust has three independent trustees who control the Trust's voting and consent rights. The FRBNY cannot exercise voting or consent rights. On October 8, 2008, the FRBNY began providing cash collateral to certain AIG insurance subsidiaries in connection with AIG's domestic securities lending program.

The FRBNY and the Treasury announced a restructuring of the government's financial support to AIG in November 2008. As part of the restructuring, the Treasury purchased $40 billion of newly issued AIG preferred shares under the Troubled Asset Relief Program ("TARP"). The TARP funds were used to pay down AIG's debt to the FRBNY. In addition, the terms of the original agreement were modified to reduce the line of credit to $60 billion; reduce the interest rate to the three-month LIBOR with a floor of 350 basis points, plus 300 basis points; reduce the fee on undrawn funds to 75 basis points; and extend the term of the agreement to five years. The other material terms of the funding were unchanged. These revised terms were more consistent with terms granted to other entities with similar credit risk.

Concurrent with the November 2008 restructuring of its financial support to AIG, the FRBNY established two limited liability companies ("LLCs"). The FRBNY extended credit to Maiden Lane II LLC ("ML II"), a Delaware limited liability company formed to purchase non-agency RMBS from the reinvestment pool of the securities lending portfolio of several regulated U.S. insurance subsidiaries of AIG. ML II borrowed $19.5 billion from the FRBNY and used the proceeds to purchase non-agency RMBS that had an approximate fair value of $20.8 billion as of October 31, 2008 from AIG's domestic insurance subsidiaries. The FRBNY is the sole and managing member and the controlling party of ML II and will remain as the controlling party as long as the FRBNY retains an economic interest in ML II. Net proceeds received by ML II will be applied to pay the FRBNY's senior loan plus interest at one-month LIBOR plus 100 basis points. As part of the agreement, the AIG subsidiaries also received from ML II a fixed deferred purchase price of up to $1.0 billion, plus interest on any such fixed deferred purchase price outstanding at one-month LIBOR plus 300 basis points, payable from the net proceeds received by ML II and only to the extent that the FRBNY's senior loan, including accrued and unpaid interest, has been paid in full. After ML II has paid the FRBNY's senior loan, including accrued and unpaid interest, and the fixed deferred purchase price in full, including accrued and unpaid interest, the FRBNY will be entitled to receive five-sixths of any additional net proceeds received by ML II as contingent interest on the senior loan and the AIG subsidiaries will be entitled to receive one-sixth of any net proceeds received by ML II as variable deferred purchase price. The FRBNY's loan and the fixed deferred purchase price of the AIG subsidiaries are collateralized by all of the assets of ML II through a pledge to Bank of New York Mellon as the collateral agent. As a result of the formation and commencement of operations of ML II, the FRBNY's lending in connection with AIG's securities lending program was terminated.

The FRBNY also extended credit to Maiden Lane III LLC ("ML III"), a Delaware limited liability company formed to purchase ABS collateralized debt obligations ("ABS CDOs") from certain third-party counterparties of AIG Financial Products Corp. ("AIGFP"). In connection with the acquisitions, the third-party counterparties agreed to terminate their related credit default swap ("CDS") contracts with AIGFP. ML III borrowed approximately $24.3 billion from the FRBNY and AIG provided an equity contribution of $5 billion to ML III. The proceeds were used to purchase ABS CDOs with a fair value of $29.6 billion. The counterparties received $26.8 billion net of principal, interest received, and finance charges paid. ML III also made a payment to AIGFP of $2.5 billion, representing the return of excess collateral previously posted by AIGFP with the counterparties. The FRBNY is the managing member and the controlling party of ML III and will remain as the controlling party as long as the FRBNY retains an economic interest in ML III. Net proceeds received by ML III will be applied to repay the FRBNY's senior loan plus interest at one-month LIBOR plus 100 basis points. The FRBNY's senior loan is collateralized by all of the assets of ML III through a pledge to Bank of New York Mellon as the collateral agent. After payment of principal and accrued and unpaid interest on the FRBNY's senior loan in full, AIG, or its assignee, is entitled to receive from ML III repayment of its equity contribution, including accrued and unpaid interest at one-month LIBOR plus 300 basis points, payable from net proceeds received by ML III as additional interest. After ML III has paid the FRBNY's senior loan and AIG's equity contribution in full, the FRBNY will be entitled to receive two-thirds of any additional net proceeds received by ML III on the senior loan and AIG, or its assignee, will be entitled to receive one-third of any net proceeds received by ML III as contingent distributions on its equity interest.

On April 17, 2009, the FRBNY, as part of the U.S. government's commitment to the orderly restructuring of AIG over time, in the face of continuing market dislocations, additionally restructured the AIG loan by lowering the interest rate. Effective April 17, 2009, the 350 basis-point floor on LIBOR used to calculate the interest rate on the loan was eliminated. The interest rate on the modified loan is the three-month LIBOR plus 300 basis points.

On December 1, 2009, the FRBNY's commitment to lend to AIG was reduced to $35 billion and the outstanding balance of the FRBNY's loan to AIG was reduced by $25 billion in exchange for a liquidation preference of nonvoting perpetual preferred interests in two limited liability companies. AIG created these limited liability companies to hold, directly or indirectly, all of the outstanding common stock of American Life Insurance Company ("ALICO") and American International Assurance Company Ltd. ("AIA"), two life insurance holding company subsidiaries of AIG. The FRBNY will be paid a 5 percent cumulative dividend on its nonvoting preferred interests through September 22, 2013 and a 9 percent cumulative dividend thereafter. Although the FRBNY has certain governance rights to protect its interests, AIG retains control of the limited liability companies and the underlying operating companies. The initial value of the FRBNY's preferred interests, which represents a percentage of the fair market value of ALICO and AIA at December 1, 2009, was $16 billion for the AIA Aurora LLC ("AIA LLC") and $9 billion for the ALICO Holdings LLC ("ALICO LLC").

In addition, the FRBNY was authorized to make loans of up to $8.5 billion to other SPVs established by AIG or its subsidiaries. Loans extended by the FRBNY to these SPVs would have been repaid from net cash flows of designated blocks of existing life insurance policies issued by certain domestic insurance subsidiaries of AIG. No loans were made under this authorization during the year ended December 31, 2009. On February 26, 2010, AIG stated in its 2009 annual report filed with the Securities and Exchange Commission that it was no longer pursuing this transaction.

Citigroup, Inc.

The Board of Governors, the Treasury, and the FDIC ("parties") jointly announced on November 23, 2008, that they would provide financial support to Citigroup, Inc. ("Citigroup"). The agreement provided funding support for possible future principal losses on up to $301 billion of Citigroup's assets. The funding support was for a period of ten years for residential assets and five years for non-residential assets. Under the agreement, a loss on a portfolio asset would have included a charge-off or realized loss upon collection, through a permitted disposition or exchange, or upon a foreclosure or short-sale loss, but not through a change in Citigroup's mark-to-market accounting for the asset or the creation or increase of a related loss reserve. The FRBNY's commitment to lend under the agreement would have been triggered at the time that qualifying losses of $56.2 billion were recognized in the covered assets pool. At that point, if Citigroup made a proper election, the FRBNY would have made a single non-recourse loan to Citigroup in an amount equal to the aggregate adjusted baseline value of the remaining covered assets, as defined in the relevant agreements. Under this agreement, no loans were made during the years ended December 31, 2009 and 2008. On December 23, 2009, the parties terminated the arrangement and, as consideration for terminating the agreement, Citigroup paid the FRBNY a $50 million termination fee and agreed to reimburse the FRBNY for its out-of-pocket expenses.

Bank of America Corporation

The parties jointly announced on January 15, 2009, that they would provide financial support to Bank of America Corporation (“Bank of America”). Under this arrangement, the Federal Reserve Bank of Richmond (“FRBR”) would have provided funding support for possible future principal losses relating to a designated pool of up to $118 billion of financial instruments. The FRBR’s commitment under the arrangement was to provide non-recourse loans to Bank of America if, and when, qualifying losses of $18 billion were recorded in the pool. On September 21, 2009, however, the parties announced that they had reached an agreement with Bank of America to terminate the agreement. As part of the termination of the agreement, Bank of America paid $57 million in compensation for out-of-pocket expenses incurred by the FRBR and an amount equal to the commitment fees required by the agreement.

(4) Significant Accounting Policies

Accounting principles for entities with the unique powers and responsibilities of a 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 the *Financial Accounting Manual for Federal Reserve Banks* (“Financial Accounting Manual” or “FAM”), which is issued by the Board of Governors. The Reserve Banks are required to adopt and apply accounting policies and practices that are consistent with the FAM and the combined financial statements have been prepared in accordance with the FAM.

Limited differences exist between the accounting principles and practices in the FAM and generally accepted accounting principles in the United States (“GAAP”), primarily due to the unique nature of the Reserve Banks’ powers and responsibilities as the nation’s central bank. The primary difference is the presentation of all SOMA securities holdings at amortized cost rather than the fair value presentation required by GAAP. Treasury securities, GSE debt securities, federal agency and GSE MBS, and investments denominated in foreign currencies comprising the SOMA are recorded at cost on a settlement-date basis rather than the trade-date basis required by GAAP. The cost basis of Treasury securities, GSE debt securities, and foreign government debt instruments is adjusted for amortization of premiums or accretion of discounts on a straight-line basis. Amortized cost more appropriately reflects the Reserve Banks’ securities holdings given the System’s unique responsibility to conduct monetary policy. Accounting for these securities on a settlement-date basis more appropriately reflects the timing of the transaction’s effect on the quantity of reserves in the banking system. Although the application of fair-value measurements to the securities holdings may result in values substantially above or below their carrying values, these unrealized changes in value have no direct effect on the quantity of reserves available to the banking system or on the prospects for future Reserve Bank earnings or capital. 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 objectives rather than profit. Accordingly, fair values, earnings, and 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.

In addition, the Reserve Banks have elected not to present a Combined Statement of Cash Flows because the liquidity and cash position of the Reserve Banks are not a primary concern given the Reserve Banks’ unique powers and responsibilities. Other information regarding the Reserve Banks’ activities is provided in, or may be derived from, the Combined Statements of Condition, Income and Comprehensive Income, and Changes in Capital. There are no other significant differences between the policies outlined in the FAM and GAAP.

Preparing the combined financial statements in conformity with the FAM requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Certain amounts relating to the prior year have been reclassified to conform to the current-year presentation. The classification of certain variable interest entities ("VIE") assets have been reclassified as follows: RMBS and non agency CMOs have been reclassified as Non-agency RMBS and agency CMOs and TBA commitments have been reclassified as federal agency and GSE MBS. Unique accounts and significant accounting policies are explained below.

(a) Consolidation

The combined financial statements include the accounts and results of operations of the Reserve Banks as well as several VIEs, which include ML, ML II, ML III, CPFF, and TALF LLC. The consolidation of the VIEs was assessed in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification (ASC) Topic 810 (ASC 810), *Consolidation* (previously FIN 46R), which requires a variable interest entity to be consolidated by its controlling financial interest holder. Intercompany balances and transactions have been eliminated in consolidation.

A Reserve Bank consolidates a VIE if it has a controlling financial interest because it will absorb a majority of the entity's expected losses, receive a majority of the entity's expected residual returns, or it is most closely associated with the VIE. To determine whether it is the controlling financial interest holder of a VIE, the Reserve Bank evaluates the VIE's design, capital structure, and relationships with the variable interest holders. The Reserve Bank reconsiders whether it is the controlling financial interest holder of a VIE, as required by ASC 810, when certain events occur.

(b) Gold and Special Drawing Rights Certificates

The Secretary of the Treasury is authorized to issue gold and special drawing rights ("SDR") certificates to the Reserve Banks.

Payment for the gold certificates by the Reserve Banks is made by crediting equivalent amounts in dollars into the account established for the Treasury. The gold certificates held by the Reserve Banks are required to be backed by the gold of the Treasury. The Treasury may reacquire the gold certificates at any time and the Reserve Banks must deliver them to the Treasury. At such time, the Treasury's account is charged, and the Reserve Banks' gold certificate accounts are reduced. The value of gold for purposes of backing the gold certificates is set by law at $42 2/9 per fine troy ounce. The Board of Governors allocates the gold certificates among the Reserve Banks once a year based on the average Federal Reserve notes outstanding in each Reserve Bank.

SDR certificates are issued by the International Monetary Fund (the "Fund") to its members in proportion to each member's quota in the Fund at the time of issuance. SDR certificates 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 to the Reserve Banks. When SDR certificates are issued to the Reserve Banks, equivalent amounts in U.S. dollars are credited to the account established for the Treasury and the Reserve Banks' SDR certificate accounts are increased. The Reserve Banks are required to purchase SDR certificates, at the direction of the Treasury, for the purpose of financing SDR acquisitions or for financing exchange stabilization operations. At the time SDR transactions occur, the Board of Governors allocates SDR certificate transactions among the Reserve Banks based upon each Reserve Bank's Federal Reserve notes outstanding at the end of the preceding year. There were no SDR transactions in 2008, and in 2009 the Treasury issued $3 billion in SDR certificates to the Reserve Banks.

(c) Loans to Depository Institutions and Other Loans

Loans, except for loans extended under TALF, are reported at their outstanding principal balances net of unamortized administrative or commitment fees, and interest income is recognized on an accrual basis. Loan administrative and commitment fees are generally deferred and amortized on a straight-line basis over the term of the loan or commitment period. This method results in an interest amount that is substantially similar to the interest method.

Loans are impaired when, based on current information and events, it is probable that the Reserve Banks will not receive the principal or interest that is due in accordance with the contractual terms of the loan agreement. Loans are evaluated to determine whether an allowance for loan loss is required. The Reserve Banks have developed procedures for assessing the adequacy of any allowance for loan losses using all available information to reflect the assessment of credit risk. This assessment includes monitoring information obtained from banking supervisors, borrowers, and other sources to assess the credit condition of the borrowers and, as appropriate, evaluating collateral values for each program. Generally, the Reserve Banks discontinue recognizing interest income on impaired loans until the borrower's repayment performance demonstrates principal and interest will be received in accordance with the term of the loan agreement. If a Reserve Bank discontinues recording interest on an impaired loan, cash payments are first applied to principal until the loan balance is reduced to zero; subsequent payments are applied as recoveries of amounts previously deemed uncollectible, if any, and then as interest income.

Impaired loans include loans that have been modified in debt restructurings involving borrowers experiencing financial difficulties. The allowance for loan restructuring is determined by discounting the restructured cash flows using the original effective rate for the loan. Similar to other impaired loans, the Reserve Banks discontinue recognizing interest income until the borrower demonstrates that it can meet the restructured terms. Performance prior to the restructuring, or significant events that coincide with the restructuring, are considered in assessing whether the borrower can meet the new terms and, if so, the Reserve Banks may resume recording interest income.

The FRBNY has elected to record the TALF loans at fair value in accordance with FASB ASC Topic 825 (ASC 825), *Fair Value Option* (previously SFAS 159). Unrealized gains (losses) on TALF loans that are recorded at fair value are reported as "Non-interest income (loss): Other loans unrealized gains" in the Combined Statements of Income and Comprehensive Income. The interest income on TALF loans is recognized based on the contracted rate and is reported as a component of "Interest Income: Other loans" in the Combined Statements of Income and Comprehensive Income. Administrative fees paid by borrowers at the initiation of each loan are recognized as incurred and not deferred, are reported as a component of "Non-interest income (loss): Other income" in the Combined Statements of Income and Comprehensive Income.

(d) Securities Purchased Under Agreements to Resell, Securities Sold Under Agreements to Repurchase, and Securities Lending

The FRBNY may engage in purchases of securities with primary dealers under agreements to resell ("repurchase transactions"). These repurchase transactions are typically executed through a tri-party arrangement ("tri-party transactions"). Tri-party transactions are conducted with two commercial custodial banks that manage the clearing, settlement, and pledging of collateral. The collateral pledged must exceed the principal amount of the transaction. Acceptable collateral under tri-party repurchase transactions primarily includes Treasury securities; pass-through mortgage securities of Fannie Mae, Freddie Mac, and Ginnie Mae; STRIP Treasury securities; and "stripped" securities of federal agencies. The tri-party transactions are accounted for as financing transactions with the associated interest income accrued over the life of the transaction. Repurchase transactions are reported at their contractual amount as "System Open Market Account: Securities purchased under agreements to resell" in the Combined Statements of Condition and the related accrued interest receivable is reported as a component of "Accrued interest receivable."

The FRBNY may engage in sales of securities with primary dealers under agreements to repurchase ("reverse repurchase transactions"). These reverse repurchase transactions may be executed through a tri-party arrangement, similar to repurchase transactions. Reverse repurchase transactions may also be executed with foreign official and international accounts. Reverse repurchase transactions are accounted for as financing transactions, and the associated interest expense is recognized over the life of the transaction. These transactions are reported at their contractual amounts in the Combined Statements of Condition and the related accrued interest payable is reported as a component of "Other liabilities."

Treasury securities and GSE debt securities held in the SOMA are lent to primary dealers to facilitate the effective functioning of the domestic securities market. Overnight securities lending transactions are fully collateralized by other Treasury securities. TSLF transactions are fully collateralized with investment-grade debt securities, collateral eligible for tri-party repurchase agreements arranged by the FRBNY, or both. The collateral taken in both overnight and term securities lending transactions is in excess of the fair value of the securities lent. The FRBNY charges the primary dealer a fee for borrowing securities, and these fees are reported as a component of "Other income." In addition, TOP fees are reported as a component of "Other income."

Activity related to securities purchased under agreements to resell, securities sold under agreements to repurchase, and securities lending is allocated to each of the Reserve Banks on a percentage basis derived from an annual settlement of the interdistrict settlement account that occurs in April each year.

The settlement also equalizes Reserve Bank gold certificate holdings to Federal Reserve notes outstanding in each District.

(e) Treasury Securities; Government-Sponsored Enterprise Debt Securities; Federal Agency and Government-Sponsored Enterprise Mortgage-Backed Securities; Investments Denominated in Foreign Currencies; and Warehousing Agreements

Interest income on Treasury securities, GSE debt securities, and investments denominated in foreign currencies comprising the SOMA is accrued on a straight-line basis. Interest income on federal agency and GSE MBS is accrued using the interest method and includes amortization of premiums, accretion of discounts, and paydown gains or losses. Paydown gains or losses result from scheduled payment and prepayment of principal and represent the difference between the principal amount and the carrying value of the related security. Gains and losses resulting from sales of securities are determined by specific issue based on average cost.

In addition to outright purchases of federal agency and GSE MBS that are held in the SOMA, the FRBNY enters into dollar roll transactions ("dollar rolls"), which primarily involve an initial transaction to purchase or sell "to be announced" ("TBA") MBS combined with an agreement to sell or purchase TBA MBS on a specified future date. The FRBNY's participation in the dollar roll market furthers the MBS Purchase Program goal of providing support to the mortgage and housing markets and fostering improved conditions in financial markets. The FRBNY accounts for outstanding commitments to sell or purchase TBA MBS on a settlement-date basis. Based on the terms of the FRBNY dollar roll transactions, 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 (ASC 860), *Accounting for Transfers of Financial Assets and Repurchase Financing Transactions,* (previously SFAS 140), and the related outstanding commitments are accounted for as sales or purchases upon settlement.

Activity related to Treasury securities, GSE debt securities, and federal agency and GSE MBS, including the premiums, discounts, and realized gains and losses, is allocated to each Reserve Bank on a percentage basis derived from an annual settlement of the interdistrict settlement account that occurs in April of each year. The settlement also equalizes Reserve Bank gold certificate holdings to Federal Reserve notes outstanding in each District. Activity related to investments denominated in foreign currencies, including the premiums, discounts, and realized and unrealized gains and losses, is allocated to each Reserve Bank based on the ratio of each Reserve Bank's capital and surplus to aggregate capital and surplus at the preceding December 31.

Foreign-currency-denominated assets are revalued daily at current foreign currency market exchange rates in order to report these assets in U.S. dollars. Realized and unrealized gains and losses on investments denominated in foreign currencies are reported as "Foreign currency gains or losses" in the Combined Statements of Income and Comprehensive Income.

Warehousing 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 over 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.

Warehousing agreements are designated as held-for-trading purposes and are valued daily at current market exchange rates. Activity related to these agreements is allocated to each Reserve Bank based on the ratio of each Reserve Bank's capital and surplus to aggregate capital and surplus at the preceding December 31.

(f) Central Bank Liquidity Swaps

Central bank liquidity swaps, which are transacted between the FRBNY and a foreign central bank, may be structured as either U.S. dollar liquidity or foreign currency liquidity swap arrangements.

Activity related to U.S. dollar and foreign currency swap transactions, including the related income and expense, is allocated to each Reserve Bank based on the ratio of each Reserve Bank's capital and surplus to aggregate capital and surplus at the preceding December 31. Similar to investments denominated in foreign currencies, the foreign currency amounts associated with these central bank liquidity swap arrangements are revalued at current foreign currency market exchange rates.

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 that the FRBNY acquires is reported as "Central bank liquidity swaps" on the Combined Statements of Condition. Because the swap transaction will be unwound at the same U.S. dollar amount and exchange rate that was used in the initial transaction, the recorded value of the foreign currency amounts is not affected by changes in the market exchange rate.

The foreign central bank compensates the FRBNY based on the foreign currency amounts held for the FRBNY. The FRBNY recognizes compensation during the term of the swap transaction and reports it as "Interest income: Central bank liquidity swaps" in the Combined Statements of Income and Comprehensive Income.

Foreign currency liquidity swaps

At the initiation of each foreign currency liquidity swap transaction, the FRBNY will transfer, at the prevailing market exchange rate, 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 would be reported as a liability by the Reserve Banks. Concurrent with this transaction, the FRBNY and the foreign central bank agree to a second transaction that obligates the FRBNY to return the foreign currency and the foreign central bank to return the U.S. dollars on a specified future date. The FRBNY compensates the foreign central bank based on the foreign currency transferred to the FRBNY. For each foreign currency swap transaction with a foreign central bank it is anticipated that the FRBNY will enter into a corresponding transaction with a U.S. depository institution in order to provide foreign currency liquidity to that institution. No foreign currency liquidity swap transactions occurred in 2008 or 2009.

(g) Investments Held by Consolidated Variable Interest Entities

Investments of the consolidated VIEs include commercial paper, federal agency and GSE MBS, commercial and residential real estate mortgage loans, non-agency RMBS, CDOs, other investment securities, other real estate owned, and derivatives. These investments are accounted for and classified as follows:

- Commercial paper held by the CPFF is designated as held-to-maturity under FASB ASC Topic 320 (ASC 320), *Investments — Debt and Equity Securities* (previously SFAS 115) according to the terms of the CPFF program. The FRBNY has the positive intent and the ability to hold the securities to maturity and, therefore, the commercial paper is recorded at amortized cost. The amortization of premiums and accretion of discounts is recorded on a straight-line basis that is not materially different from the interest method. Interest income on the commercial paper is reported as "Interest income: Investments held by consolidated variable interest entities" in the Combined Statements of Income and Comprehensive Income. All other investments, consisting of short-term highly liquid assets, held by the CPFF are classified as trading securities under ASC 320 and are recorded at fair value.

  The FRBNY evaluates commercial paper for impairment on a quarterly basis. An investment is impaired if its fair value falls below its recorded value and the decline is considered other-than-temporary. An other-than-temporary-impairment is triggered if (1) the FRBNY has the intent to sell the security, (2) it is more likely than not that the FRBNY will be required to sell the security before recovery of its recorded investment, or (3) the FRBNY does not expect to recover the entire amortized cost basis of the security even if it does not intend to sell the security.

- ML follows the guidance in ASC 320 when accounting for investments in debt securities. ML classifies its debt securities as available for sale and has elected the fair-value option for all eligible assets and liabilities in accordance with ASC 825. Other financial instruments, including derivatives contracts in ML, are recorded at fair value in accordance with FASB ASC Topic 815 (ASC 815), *Derivatives and Hedging* (previously SFAS 133).

- ML II and ML III qualify as non-registered investment companies under the provisions of the American Institute of Certified Public Accountants' *Audit and Accounting Guide for Investment Companies* and, therefore, all investments are recorded at fair value in accordance with FASB ASC Topic 946 (ASC 946), *Financial Services-Investment Companies* (previously the American Institute of Certified Public Accountants *Audit and Accounting Guide for Investment Companies*).

- TALF LLC follows the guidance in ASC 320 when accounting for ABS investments once obtained. All other investments held by the TALF LLC are classified as available for sale securities under

ASC 320 and TALF LLC has elected the fair value option for all eligible assets in accordance with ASC 825. These assets are recorded as "Investments held by consolidated variable interest entities" in the Combined Statements of Condition.

- Interest income, accretion of discounts, amortization of premiums on investments, and paydown gains and losses on federal agency and GSE MBS, non-agency RMBS, and CMOs held by consolidated VIEs are reported in "Interest income: Investments held by consolidated variable interest entities" in the Combined Statements of Income and Comprehensive Income. Realized and unrealized gains (losses) on investments in consolidated VIEs that are recorded at fair value are reported as "Non-interest income (loss): Investments held by consolidated variable interest entities losses, net" in the Combined Statements of Income and Comprehensive Income.

(h) Preferred Securities

As part of the restructuring of the AIG loan, the FRBNY was issued preferred securities in AIA LLC and ALICO LLC, which were created to hold all of the outstanding common stock of AIA and ALICO, respectively. The preferred securities are presented at cost consistent with ASC 320 and are reported on the Combined Statements of Condition as "Preferred securities." The 5 percent cumulative dividend accrued on the preferred securities is reported as "Dividends on preferred securities" on the Combined Statements of Income and Comprehensive Income. On a quarterly basis, the accrued dividends are capitalized and increase the recorded cost of the FRBNY's preferred interest in AIA LLC and ALICO LLC. A preferred security is impaired if its fair value falls below its recorded value and the decline is considered other-than-temporary. An other-than-temporary impairment is triggered if (1) the FRBNY has the intent to sell the security, (2) it is more likely than not that the FRBNY will be required to sell the security before recovery of its recorded investment, or (3) the FRBNY does not expect to recover the entire amortized cost basis of the security even if it does not intend to sell the security. Dividends are accrued unless the impairment analysis indicates that the dividends will not be collected.

(i) Bank Premises, Equipment, and Software

Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, which range from two to 50 years. Major alterations, renovations, and improvements are capitalized at cost as additions to the asset accounts and are depreciated over the remaining useful life of the asset or, if appropriate, over the unique useful life of the alteration, renovation, or improvement. Maintenance, repairs, and minor replacements are charged to operating expense in the year incurred.

Costs incurred for software during the application development stage, whether developed internally or acquired for internal use, are capitalized based on the purchase cost and the cost of direct services and materials associated with designing, coding, installing, and testing the software. Capitalized software costs are amortized on a straight-line basis over the estimated useful lives of the software applications, which range from two to five years. Maintenance costs related to software are charged to expense in the year incurred.

Capitalized assets, including software, buildings, leasehold improvements, furniture, and equipment, are impaired and an adjustment is recorded when events or changes in circumstances indicate that the carrying amount of assets or asset groups is not recoverable and significantly exceeds the assets' fair value.

(j) Federal Reserve Notes

Federal Reserve notes are the circulating currency of the United States. These notes, which are identified as issued to a specific Reserve Bank, must be fully collateralized. Assets eligible to be pledged as collateral security include all of the Reserve Banks' assets. The collateral value is equal to the book value of the collateral tendered with the exception of securities, for which the collateral value is equal to the par value of the securities tendered. The par value of securities pledged for securities sold under agreements to repurchase is deducted.

The Board of Governors may, at any time, call upon a Reserve Bank for additional security to adequately collateralize the outstanding Federal Reserve notes. To satisfy the obligation to provide sufficient collateral for outstanding Federal Reserve notes, the Reserve Banks have entered into an agreement that provides for certain assets of the Reserve Banks to be jointly pledged as collateral for the Federal Reserve notes issued to all Reserve Banks. In the event that this collateral is insufficient, the Federal Reserve Act provides that Federal Reserve notes become a first and paramount lien on all the assets of the Reserve Banks. Finally, Federal Reserve notes are obligations of the United States government. At December 31, 2009 and 2008, all Federal Reserve notes issued to the Reserve Banks were fully collateralized.

"Federal Reserve notes outstanding, net" in the Combined Statements of Condition represents the Federal Reserve notes outstanding, reduced by the Reserve Banks' currency holdings of $193,141 million and $169,681 million at December 31, 2009 and 2008, respectively.

At December 31, 2009, all Federal Reserve notes were fully collateralized. All gold certificates, all special drawing rights certificates, and $871,609 million of domestic securities and securities purchased under agreements to resell were pledged as collateral. At December 31, 2009, no investments denominated in foreign currencies were pledged as collateral.

(k) Beneficial Interest in Consolidated Variable Interest Entities

ML, ML II, ML III, and TALF LLC have outstanding senior and subordinated financial interests, inclusive of a fixed deferred purchase price in ML II and an equity contribution in ML III. Upon issuance of the senior and subordinated financial interests, ML, ML II, ML III, and TALF LLC each elected to measure these obligations at fair value in accordance with ASC 825. Principal, interest, and changes in fair value on the senior financial interest, which were extended by the FRBNY, are eliminated in consolidation. The subordinated financial interest is recorded at fair value as "Beneficial interest in consolidated variable interest entities" in the Combined Statements of Condition. Interest expense and changes in fair value of the subordinated financial interest are recorded in "Interest expense: Beneficial interest in consolidated variable interest entities" and "Non-interest income (loss): Beneficial interest in consolidated variable interest entities losses, net," respectively, in the Combined Statements of Income and Comprehensive Income.

(l) Treasury Supplemental Financing Account and Other Deposits

The Treasury's temporary supplementary program consists of a series of Treasury bill auctions, in addition to Treasury's standard borrowing program. The proceeds of this debt are held in an account at the FRBNY that is separate from the Treasury's general account, and which is reported as "Treasury, supplementary financing account" in the Combined Statements of Condition. The purpose of placing funds in this account is to drain reserves from the banking system and partially offset the reserve impact of the Reserve Bank's lending and liquidity initiatives.

Other deposits represent amounts held in accounts at the Reserve Banks by GSEs and foreign central banks and governments.

(m) Items in Process of Collection and Deferred Credit Items

"Items in process of collection" in the Combined Statements of Condition primarily represents amounts attributable to checks that have been deposited for collection and that, as of the balance sheet date, have not yet been presented to the paying bank. "Deferred credit items" are the counterpart liability to items in process of collection. The amounts in this account arise from deferring credit for deposited items until the amounts are collected. The balances in both accounts can vary significantly.

(n) Capital Paid-in

The Federal Reserve Act requires that each member bank subscribe to the capital stock of the Reserve Bank in an amount equal to six percent of the capital and surplus of the member bank. These shares are nonvoting with a par value of $100 and may not be transferred or hypothecated. As a member bank's capital and surplus changes, its holdings of Reserve Bank stock must be adjusted. Currently, only one-half of the subscription is paid-in and the remainder is subject to call. A member bank is liable for Reserve Bank liabilities up to twice the par value of stock subscribed by it.

By law, each Reserve Bank is required to pay each member bank an annual dividend of six percent on the paid-in capital stock. This cumulative dividend is paid semiannually. To reflect the Federal Reserve Act requirement that annual dividends be deducted from net earnings, dividends are presented as a distribution of comprehensive income in the Combined Statements of Income and Comprehensive Income.

(o) Surplus

The Board of Governors requires the Reserve Banks to maintain a surplus equal to the amount of capital paid-in as of December 31 of each year. Accumulated other comprehensive income is reported as a component of surplus in the Combined Statements of Condition and the Combined Statements of

Changes in Capital. The balance of accumulated other comprehensive income is comprised of expenses, gains, and losses related to the System retirement plan and other postretirement benefit plans that, under GAAP, are included in other comprehensive income, but excluded from net income. Additional information regarding the classifications of accumulated other comprehensive income is provided in Note 15.

(p) Interest on Federal Reserve Notes

The Board of Governors requires 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. This amount is reported as "Payments to U.S. Treasury as interest on Federal Reserve notes" in the Combined Statements of Income and Comprehensive Income. The amount due to the Treasury is reported as "Accrued interest on Federal Reserve notes" in the Combined Statements of Condition. If overpaid during the year, the amount is reported as "Prepaid interest on Federal Reserve notes" in the Combined Statements of Condition. Payments are made weekly to the Treasury.

In the event of losses or an increase in capital paid-in at a Reserve Bank, payments to the Treasury are suspended and earnings are retained until the surplus is equal to the capital paid-in.

In the event of a decrease in capital paid-in, the excess surplus, after equating capital paid-in and surplus at December 31, is distributed to the Treasury in the following year.

(q) Interest on Depository Institution Deposits

On October 9, 2008, the Reserve Banks began paying interest to depository institutions on qualifying balances held at the Reserve Banks. The interest rates paid on required reserve balances and excess balances are determined by the Board of Governors, based on an FOMC-established target range for the effective federal funds rate.

(r) Income and Costs Related to Treasury Services

The Reserve Banks are required by the Federal Reserve Act to serve as fiscal agent and depositary of the United States Government. By statute, the Department of the Treasury has appropriations to pay for these services. During the years ended December 31, 2009 and 2008, the Reserve Banks were reimbursed for all material services provided to the Department of the Treasury as its fiscal agent.

(s) Assessments by the Board of Governors

The Board of Governors assesses the Reserve Banks to fund its operations based on each Reserve Bank's capital and surplus balances as of December 31 of the prior year. The Board of Governors also assesses each Reserve Bank for the expenses incurred by the Treasury to produce and retire Federal Reserve notes based on each Reserve Bank's share of the number of notes comprising the System's net liability for Federal Reserve notes on December 31 of the prior year.

(t) Taxes

The Reserve Banks are exempt from federal, state, and local taxes, except for taxes on real property. The Reserve Banks' real property taxes were $37 million and $38 million for the years ended December 31, 2009 and 2008, respectively, and are reported as a component of "Occupancy expense."

(u) Restructuring Charges

The Reserve Banks recognize restructuring charges for exit or disposal costs incurred as part of the closure of business activities in a particular location, the relocation of business activities from one location to another, or a fundamental reorganization that affects the nature of operations. Restructuring charges may include costs associated with employee separations, contract terminations, and asset impairments. Expenses are recognized in the period in which the Reserve Banks commit to a formalized restructuring plan or execute the specific actions contemplated in the plan and all criteria for financial statement recognition have been met.

Note 16 describes the Reserve Banks' restructuring initiatives and provides information about the costs and liabilities associated with employee separations and contract terminations. The costs associated with the impairment of certain of the Reserve Banks' assets are discussed in Note 11. Costs and liabilities associated with enhanced pension benefits in connection with the restructuring activities for all of the Reserve Banks are recorded on the books of the FRBNY. Costs and liabilities associated with enhanced postretirement benefits are discussed in Note 14.

In 2009, the Reserve Banks continued their check restructuring initiatives to align check processing infrastructure and operations with declining check processing volumes. Additional announcements in 2009 included restructuring plans associated with discontinuing check print sites.

(v) Recently Issued Accounting Standards

In December 2008, the FASB issued FASB Staff Position (FSP) 132(R)-1, *Employers Disclosures about Postretirement Benefit Plan Assets,* (codified in FASB ASC Topic 715 (ASC 715) *Compensation — Retirement Benefits*). ASC 715 provides rules for the disclosure of information about assets held in a defined benefit plan in the financial statements of the employer sponsoring that plan, and additional disclosures about asset categories and concentrations of risk. It is effective for financial statements with fiscal years ending after December 15, 2009. The disclosures required by ASC 715 have been reflected, as appropriate, in the accompanying footnotes.

In March 2008, FASB issued Statement of Financial Accounting Standards (SFAS) 161, *Disclosures about Derivative Instruments and Hedging Activities—an amendment of FASB Statement No. 133,* (codified in FASB ASC Topic 815 (ASC 815), *Derivatives and Hedging*), which requires expanded qualitative, quantitative, and credit-risk disclosures about derivatives and hedging activities and their effects on a company's financial position, financial performance, and cash flows. These provisions of ASC 815 are effective for the Reserve Banks' combined financial statements for the year beginning on January 1, 2009 and have not had a material effect on the Reserve Banks' combined financial statements. The disclosure requirements have been reflected, as appropriate, in Note 9.

In February 2008, FASB issued FSP SFAS 140-3, *Accounting for Transfers of Financial Assets and Repurchase Financing Transactions,* (codified in FASB ASC Topic 860 (ASC 860), *Transfers and Servicing*). ASC 860 requires that an initial transfer of a financial asset and a repurchase financing that was entered into contemporaneously with, or in contemplation of, the initial transfer be evaluated together as a linked transaction unless certain criteria are met. These provisions of ASC 860 are effective for the Reserve Banks' combined financial statements for the year beginning on January 1, 2009 and have not had a material effect on the Reserve Banks' combined financial statements. The requirements of this standard have been reflected in the accompanying footnotes.

In June 2009, FASB issued SFAS 166, *Accounting for Transfers of Financial Assets—an amendment to FASB Statement No. 140,* (codified in FASB ASC 860). The new guidance modifies existing guidance to eliminate the scope exception for qualifying SPVs and clarifies that the transferor must consider all arrangements of the transfer of financial assets when determining if the transferor has surrendered control. These provisions of ASC 860 are effective for the Reserve Banks' combined financial statements for the year beginning on January 1, 2010, and earlier adoption is prohibited. The adoption of this standard is not expected to have a material effect on the Reserve Banks' combined financial statements.

In April 2009, FASB issued FSP SFAS 115-2 and SFAS 124-2, *Recognition and Presentation of Other-Than-Temporary-Impairments,* (codified in FASB ASC Topic 320 (ASC 320) *Investment-Debt and Equity Securities*), which amends the other-than-temporary impairment guidance for debt securities and the financial statement presentation and disclosure requirements. These provisions of ASC 320, which are effective for the Reserve Banks' combined financial statements ended December 31, 2009, have not had a material effect on the Reserve Banks' combined financial statements.

In April 2009, FASB issued FSP 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly,* (codified in FASB ASC Topic 820 (ASC 820), *Fair Value Measurements and Disclosures*) which provides additional guidance for estimating fair value when the value and level of market activity for an asset or liability have significantly decreased. The standard also provides guidance on identifying circumstances that indicate a transaction is not orderly. The provisions of the FSP, which are effective for the Reserve Banks' combined financial statements for the year ending December 31, 2009, were considered in determining the valuation of assets and liabilities that are measured at fair value. The adoption of this provision did not have a material effect on the Reserve Banks' combined financial statements.

In May 2009, FASB issued SFAS No. 165, *Subsequent Events,* (codified in FASB ASC Topic 855 (ASC 855), *Subsequent Events*), which establishes general standards of accounting for and disclosing events that occur after the balance sheet date but before financial statements are issued or are available to be issued. ASC 855 sets forth (i) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements; (ii) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements; and (iii) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date, including disclosure of the date through which an entity has evaluated subsequent events and whether that represents the date the financial statements were issued or were available to be issued. The Reserve Banks adopted ASC 855 for the period ended December 31, 2009 and the required disclosures are reflected in Note 17.

In June 2009, FASB issued SFAS No. 167, *Amendments to FASB Interpretation No. 46(R),* (codified in FASB ASC 810), which expands the scope of Interpretation 46R, *Consolidation of Variable Interest Entities* and changes the approach for determining whether an entity has a controlling interest in a VIE by making a qualitative assessment of its financial interests. Additional disclosures are required for a variable interest in a VIE. These provisions of ASC 810 are effective for the Reserve Banks' combined financial statements for the year beginning on January 1, 2010, and earlier adoption is prohibited. The adoption of this standard is not expected to have a material effect on the Reserve Banks' combined financial statements.

In June 2009, the FASB issued SFAS No. 168, *The Statement of Financial Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles,* a replacement of SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* (SFAS 168). SFAS 168 establishes the FASB ASC as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with GAAP. The ASC does not change current GAAP, but it introduces a new structure that organizes the authoritative standards by topic. SFAS 168 is effective for financial statements issued for periods ending after September 15, 2009. As a result, both the ASC and the legacy standard are referenced in the Reserve Banks' combined financial statements and footnotes.

In January 2010, the FASB issued *Accounting Standards Update 2010-06,* (codified in FASB ASC Topic 820 (ASC 820), *Fair Value Measurements and Disclosures*) which requires additional disclosures related to fair value measurements. This update is effective for the Reserve Banks' combined financial statements for the year beginning on January 1, 2010 and early adoption is prohibited. The adoption of this update is not expected to have a material effect on the Reserve Banks' combined financial statements.

(5) Loans

The loan amounts outstanding at December 31 were as follows (in millions):

	2009	2008
Primary, secondary, and seasonal credit	$20,700	$ 93,790
TAF	75,918	450,220
Loans to depository institutions	$96,618	$544,010
AMLF	$ -	$ 23,765
PDCF	-	37,404
TALF loans, fair value	48,183	-
AIG	22,738	38,913
Other loans	70,921	100,082
Allowance for loan restructuring (AIG)	(1,488)	-
Other loans, net	$69,433	$100,082

The remaining maturity distributions, net of allowance, of loans outstanding at December 31 were as follows (in millions):

	2009			
	Primary, secondary, and seasonal credit	TAF	TALF loans, fair value	AIG, net
Within 15 days	$16,304	$75,918	$ -	$ -
16 to 90 days	4,396	-	-	-
Over 1 year to 5 years	-	-	48,183	21,250
Total loans	$20,700	$75,918	$48,183	$21,250

	2008				
	Primary, secondary, and seasonal credit	TAF	AMLF	PDCF	AIG
Within 15 days	$85,846	$235,424	$ 9,682	$37,404	$ -
16 to 90 days	7,944	214,796	14,083	-	-
Over 1 year to 5 years	-	-	-	-	38,913
Total loans	$93,790	$450,220	$23,765	$37,404	$38,913

Loans to depository institutions

The Reserve Banks offer primary, secondary, and seasonal credit to eligible borrowers. Each program has its own interest rate. Interest is accrued using the applicable interest rate established at least every 14 days by the Reserve Banks' boards of directors, subject to review and determination by the Board of Governors. Primary and secondary credit are extended on a short-term basis, typically overnight, whereas seasonal credit may be extended for a period of up to nine months.

Primary, secondary, and seasonal credit lending is collateralized to the satisfaction of the Reserve Banks to reduce credit risk. Assets eligible to collateralize these loans include consumer, business, and real estate loans; Treasury securities; GSE debt securities; foreign sovereign debt; municipal, corporate, and state and local government obligations; ABS; corporate bonds; commercial paper; and bank-issued assets, such as certificates of deposit, bank notes, and deposit notes. Collateral is assigned a lending value that is deemed appropriate by the Reserve Banks, which is typically fair value or face value reduced by a margin.

Depository institutions that are eligible to borrow under the Reserve Banks' primary credit program are also eligible to participate in the TAF program. Under the TAF program, the Reserve Banks conduct auctions for a fixed amount of funds, with the interest rate determined by the auction process, subject to a minimum bid rate. TAF loans are extended on a short-term basis, with terms ranging from 28 to 84 days. All advances under the TAF program must be collateralized to the satisfaction of the Reserve Banks. Assets eligible to collateralize TAF loans include the complete list noted above for loans to depository institutions. Similar to the process used for primary, secondary, and seasonal credit, a lending value is assigned to each asset that is accepted as collateral for TAF loans reduced by a margin.

Loans to depository institutions are monitored on a daily basis to ensure that borrowers continue to meet eligibility requirements for these programs. The financial condition of borrowers is monitored by the Reserve Banks and, if a borrower no longer qualifies for these programs, the Reserve Banks will generally request full repayment of the outstanding loan or, for primary and seasonal credit lending, may convert the loan to a secondary credit loan. Collateral levels are reviewed daily against outstanding obligations and borrowers that no longer have sufficient collateral to support outstanding loans are required to provide additional collateral or to make partial or full repayment.

At December 31, 2009 and 2008, the FRBNY did not have any impaired loans to depository institutions and no allowance for loan losses was required.

Other loans

AMLF

The FRBB administered the AMLF and was authorized to extend loans to eligible borrowers on behalf of the other Reserve Banks. All loans extended under the AMLF were recorded as assets by the FRBB and, if the borrowing institution settled to a depository account in another Reserve Bank District, the funds were credited to the institution's depository account by the appropriate Reserve Bank and settled between the Banks through the interdistrict settlement account. The loans extended under the AMLF were nonrecourse, so that the FRBB had recourse only to the collateral pledged by the borrowers. The credit risk related to the AMLF was assumed by the FRBB. No losses were incurred on loans extended during the years ended December 31, 2009 and 2008. Eligible collateral under the program was limited to U.S. dollar-denominated ABCP that was not rated lower than A-1/P-1/F1 and was required to be purchased from an eligible money market mutual fund. The terms of loans under the AMLF were limited to 120 days if the borrower was a bank or 270 days for nonbank borrowers. The interest rate for advances made under the AMLF was equal to the FRBB's primary credit rate offered to depository institutions at the time the advance was made.

At December 31, 2009, the FRBB did not have any AMLF loans outstanding. At December 31, 2008, no AMLF loans were impaired and no allowance for loan losses was required.

PDCF

The PDCF provided secured overnight financing to primary dealers in exchange for a specified range of collateral, including Treasury securities; federal agency and GSE MBS; other MBS; municipal securities; ABS; and money market equities, for which prices were available. Interest on PDCF secured financing was accrued using the primary credit rate offered by the Reserve Banks to depository institutions. The secured financing is reported as a component of "Other loans" in the Combined Statements of Condition. The frequency-based fees are reported as "Other income" in the Combined Statements of Income and Comprehensive Income.

At December 31, 2009, the Reserve Banks did not have any PDCF loans outstanding. At December 31, 2008, no PDCF loans were impaired and no allowance for loan losses was required.

TALF

Credit extensions under TALF are nonrecourse loans secured by eligible collateral. Each TALF loan has a three-year maturity, except for loans secured by SBA Pool Certificates, loans secured by SBA Development Company Participation Certificates, or ABS backed by student loans or commercial mortgage loans, which have a five-year maturity if the borrower so elects.

The FRBNY has elected the fair value option for all TALF loans under ASC 825. Recording all TALF loans at fair value, rather than at the remaining principal amount outstanding, results in consistent accounting treatment among all TALF-related transactions and provides the most appropriate presentation of the TALF program on the financial statements by matching the change in fair value of TALF loans, the related put agreement with the consolidated TALF LLC, and the valuation of the other beneficial interests in TALF LLC. Additional information regarding the TALF LLC assets and liabilities is presented in Note 9.

In certain cases where there is limited activity around inputs to the valuation, loans are classified within Level 3 of the valuation hierarchy. Because external price information was not available, market-based models were used to determine the fair value of the TALF loans. The fair value of the TALF loans was determined by valuing the future cash flows from loan interest income and the estimated fair value losses associated with collateral that may be put to the FRBNY. The valuation model takes into account a range of outcomes on TALF loan repayments, market prices of the collateral, risk premiums estimated using market prices, and the volatilities of market risk factors. Other methodologies employed or assumptions made in determining fair value could result in an amount that differs significantly from the amount reported.

The following table presents the TALF loans at fair value as of December 31, 2009, by ASC 820 hierarchy (in millions):

	Fair value hierarchy			Total
	Level 1	Level 2	Level 3	fair value
TALF loans	$ -	$ -	$48,183	$48,183

The table below presents a reconciliation of the TALF loans, which are measured at fair value using significant unobservable inputs (Level 3) during the period February 4, 2009 to December 31, 2009 (in millions):

	Fair Value at February 4, 2009	Loans originated[1]	Unrealized gains	Transfers out[2]	Fair Value at December 31, 2009
TALF loans	$ -	$61,626	$557	$(14,000)	$48,183

1. Loans originated includes $52 million in accrued interest receivable.
2. Net transfers out represent principal prepayments.

The fair value of TALF loans reported in the Combined Statements of Condition at December 31, 2009 includes $557 million in unrealized gains. FRBNY attributes substantially all changes in fair value of nonrecourse loans to changes in instrument specific credit spreads.

The table below presents principal and accrued interest by concentration for the TALF loans as of December 31, 2009 (in millions):

	Concentration of Unpaid Principal Balance and Accrued Interest			
	Years to Maturity			Percent
Collateral Type and Credit Rating	1–3	4–5	Total	of Total
Auto (AAA)	$ 5,851	$ -	$ 5,851	12%
CMBS (AA)	-	25	25	0%
CMBS (AAA)	3,572	4,941	8,513	18%
Credit Card (AAA)	20,297	-	20,297	43%
Floorplan (AAA)	2,427	-	2,427	5%
SBAs (AAA)	915	357	1,272	3%
Student Loan (AAA)	2,236	4,168	6,404	13%
Other (AAA)[1]	2,837	-	2,837	6%
Total	$38,135	$9,491	$47,626	100%

1. Includes equipment, servicing advances, and premium finance ABS.

The aggregate remaining principal amount outstanding on TALF loans as of December 31, 2009 was $47,574 million.

At December 31, 2009, no TALF loans were over 90 days past due or in nonaccrual status. Because the TALF loans are measured at fair value, an allowance for loan losses was not required.

AIG

The $21,250 million extended to AIG under the revolving line of credit is net of unamortized deferred commitment fees and allowance for restructuring and includes unpaid commitments fees and accrued interest. The AIG loan is reported as a component of "Other loans" in the Combined Statements of Condition.

The table below represents the components of the loan amounts outstanding to AIG at December 31.

AIG Loan Components	2009	2008
Line of credit drawn	$17,900	$36,800
Accrued interest	3,835	1,931
Unpaid commitment fees	1,700	1,700
Unamortized deferred commitment fees	(697)	(1,518)
Allowance for loan restructuring, net	(1,488)	-
Loan to AIG, net	$21,250	$38,913

The fair value of the AIG line of credit provided by the FRBNY, based on estimated draws and repayments, was not materially different from the net amount reported as a component of "Other loans" in the Combined Statements of Condition as of December, 31, 2009.

The activity related to the allowance for loan restructuring for the year ended December 31, 2009 was as follows (in millions):

	Allowance for Loan Restructuring January 1, 2009	Provision for Loan Restructuring	Recoveries	Allowance for Loan Restructuring December 31, 2009
AIG loan	$ -	$(2,621)	$1,133	$(1,488)

The allowance for loan restructuring represents the economic effect of the reduction of the interest rate on loans the FRBNY made to AIG prior to April 17, 2009, as part of the loan restructuring that occurred on that date. The restructuring charges will be recovered over the remaining term of the related loan. The allowance outstanding, net of amortized recoveries, is deducted from "Other loans" in the Combined Statements of Condition and recoveries are reported as a component of "Interest income: Other loans" on the Combined Statements of Income and Comprehensive Income. The average balance of the credit extensions to AIG under the revolving line of credit, net of the allowance for restructuring, during the year ended December 31, 2009 was $39,099 million. Interest income recognized on credit extensions to AIG during the year ended December 31, 2009 was $3,996 million. No interest income was foregone after the recorded restructuring.

(6) Treasury Securities; Government-Sponsored Enterprise Debt Securities; Federal Agency and Government-Sponsored Enterprise Mortgage-Backed Securities; Securities Purchased Under Agreements To Resell; Securities Sold Under Agreements to Repurchase; and Securities Lending

The FRBNY, on behalf of the Reserve Banks, holds securities bought outright in the SOMA.

The total of the Treasury securities, GSE debt securities, and federal agency and GSE MBS, net, excluding accrued interest, held in the SOMA at December 31 was as follows (in millions):

	2009					
	Treasury securities					
	Bills	Notes	Bonds	Total Treasury securities	GSE debt securities	Federal agency and GSE MBS
Par	$18,423	$568,323	$189,843	$776,588	$159,879	$908,371
Unamortized premiums	-	6,545	24,460	31,005	7,509	12,110
Unaccreted discounts	-	(991)	(630)	(1,621)	(26)	(1,554)
Total amortized cost	$18,423	$573,877	$213,673	$805,972	$167,362	$918,927
Fair Value	$18,422	$583,040	$230,717	$832,180	$167,444	$914,290

	2008				
	Treasury securities				
	Bills	Notes	Bonds	Total Treasury securities	GSE debt securities
Par	$18,423	$334,779	$122,719	$475,921	$19,708
Unamortized premiums	-	274	6,711	6,985	1,064
Unaccreted discounts	-	(837)	(620)	(1,457)	(32)
Total amortized cost	$18,423	$334,216	$128,810	$481,449	$20,740
Fair Value	$18,423	$357,709	$169,433	$545,564	$20,863

The fair value amounts in the above tables are presented solely for informational purposes. Although the fair value of security holdings can be substantially greater than or less than the recorded value at any point in time, these unrealized gains or losses have no effect on the ability of the Reserve Banks, as the central bank, to meet their financial obligations and responsibilities. Fair value was determined by reference to quoted market values for identical securities, except for federal agency and GSE MBS for which fair values were determined using a model-based approach based on observable inputs for similar securities.

The fair value of the fixed-rate Treasury securities, GSE debt securities, and federal agency and GSE MBS in the SOMA's holdings is subject to market risk, arising from movements in market variables, such as interest rates and securities prices. The fair value of federal agency and GSE MBS is also affected by the rate of prepayments of mortgage loans underlying the securities.

The following table provides additional information on the amortized cost and fair values of the federal agency and GSE MBS portfolio at December 31, 2009 (in millions):

Distribution of MBS holdings by coupon rate	Amortized cost	Fair value
4.0%	$170,119	$165,740
4.5%	434,352	431,646
5.0%	195,418	196,411
5.5%	103,379	104,583
6.0%	12,710	12,901
Other[1]	2,949	3,009
Total	$918,927	$914,290

1. Represents less than one percent of the total portfolio

Financial information related to securities purchased under agreements to resell and securities sold under agreements to repurchase for the years ended December 31, 2009 and 2008, was as follows (in millions):

	Securities purchased under agreements to resell		Securities sold under agreements to repurchase	
	2009	2008	2009	2008
Contract amount outstanding, end of year	$ -	$ 80,000	$77,732	$88,352
Average daily amount outstanding, during the year	3,616	86,227	67,837	55,169
Maximum month-end balance outstanding, during the year	-	119,000	77,732	98,559
Securities pledged, end of year	-	-	77,860	78,896

The Reserve Banks revised the disclosure of securities purchased under agreements to resell and securities sold under agreements to repurchase from a weighted average calculation, disclosed in 2008, to the simple daily average calculation, disclosed above. The previously reported Reserve Bank total 2008 weighted average amount outstanding for securities purchased under agreements to resell was $97,037 million. The previously reported Reserve Bank total 2008 weighted average amount outstanding for securities sold under agreements to repurchase was $65,461 million.

The contract amounts for securities purchased under agreements to resell and securities sold under agreements to repurchase approximate fair value.

The remaining maturity distribution of Treasury securities, GSE debt securities, federal agency and GSE MBS bought outright, securities purchased under agreements to resell, and securities sold under agreements to repurchase at December 31, 2009 was as follows (in millions):

	Treasury securities (Par value)	GSE debt securities (Par value)	Federal agency and GSE MBS (Par value)	Securities purchased under agreements to resell (Contract amount)	Securities sold under agreements to repurchase (Contract amount)
Within 15 days	$ 11,617	$ 68	$ -	$-	$77,732
16 days to 90 days	28,853	3,046	-	-	-
91 days to 1 year	50,771	21,528	-	-	-
Over 1 year to 5 years	326,874	99,402	12	-	-
Over 5 years to 10 years	213,720	33,788	20	-	-
Over 10 years	144,753	2,047	908,339	-	-
Total	$776,588	$159,879	$908,371	$-	$77,732

Federal agency and GSE MBS are reported at stated maturity in the table above. The estimated weighted average life of these securities at December 31, 2009, which differs from the stated maturity primarily because it factors in prepayment assumptions, is approximately 6.4 years.

At December 31, 2009 and 2008, Treasury securities and GSE debt securities with par values of $21,610 million and $180,765 million, respectively, were loaned from the SOMA.

At December 31, 2009, the total of other investments was $5 million. Other investments consist of cash and short-term investments related to the federal agency and GSE MBS portfolio.

At December 31, 2009, the total of other liabilities was $601 million. These other liabilities, which are related to purchases of federal agency and GSE MBS, arise from the failure of a seller to deliver securities to the FRBNY on the settlement date. Although the FRBNY has ownership of and records its investments in the MBS as of the contractual settlement date, it is not obligated to make payment until the securities are delivered, and the amount reported as other liabilities represents the Reserve Banks' obligation to pay for the securities when delivered.

The FRBNY enters into commitments to buy federal agency and GSE MBS and records the related MBS on a settlement-date basis. As of December 31, 2009, the total purchase price of the federal agency and GSE MBS under outstanding commitments was $160,099 million, of which $32,838 million was related to dollar rolls. These commitments, which had contractual settlement dates extending through March 2010, are primarily for the purchase of TBA MBS for which the number and identity of the pools that will be delivered to fulfill the commitment are unknown at the time of the trade. These commitments are subject to market and counterparty risks that result from their future settlement. As of December 31, 2009, the fair value of federal agency and GSE MBS under outstanding commitments was $158,868 million. During the year ended December 31, 2009, the Reserve Banks recorded net gains from dollar roll related sales of $879 million. These net gains are reported as "Non-Interest Income (Loss): Federal agency and government-sponsored enterprise mortgage-backed securities gains, net" in the Combined Statements of Income and Comprehensive Income.

(7) Investments Denominated In Foreign Currencies

The FRBNY, on behalf of the Reserve Banks, holds foreign currency deposits with foreign central banks and with the Bank for International Settlements and invests in foreign government debt instruments. These investments are guaranteed as to principal and interest by the issuing foreign governments. In addition, the FRBNY enters into transactions to purchase foreign-currency-denominated government-debt securities under agreements to resell for which the accepted collateral is the debt instruments issued by the governments of Belgium, France, Germany, Italy, the Netherlands, and Spain.

The Reserve Banks' investments denominated in foreign currencies, including accrued interest, valued at amortized cost and foreign currency market exchange rates at December 31, was as follows (in millions):

	2009	2008
Euro:		
Foreign currency deposits	$ 7,396	$ 5,563
Securities purchased under agreements to resell	2,591	4,076
Government debt instruments	4,936	4,609
Japanese yen:		
Foreign currency deposits	3,403	3,483
Government debt instruments	6,946	7,073
Total	$25,272	$24,804

At December 31, 2009 and 2008, the fair value of investments denominated in foreign currencies, including accrued interest, was $25,480 million and $25,021 million, respectively. The fair value of government debt instruments was determined by reference to quoted prices for identical securities. The cost basis of foreign currency deposits and securities purchased under agreements to resell, adjusted for accrued interest, approximates fair value. Similar to the Treasury securities, GSE debt securities, and federal agency and GSE MBS discussed in Note 6, unrealized gains or losses have no effect on the ability of the Reserve Banks, as the central bank, to meet its financial obligations and responsibilities. The fair value is presented solely for informational purposes.

The remaining maturity distribution of investments denominated in foreign currencies at December 31, 2009 was as follows (in millions):

	Euro	Japanese yen	Total
Within 15 days	$ 6,067	$ 3,623	$ 9,690
16 days to 90 days	2,505	463	2,968
91 days to 1 year	2,408	2,368	4,776
Over 1 year to 5 years	3,943	3,895	7,838
Total	$14,923	$10,349	$25,272

At December 31, 2009 and 2008, the authorized warehousing facility was $5 billion, with no balance outstanding.

In connection with its foreign currency activities, the FRBNY may enter into transactions that contain varying degrees of off-balance-sheet market risk that result from their future settlement and counterparty credit risk. The FRBNY controls these risks by obtaining credit approvals, establishing transaction limits, receiving collateral in some cases, and performing daily monitoring procedures.

(8) Central Bank Liquidity Swaps

U.S. Dollar Liquidity Swaps

At December 31, 2009 and 2008, the total Reserve Bank amount of foreign currency held under U.S. dollar liquidity swaps was $10,272 million and $553,728 million, respectively.

The remaining maturity distribution of U.S. dollar liquidity swaps at December 31 was as follows (in millions):

	2009			2008		
	Within 15 days	16 days to 90 days	Total	Within 15 days	16 days to 90 days	Total
Australian dollar	$ -	$-	$ -	$ 10,000	$ 12,830	$ 22,830
Danish krone	-	-	-	-	15,000	15,000
Euro	6,506	-	6,506	150,969	140,383	291,352
Japanese yen	545	-	545	47,893	74,823	122,716
Korean won	-	-	-	-	10,350	10,350
Mexican peso	3,221	-	3,221	-	-	-
Norwegian krone	-	-	-	2,200	6,025	8,225
Swedish krona	-	-	-	10,000	15,000	25,000
Swiss franc	-	-	-	19,221	5,954	25,175
U.K. pound	-	-	-	120	32,960	33,080
Total	$10,272	$-	$10,272	$240,403	$313,325	$553,728

Foreign Currency Liquidity Swaps

There were no transactions related to the foreign currency liquidity swaps during the years ended December 31, 2008 and 2009.

(9) Investments Held By Consolidated Variable Interest Entities

The combined financial statements include the accounts and results of operations of several VIEs, specifically ML, ML II, ML III, CPFF and TALF LLC. The consolidation of the VIEs was assessed in accordance with ASC 810, which requires a variable interest entity to be consolidated by its controlling financial interest holder.

(a) Summary Information for Consolidated Variable Interest Entities

The total assets of consolidated VIEs, including cash, cash equivalents, and accrued interest, at December 31 were as follows (in millions):

	2009	2008
CPFF	$14,233	$334,910
ML	28,140	30,635
ML II	15,912	19,195
ML III	22,797	27,256
TALF LLC	298	-
Total	$81,380	$411,996

The FRBNY's maximum exposure to loss at December 31, 2009 and 2008 was $73,879 million and $405,377 million, respectively. These estimates incorporate potential losses associated with assets recorded on the FRBNY's balance sheet, net of the fair value of subordinated interests (beneficial interest in consolidated VIEs).

The classification of significant assets and liabilities of the consolidated VIEs at December 31 was as follows (in millions):

	2009	2008
Assets:		
Commercial paper	$ 9,421	$333,631
CDOs	22,650	26,957
Non-agency RMBS	17,552	20,675
Federal agency and GSE MBS	18,149	15,654
Commercial mortgage loans	4,025	5,553
Residential mortgage loans	583	937
Swap contracts	1,127	2,454
Other investments	5,467	2,340
Subtotal	$78,974	$408,201
Cash, cash equivalents, and accrued interest receivable	2,406	3,795
Total investments held by consolidated variable interest entities	$81,380	$411,996
Liabilities:		
Beneficial interest in consolidated variable interest entities	$ 5,095	$ 2,824
Other liabilities[1]	$ 1,316	$ 5,813

1. The amounts reported as "Consolidated variable interest entities: Other liabilities" in the Combined Statements of Condition at December 31, 2009 included $980 million related to cash collateral received on swap contracts and at December 31, 2008 included $2,572 million related to cash collateral received on swap contracts and $2,369 million payable for investments purchased by VIEs. The amount also included accrued interest, unearned registration fees, and accrued other expenses.

Total realized gains (losses) and unrealized gains (losses) for the 12 months ended December 31, 2009, were as follows (in millions):

	Total portfolio holdings realized gains (losses)	Fair value changes unrealized gains (losses)	Total portfolio holdings realized/ unrealized gains (losses)
CDOs	$ (3)	$(1,211)	$(1,214)
Non-agency RMBS	217	(991)	(774)
Federal agency and GSE MBS	322	521	843
Commercial mortgage loans	(47)	(1,177)	(1,224)
Residential mortgage loans	(48)	(219)	(267)
Swap contracts	(119)	212	93
Other investments	12	712	724
Other assets	(182)	64	(118)
Total	$ 152	$(2,089)	$(1,937)

Total realized gains (losses) and unrealized gains (losses) for the 12 months ended December 31, 2008, were as follows (in millions):

	Total portfolio holdings realized gains (losses)	Fair value changes unrealized gains (losses)	Total portfolio holdings realized/ unrealized gains (losses)
CDOs	$ -	$(3,281)	$(3,281)
Non-agency RMBS	(4)	(3,001)	(3,005)
Federal agency and GSE MBS	(166)	50	(116)
Commercial mortgage loans	42	(2,130)	(2,088)
Residential mortgage loans	(3)	(563)	(566)
Swap contracts	(70)	155	85
Other investments	237	(892)	(655)
Total	$ 36	$(9,662)	$(9,626)

The net income (loss) attributable to ML, ML II, ML III and CPFF for the 12 months ended December 31, 2009 and for TALF LLC for the period from inception to December 31, 2009 was as follows (in millions):

	ML	ML II	ML III	CPFF	TALF LLC	Total
Interest income:						
Portfolio interest income	$1,476	$1,088	$ 3,032	$4,224	$ -	$ 9,820
Less: Interest expense	61	33	171	-	2	267
Net interest income	1,415	1,055	2,861	4,224	(2)	9,553
Non-interest income:						
Portfolio holdings gains (losses)	(102)	(604)	(1,239)	8	-	(1,937)
Less: Unrealized gains (losses) on beneficial interest in consolidated VIEs	61	34	(1,299)	-	(699)[1]	(1,903)
Net non-interest income (loss)	(41)	(570)	(2,538)	8	(699)	(3,840)
Total net interest income and non-interest income	1,374	485	323	4,232	(701)	5,713
Less: Professional fees	55	12	27	30	1	125
Net income (loss) attributable to consolidated VIEs	$1,319	$ 473	$ 296	$4,202	$(702)[2]	$ 5,588

1. The TALF LLC reported net operating income of $776 million for the period from inception to December 31, 2009 includes gains of $557 million on the put option between FRBNY and TALF LLC that are eliminated in consolidation. The unrealized loss on beneficial interest in consolidated VIEs represent Treasury's 90 percent financial interest in the TALF LLC's net operating income before consolidation.

2. The FRBNY earned $1,025 million on TALF loans during the year ended December 31, 2009 which offsets the net loss attributable to TALF LLC. Earnings on TALF loans that are reported on the Combined Statements of Income include interest income of $414 million reported as a component of "Interest income: Other loans, net," gains on the valuation of loans of $557 reported as "Non-Interest Income (Loss): Other loans unrealized gains," and administrative fees of $54 million reported as a component of "Non-Interest Income (Loss): Other income."

The net income (loss) attributable to consolidated VIEs from inception through December 31, 2008 was as follows (in millions):

	ML	ML II	ML III	CPFF	Total
Interest income:					
Portfolio interest income	$ 1,561	$ 302	$ 517	$1,707	$ 4,087
Less: Interest expense	332	103	28	-	463
Net interest income	1,229	199	489	1,707	3,624
Non-interest income:					
Portfolio holdings (losses) gains	(5,497)	(1,499)	(2,633)	3	(9,626)
Less: Unrealized gains on beneficial interest in consolidated VIEs	1,188	1,003	2,198	-	4,389
Net non-interest (loss) income	(4,309)	(496)	(435)	3	(5,237)
Total net interest income and non-interest income	(3,080)	(297)	54	1,710	(1,613)
Less: Professional fees	54	5	9	12	80
Net income (loss) attributable to consolidated VIEs	$(3,134)	$ (302)	$ 45	$1,698	$(1,693)

The subordinated financial interest of the consolidated VIEs from inception through December 31, 2009 is as follows (in millions):

	ML subordinated loan	ML II deferred purchase price	ML III equity contribution	TALF Treasury contribution	Total
Beginning principal in 2008	$ 1,150	$ 1,000	$ 5,000	$ -	$ 7,150
Interest accrued and capitalized	38	3	22	-	63
Ending principal balance	1,188	1,003	5,022	-	7,213
Unrealized (gain)	(1,188)	(1,003)	(2,198)	-	(4,389)
Balance at December 31, 2008	$ -	$ -	$ 2,824	$ -	$ 2,824
Treasury loan	$ -	$ -	$ -	$100	$ 100
Interest accrued and capitalized	61	34	171	2	268
Ending principal balance	61	34	2,995	102	3,192
Unrealized (gain)/loss	(61)	(34)	1,299	699	1,903
Balance at December 31, 2009	$ -	$ -	$ 4,294	$801	$ 5,095

(b) Commercial Paper Funding Facility LLC

The CPFF Program charged a lending rate for unsecured commercial paper equal to a three-month OIS rate plus 100 basis points per annum, with an additional surcharge of 100 basis points per annum for an unsecured credit enhancement fee. The interest rate for ABCP is the three-month OIS rate plus 300 basis points.

Unsecured commercial paper issuers covered by the FDIC Temporary Liquidity Guarantee Program are viewed as having a satisfactory guarantee and the credit enhancement fee for those participants is waived. The credit enhancement fee is amortized on a straight-line basis over the term of the commercial paper, which is not materially different from the interest method. The registration fees are amortized on a straight-line basis over the life of the program, which is not materially different from the interest method.

The FRBNY conducts a periodic review of the CPFF's commercial paper to determine if impairment is other than temporary such that a loss should be recognized. At December 31, 2009 there were no commercial paper securities for which management considered impairments to be other than temporary.

The remaining maturity distribution of the commercial paper and trading securities held by the CPFF at December 31, 2009 was as follows (in millions):

	Commerical paper			
	Asset backed	Non-asset backed	Trading securities	Total
Within 15 days	$ -	$ -	$ 1	$ 1
16 days to 60 days	7,422	1,999	30	9,451
61 days to 92 days	-	-	2,364	2,364
93 days to 124 days	-	-	2,392	2,392
Total	$7,422	$1,999	$4,787	$14,208

Top-tier commercial paper has received the highest ratings (A-1, P-1, F1) from all rating agencies that provide a rating for the paper. Split-rated commercial paper has received a top tier rating from two rating agencies and second tier rating (A-2, P-2, F2) from a third rating agency. All of the commercial paper held by the CPFF at December 31, 2009 was top-tier. The credit ratings profile of the commercial paper held by the CPFF by asset type, issuer type, and industry sector, at December 31, 2009 was as follows (in millions):

	Commerical paper
Asset backed	
Multi-seller	$3,583
Securities arbitrage	2,741
Structured investment vehicle	1,088
Investment company	10
	7,422
Non-asset backed	
Insurance	1,999
	1,999
Total	$9,421

The largest issuer, an asset-backed commercial paper conduit of a diversified financial company, represents 29 percent of the total commercial paper portfolio holdings at December 31, 2009. This entity and affiliates of this entity, together, represent 62 percent of the total commercial paper portfolio held at December 31, 2009.

(c) Maiden Lane LLC

ML's investment portfolio consists primarily of federal agency and GSE MBS, non-agency RMBS, commercial and residential mortgage loans, and derivatives. A description of the significant holdings at December 31, 2009 and the associated credit risk for each holding follows.

i. Debt Securities

ML has investments in federal agency and GSE MBS, which represent fractional ownership interests in RMBS issued by federal agencies and GSEs. The yield characteristics of these securities may differ from traditional debt securities. One such major difference is that all or a principal part of the obligations may be prepaid at any time because the underlying mortgages may be prepaid at any time. A portion of ML's investments include interest only ("IO") or principal only ("PO") security classes. The IO class receives the interest cash flows from the underlying mortgages, while the PO class receives the principal cash flows. The yield to maturity on these securities is sensitive to the rate of principal repayments (including prepayments) on the related underlying mortgage assets. The principal prepayments may have a material effect on yield to maturity. If the underlying mortgage assets experience greater-than-anticipated prepayments of principal, ML may not fully recoup its initial investment in IO classes.

The yield to maturity on the PO classes may be impacted by delinquencies or defaults on the underlying mortgage assets. The rate of delinquencies and defaults on residential mortgage loans and the aggregate amount of the resulting losses can be affected by a number of factors, including general economic conditions, particularly those in the area where the related mortgaged property is located, the level of the borrower's equity in the mortgaged property and the individual financial circumstances of the borrower. Changes in economic conditions, including delinquencies and defaults on the underlying mortgages, can affect the value, income, and liquidity of ML's positions.

ML's non-agency RMBS investments expose ML to varying levels of credit, interest rate, general market, and concentration risk. Credit-related risk on non-agency RMBS arises from losses due to delinquencies and defaults by borrowers on the underlying mortgage loans and breaches by originators and servicers of their obligations under the underlying documentation pursuant to which the non-agency RMBS are issued. The rate of delinquencies and defaults on residential mortgage loans and the aggregate amount of the resulting losses can be affected by a number of factors, including general economic conditions, particularly those in the area where the related mortgaged property is located; the level of the borrower's equity in the mortgaged property; and the individual financial circumstances of the borrower.

The rate of interest payable on certain non-agency RMBS may be set or effectively capped at the weighted average net coupon of the underlying mortgage loans themselves, often referred to as an "available funds cap." As a result of this available funds cap, the return to ML on such non-agency RMBS is dependent on the relative timing and rate of delinquencies and prepayments of mortgage loans bearing a higher interest rate.

As of December 31, 2009, approximately 51 percent of the properties collateralizing the non-agency RMBS held by ML were located in California and Florida, based on the geographic location data available for the underlying loans by aggregate unpaid principal balance.

Other investments are primarily comprised of CMBS and CDOs.

At December 31, 2009, the ratings breakdown of the $20,965 million of debt securities, which are recorded at fair value in the ML portfolio, as a percentage of aggregate fair value of all securities in the portfolio was as follows:

	Ratings[1]						
	AAA	AA+ to AA-	A+ to A-	BBB+ to BBB-	BB+ and Lower	Govern-ment / Agency	Total
Security Type:[2]							
Federal agency and GSE MBS	0.0%	0.0%	0.0%	0.0%	0.0%	86.6%	86.6%
Non-agency RMBS	0.5%	0.5%	0.8%	0.3%	7.0%	0.0%	9.1%
Other[3]	1.2%	0.6%	0.5%	0.7%	1.2%	0.1%	4.3%
Total	1.7%	1.1%	1.3%	1.0%	8.2%	86.7%	100.0%

1. Lowest of all ratings is used for the purposes of this table for securities rated by two or more nationally recognized statistical rating organizations.

2. This table does not include ML's commercial and residential mortgage loans, swaps, and other derivative contracts.

3. Includes all asset sectors that, individually, represent less than five percent of aggregate fair value of debt securities.

ii. Commercial and Residential Mortgage Loans

Commercial and residential mortgage loans are subject to a high degree of credit risk because of exposure to loss from loan defaults. Default rates are subject to a wide variety of factors, including, but not limited to, property performance, property management, supply and demand, construction trends, consumer behavior, regional economic conditions, interest rates, and others.

The performance profile for the commercial and residential mortgage loans at December 31, 2009 was as follows (in millions):

	Remaining principal amount outstanding	Fair value	Fair value as a percentage of remaining principal
Performing loans:			
Commercial	$7,037	$3,879	55.1%
Residential	747	378	50.6%
Subtotal	7,784	4,257	54.7%
Non-performing loans (past due more than 90 days)[1]			
Commercial	1,081	146	13.5%
Residential	739	205	27.7%
Subtotal	1,820	351	19.3%
Total			
Commercial	8,118	4,025	49.6%
Residential	1,486	583	39.2%
Total loans	$9,604	$4,608	48.0%

1. In 2009 ML changed its classification of non-performing/nonaccrual loans to include loans with payments past due greater than 90 days or when ML has doubts about the future performance of the loan assets. The prior year classification included all loans greater than 60 days past due. This change in presentation was made to conform to industry standards and did not have a material effect on ML's consolidated financial statements.

The following table summarizes the state in which residential mortgage loans are collateralized and the property types of the commercial mortgage loans held in the ML portfolio at December 31, 2009:

	Concentration of unpaid principal balances	
	Residential	Commercial[2]
By State:		
California	36.4%	
Florida	9.1%	
Other[1]	54.5%	
	100.0%	
By Property:		
Hospitality		82.8%
Office		9.1%
Other[1]		8.1%
		100.0%

1. No other individual state or property type comprises more than five percent of the total.
2. One borrower represents approximately 50 percent of total unpaid principal balance of the commercial mortgage loan portfolio.

iii. Derivative Instruments

Derivative contracts are instruments, such as futures or swap contracts, which derive their value from underlying assets, indices, reference rates, or a combination of these factors. The ML portfolio includes various derivative financial instruments, primarily consisting of a total return swap agreement ("TRS") with JPMC. ML and JPMC entered into the TRS with reference obligations representing single-named credit default swaps ("CDS") primarily on ABS and interest rate swaps ("IRS") with various market participants, including JPMC. ML, through its Investment Manager, currently manages the CDS contracts within the TRS as a runoff portfolio and may unwind, amend, or novate reference obligations on an ongoing basis.

On an ongoing basis, per the terms of the TRS, ML pledges collateral for credit or liquidity related shortfalls based on 20 percent of the notional amount of sold CDS protection and 10 percent of the present value of future premiums on purchased CDS protection. Separately, ML and JPMC engage in bilateral posting of collateral to cover the net mark-to-market ("MTM") variations in the swap portfolio. ML only nets the collateral received from JPMC from the bilateral MTM posting for the reference obligations where JPMC is the counterparty. The values of ML's cash equivalents and investments, purchased by the re-hypothecation of cash collateral associated with the TRS, were $0.8 billion and $0.5 billion, respectively, as of December 31, 2009 and $2.1 billion and $0.5 billion, respectively, as of December 31, 2008. In addition, ML has pledged $1.5 billion and $3.0 billion of federal agency and GSE MBS to JPMC as of December 31, 2009 and 2008, respectively.

ML enters into additional derivative contracts consisting of futures and interest rate swaps to economically hedge its exposure to interest rates. All derivatives are recorded at fair value in accordance with ASC 815. None of the derivatives held in ML are designated as hedging instruments for accounting purposes.

The following risks are associated with the derivative instruments within ML as part of the TRS agreement with JPMC as well as any derivatives outside of the TRS:

Market Risk

IRS obligate two parties to exchange one or more payments typically calculated with reference to fixed or periodically reset rates of interest applied to a specified notional principal amount. Notional principal is the amount to which interest rates are applied to determine the payment streams under IRS. Such notional principal amounts often are used to express the volume of these transactions but are not actually exchanged between the counterparties.

Futures contracts are agreements to buy and sell financial instruments for a set price on a future date. Initial margin deposits are made upon entering into futures contracts in the form of cash or securities. During the period that a futures contract is open, changes in the value of the contract are recorded as unrealized gains or losses by revaluing the contracts on a daily basis to reflect the market value of the contract at the end of each day's trading. Variation margin payments are paid or received, depending upon whether unrealized gains or losses result. When the contract is closed, ML will record a realized gain or loss equal to the difference between the proceeds from (or cost of) the closing transaction and ML's cost basis in the contract. The use of futures transactions involves the risk of imperfect correlation in movements in the price of futures contracts, interest rates and the underlying hedged assets. ML is also at risk of not being able to enter into a closing transaction for the futures contract because of an illiquid secondary market. ML had pledged collateral related to future contracts of $40 million and $69 million as of December 31, 2009 and 2008, respectively.

CDS are agreements that provide protection for the buyer against the loss of principal on a bond or loan in case of a default by the issuer. The nature of a credit event is established by the protection buyer and protection seller at the inception of a transaction, and such events include bankruptcy, insolvency or failure to meet payment obligations when due. The buyer of the CDS pays a premium in return for payment protection upon the occurrence, if any, of a credit event. Upon the occurrence of a triggering credit event, the maximum potential amount of future payments the seller could be required to make under a CDS is equal to the notional amount of the contract. Such future payments could be reduced or offset by amounts recovered under recourse or by collateral provisions outlined in the contract, including seizure and liquidation of collateral pledged by the buyer. ML's derivatives portfolio consists of purchased credit protection with underlying referenced names not correlated to offset its exposure to sold credit protection.

Credit Risk

Credit risk is the risk of financial loss resulting from failure by a counterparty to meet its contractual obligations to ML. This can be caused by factors directly related to the counterparty, such as business or management. Taking collateral is the most common way to mitigate credit risk. ML takes financial collateral in the form of cash and marketable securities as part of the TRS agreement with JPMC as well as the over-the-counter derivatives activities outside of the TRS.

The following table summarizes the notional amounts of derivative instruments by contract type outstanding as of December 31, 2009 and 2008 (in millions):

	Notional Amounts[1,2]	
	2009	2008
Interest rate contracts:		
IRS	$ 3,185	$11,188
Futures and options on futures[3]	70	45
Credit derivatives:		
CDS	7,323	11,791
Total	$10,578	$23,024

1. Represents the sum of gross long and gross short notional derivative contracts.
2. There were 1,764 and 3,606 CDS and IRS contracts outstanding as of December 31, 2009 and 2008, respectively.
3. Futures and options on futures related to contract obligations and not gross notional amounts.

The following table summarizes the fair value of derivative instruments by contract type on a gross basis as of December 31, 2009 (in millions):

	Derivatives used in trading activities	
	Gross derivative assets	Gross derivative liabilities
Interest rate contracts:		
Swaps	$ 5	$ 195
Futures	20	-
Credit derivatives:		
CDS	3,271	1,816
Counterparty netting	(1,868)	(1,868)
Cash collateral	(281)	-
Total	$ 1,147	$ 143

The table below summarizes certain information regarding protection sold through CDS as of December 31, 2009 (in millions):

	Maximum Potential Payout / Notional					Fair Value
	Years to Maturity					
Credit Ratings of the Reference Obligation	Up to 1 year	1–3	3–5	Over 5	Total	Liability
Investment grade (AAA to BBB-)	$40	$140	$ 5	$ 165	$ 350	$ 154
Non-investment grade	5	20	120	1,954	2,099	1,640
Total credit default swaps sold	$45	$160	$125	$2,119	$2,449	$1,794

(d) Maiden Lane II LLC

ML II's investments in non-agency RMBS expose ML II to varying levels of credit, interest rate, general market, and concentration risk. Credit-related risk on non-agency RMBS arises from losses due to delinquencies and defaults by borrowers on the underlying mortgage loans and breaches by originators and servicers of their obligations under the underlying documentation pursuant to which the non-agency RMBS are issued. The rate of delinquencies and defaults on residential mortgage loans and the aggregate amount of the resulting losses can be affected by a number of factors, including general economic conditions, particularly those in the area where the related mortgaged property is located; the level of the borrower's equity in the mortgaged property; and the individual financial circumstances of the borrower.

The rate of interest payable on certain non-agency RMBS may be set or effectively capped at the weighted average net coupon of the underlying mortgage loans, often referred to as an available funds cap. As a result of this available funds cap, the return to the holder of such non-agency RMBS is dependent on the relative timing and rate of delinquencies and prepayments of mortgage loans bearing a higher rate of interest.

At December 31, 2009, the type/sector and rating composition of ML II's $15,643 million non-agency RMBS portfolio, recorded at fair value, as a percentage of aggregate fair value, was as follows:

	Rating[1,3]					
	AAA	AA+ to AA-	A+ to A-	BBB+ to BBB-	BB+ and lower	Total
Asset Type:						
Alt-A ARM	0.9%	3.1%	2.2%	1.9%	23.3%	31.3%
Subprime	7.7%	2.8%	3.0%	1.9%	39.4%	54.8%
Option ARM	0.0%	0.0%	0.0%	0.1%	6.0%	6.1%
Other[2]	0.1%	0.6%	0.0%	0.0%	7.2%	7.8%
Total	8.7%	6.4%	5.2%	3.8%	75.9%	100.0%

1. Lowest of all ratings is used for the purposes of this table if rated by two or more nationally recognized statistical rating organizations.

2. Includes all asset types that, individually, represent less than five percent of aggregate outstanding fair value of debt securities.

3. Rows and columns may not total due to rounding.

At December 31, 2009, approximately 44 percent of the properties collateralizing the non-agency RMBS held by ML II were located in California and Florida based on the geographic location data available for the underlying loans by aggregate unpaid principal balance.

(e) Maiden Lane III LLC

The primary holdings within ML III are ABS CDOs. An ABS CDO is a security issued by a bankruptcy remote entity that is backed by a diversified pool of debt securities, which in the case of ML III are primarily RMBS and CMBS. The cash flows of ABS CDOs can be split into multiple segments, called "tranches," which vary in risk profile and yield. The junior tranches bear the initial risk of loss, followed by the more senior tranches. The ABS CDOs in the ML III portfolio largely represent senior tranches. Because they are shielded from defaults by the subordinated tranches, senior tranches typically have higher credit ratings and lower yields than the underlying securities, and will often receive investment-grade ratings from one or more of the nationally recognized rating agencies. Despite the protection afforded by the subordinated tranches, senior tranches can experience substantial losses from actual defaults on the underlying non-agency RMBS or CMBS.

ABS CDO securities are limited recourse obligations of the issuer thereof payable solely from the underlying securities owned by the issuer or proceeds thereof. Consequently, holders of ABS CDO securities must rely solely on distributions on the collateral underlying such ABS CDO securities or the proceeds thereof for payment. Such collateral may consist of investment-grade debt securities, high-yield debt securities, loans, structured finance securities, synthetic securities and other debt instruments. Investments in assets through the purchase of synthetic securities present risks in addition to those resulting from direct purchases of those assets because the buyer of such synthetic security usually will have a contractual relationship only with the synthetic security counterparty and not the obligor on the reference obligation of such synthetic security. The buyer of a synthetic security will not benefit from any collateral supporting the reference obligation of such synthetic security, will not have any remedies that would normally be available to the holder of such reference obligation, and will be subject to the credit risk of the synthetic security counterparty as well as the obligor on such reference obligation. Over the last several years, there has been a significant increase in the default rates of, delinquencies on, and rating downgrades reported on RMBS and CMBS. As a result of increases in the default rates and delinquencies, there has been a decrease in the amount of credit support available for the ABS CDO securities backed by such RMBS and CMBS since the issue date thereof. Diminished credit support as a result of increases in the default rates of, delinquencies on, and rating downgrades reported on RMBS and CMBS could increase the likelihood that payments may not be made to holders of ABS CDO securities.

Certain ABS CDO issuers can issue short-term eligible investments under Rule 2a-7 of the Investment Company Act of 1940 if the ABS CDO contains arrangements to remarket the securities at defined periods. The investments must contain put options ("2a-7 Puts") which allow the purchasers to sell the ABS CDO at par to a third-party ("Put Provider"), if a scheduled remarketing is unsuccessful due to reasons other than a credit or bankruptcy event. As of December 31, 2009, the total notional value of ABS CDOs held by ML III with embedded 2a-7 Puts, for which AIGFP was, directly or indirectly, the Put Provider, was $1.6 billion. ML III has entered into an agreement not to exercise the 2a-7 Puts, or to only exercise the 2a-7 Puts if it simultaneously repurchases the ABS CDOs at par. In return, ML III will receive the put premiums and AIGFP will take the necessary steps to attempt conversion of the ABS CDOs to long-term notes. The termination dates of this agreement range from December 31, 2010 to April 30, 2011 depending on the respective ABS CDOs.

CMBS and RMBS expose ML III to varying levels of credit, interest rate, liquidity, and concentration risk. Credit-related risk arises from losses due to delinquencies and defaults by borrowers on the underlying mortgage loans and breaches by originators and servicers of their obligations under the underlying documentation pursuant to which the securities are issued. The rate of delinquencies and defaults on residential and commercial mortgage loans and the aggregate amount of the resulting losses can be affected by a number of factors, including general economic conditions, particularly those in the area where the related mortgaged property is located; the level of the borrower's equity in the mortgaged property; and the individual financial circumstances of the borrower.

At December 31, 2009, the investment type/vintage and rating composition of ML III's $22,339 million portfolio, recorded at fair value, as a percentage of aggregate fair value of all securities in the portfolio was as follows:

	Rating[1,2,3]						
	AAA	AA+ to AA-	A+ to A-	BBB+ to BBB-	BB+ and Lower	Not Rated	Total
ABS CDOs:							
High-Grade ABS CDOs	0.0%	0.0%	0.0%	0.0%	68.9%	0.0%	68.9%
Pre-2005	0.0%	0.0%	0.0%	0.0%	24.3%	0.0%	24.3%
2005	0.0%	0.0%	0.0%	0.0%	30.6%	0.0%	30.6%
2006	0.0%	0.0%	0.0%	0.0%	7.3%	0.0%	7.3%
2007	0.0%	0.0%	0.0%	0.0%	6.7%	0.0%	6.7%
Mezzanine ABS CDOs	0.0%	0.2%	0.0%	0.5%	8.0%	0.3%	8.9%
Pre-2005	0.0%	0.2%	0.0%	0.5%	4.4%	0.3%	5.4%
2005	0.0%	0.0%	0.0%	0.0%	2.8%	0.0%	2.8%
2006	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
2007	0.0%	0.0%	0.0%	0.0%	0.7%	0.0%	0.7%
Commercial Real-Estate CDOs	1.5%	0.5%	18.9%	0.0%	0.0%	0.0%	21.0%
Pre-2005	1.5%	0.5%	3.1%	0.0%	0.0%	0.0%	5.2%
2005	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
2006	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
2007	0.0%	0.0%	15.8%	0.0%	0.0%	0.0%	15.8%
RMBS, CMBS, & Other:	0.2%	0.2%	0.1%	0.1%	0.6%	0.0%	1.2%
Pre-2005	0.0%	0.0%	0.0%	0.0%	0.1%	0.0%	0.2%
2005	0.1%	0.1%	0.1%	0.1%	0.4%	0.0%	0.9%
2006	0.0%	0.0%	0.0%	0.0%	0.1%	0.0%	0.1%
2007	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Total Investments	1.7%	0.8%	19.1%	0.6%	77.5%	0.3%	100.0%

1. Lowest of all ratings is used for the purposes of this table if rated by two or more nationally recognized statistical rating organizations.
2. The year of issuance with the highest concentration of underlying assets as measured by outstanding principal balance determines the vintage of the CDO.
3. Rows and columns may not total due to rounding

(f) TALF LLC

TALF loans are extended on a non-recourse basis by the FRBNY. If the borrower does not repay the loan, the FRBNY will enforce its rights in the collateral and may sell the collateral, pursuant to a put agreement, to TALF LLC, established for the purpose of purchasing such assets. As of December 31, 2009 the FRBNY did not enforce its rights to the TALF loan collateral or exercise the put option. As a result, TALF LLC did not purchase any assets from the FRBNY.

Cash receipts resulting from the put option fees paid to the TALF LLC and proceeds from the Treasury's subordinated loan are invested in the following types of U.S. dollar-denominated short-term investments and cash equivalents eligible for purchase by the TALF LLC: (1) Treasury securities, (2) federal agency securities that are senior, negotiable debt obligations of the Federal National Mortgage Association ("FNMA"), Federal Home Loan Mortgage Corporation ("FHLMC"), Federal Home Loan Banks ("FHLB"), and Federal Farm Credit Banks ("FFCB") which have a fixed rate of interest, (3) repurchase agreements that are collateralized by Treasury and federal agency securities and fixed-rate agency MBS, and (4) money market mutual funds registered with the Securities and Exchange Commission and regulated under Rule 2a-7 of the Investment Company Act that invest exclusively in Treasury and federal agency securities.

(g) Fair-Value Measurement

The consolidated VIEs have adopted ASC 820 and ASC 825 and have elected the fair value option for all securities and commercial and residential mortgages held by ML and TALF LLC. ML II and ML III qualify as nonregistered investment companies under the provisions of ASC 946 and, therefore, all investments are recorded at fair value in accordance with ASC 820. In addition, the FRBNY has elected to record the beneficial interests in ML, ML II, ML III, and the TALF LLC at fair value.

The accounting and classification of these investments appropriately reflects the VIEs' and the FRBNY's intent with respect to the purpose of the investments and most closely reflects the amount of the assets available to liquidate the entities' obligations.

i. Fair Value Hierarchy

ASC 820 establishes a three-level fair value hierarchy that distinguishes between market participant assumptions developed using market data obtained from independent sources (observable inputs) and the consolidated VIEs assumptions about market participant assumptions developed using the best information available in the circumstances (unobservable inputs).

The three levels established by ASC 820 are described below:

- Level 1 — Valuation is based on quoted prices for identical instruments traded in active markets.
- Level 2 — Valuation is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 — Valuation is based on inputs from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the consolidated VIE's estimates of assumptions that market participants would use in pricing the asset and liability. Valuation techniques include the use of option pricing models, discounted cash flow models, and similar techniques.

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

ii. Determination of Fair Value

The consolidated VIEs value their investments on the basis of the last available bid prices or current market quotations provided by dealers, or pricing services selected by their designated investment managers. To determine the value of a particular investment, pricing services may use information on transactions in such investments; quotations from dealers; pricing metrics; market transactions in comparable investments; relationships observed in the market between investments; and calculated yield measures based on valuation methodologies commonly employed in the market for such investments.

Market quotations may not represent fair value in circumstances in which the investment manager believes that facts and circumstances applicable to an issuer, a seller, a purchaser, or the market for a particular security result in the current market quotations reflecting an inaccurate fair value of the security. To determine fair value, the investment manager applies proprietary valuation models that use collateral performance scenarios and pricing metrics derived from the reported performance of the universe of bonds with similar characteristics as well as the observable market.

Because of the inherent uncertainty of determining the fair value of investments that do not have a readily available fair value, the fair value of these investments may differ significantly from the values that would have been reported if a readily available fair value had existed for these investments and may differ materially from the values that may ultimately be realized.

The fair value of the liability for the beneficial interests of consolidated VIEs is estimated based upon the fair value of the underlying assets held by the VIEs. The holders of these beneficial interests do not have recourse to the general credit of the FRBNY.

iii. Valuation Methodologies for Level 3 Assets and Liabilities

In certain cases where there is limited activity around inputs to the valuation, securities are classified within level 3 of the valuation hierarchy. For example, in valuing CDOs, certain collateralized mortgage obligations, and commercial and residential mortgage loans, the determination of fair value is based on collateral performance scenarios. These valuations also incorporate pricing metrics derived from the reported performance of the universe of bonds as well as observations and estimates of market data. Because external price information is not available, market-based models are used to value these securities. Key inputs to the model are market spreads, data for each credit rating, collateral type, and other relevant contractual features. Because there is lack of observable pricing, securities and investment loans that are carried at fair value are classified within level 3.

The following tables present the financial instruments recorded in VIEs at fair value as of December 31 by ASC 820 hierarchy (in millions):

	2009				
	Level 1	Level 2	Level 3	Netting[1]	Total fair value
Assets:					
Cash equivalents	$1,933	$ 142	$ -	$ -	$ 2,075
CDOs	-	241	22,409	-	22,650
Non-agency RMBS	-	9,461	8,091	-	17,552
Federal agency and GSE MBS	-	18,125	24	-	18,149
Commercial mortgage loans	-	-	4,025	-	4,025
Residential mortgage loans	-	-	583	-	583
Swap contracts	-	5	3,272	(2,150)	1,127
Other investments	31	5,413	23	-	5,467
Other assets	20	-	-	-	20
Total assets	$1,984	$33,387	$38,427	$(2,150)	$71,648
Liabilities:					
Beneficial interest in consolidated VIEs	$ -	$ -	$ 5,095	$ -	$ 5,095
Swap contracts	-	195	1,816	(1,868)	143
Total liabilities	$ -	$ 195	$ 6,911	$(1,868)	$ 5,238

1. Derivative receivables and payables and the related cash collateral received and paid are shown netted when a master netting agreement exists.

	2008			
	Level 1	Level 2	Level 3	Total fair value
Assets:				
CDOs	$-	$ 155	$26,802	$26,957
Non-agency RMBS	-	8,165	12,510	20,675
Federal agency and GSE MBS	-	14,759	895	15,654
Commercial mortgage loans	-	-	5,553	5,553
Residential mortgage loans	-	-	937	937
Swap contracts	-	-	2,454	2,454
Other investments	-	1,992	348	2,340
Total assets	$-	$25,071	$49,499	$74,570
Liabilities:				
Beneficial interest in consolidated variable interest entities	$-	$ -	$ 2,824	$ 2,824

The tables below present a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (level 3) at December 31, 2009 and 2008. Unrealized gains and losses related to those assets still held at December 31, 2009 and 2008 are reported as a component of "Consolidated variable interest entities: Investments held by consolidated variable interest entities, net" in the Combined Statements of Condition.

	2009					
	Fair value January 1	Net purchases, sales, and settlements	Total realized/ unrealized gains (losses)	Net transfers in or out	Fair value December 31	Change in unrealized gains/(losses) related to financial instruments held at December 31, 2009
Assets:						
CDOs	$26,802	$(3,123)	$(1,267)	$ (3)	$22,409	$(1,265)
Non-agency RMBS	12,510	(1,481)	(499)	(2,439)	8,091	(533)
Federal agency and GSE MBS	895	(248)	-	(623)	24	-
Commercial mortgage loans	5,553	(305)	(1,223)	-	4,025	(1,177)
Residential mortgage loans	937	(86)	(268)	-	583	(219)
Other investments	348	(263)	30	(92)	23	29
Total assets	$47,045	$(5,506)	$(3,327)	$(3,157)	$35,155	$(3,165)
Net swap contracts[2]	2,454	(906)	94	(186)	1,456	212
Liabilities:						
Beneficial interest in consolidated variable interest entities	$ (2,824)	$ (368)[1]	$(1,903)	$ -	$ (5,095)	$(1,903)

1. Includes $268 million in capitalized interest.
2. Level 3 derivative assets and liabilities are presented net for the purposes of this table.

	2008					
	Fair value January 1	Net purchases, sales, and settlements	Total realized/ unrealized gains (losses)	Net transfers in or out	Fair value December 31	Change in unrealized gains/(losses) related to financial instruments held at December 31, 2008
Assets:						
CDOs	$-	$29,740	$(2,938)	$-	$26,802	$(2,938)
Non-agency RMBS	-	14,668	(2,158)	-	12,510	(2,159)
Federal agency and GSE MBS	-	891	4	-	895	4
Commercial mortgage loans	-	7,683	(2,130)	-	5,553	(2,130)
Residential mortgage loans	-	1,500	(563)	-	937	(563)
Swap contracts	-	2,369	85	-	2,454	155
Other investments	-	625	(277)	-	348	(278)
Total assets	$-	$57,476	$(7,977)	$-	$49,499	$(7,909)
Liabilities:						
Beneficial interest in consolidated variable interest entities	$-	$ (7,213)[1]	$ 4,389	$-	$ (2,824)	$ 4,389

1. Includes $63 million in capitalized interest.

(h) Professional Fees

The consolidated VIEs have recorded costs for professional services provided by several nationally recognized institutions to serve as investment managers, administrators, and custodians for the VIEs' assets. The fees charged by the investment managers, custodians, and administrators, as well as the auditors, attorneys, and other service providers, are recorded in "Professional fees related to consolidated variable interest entities" in the Combined Statements of Income and Comprehensive Income.

(10) Non-Consolidated Variable Interest Entities

In December 2009, the FRBNY obtained preferred securities in two VIEs. The FRBNY does not consolidate these VIEs because it does not have a controlling financial interest. The FRBNY's maximum exposure to any potential losses of the VIEs, should they occur, is limited to the recorded value of the FRBNY's investment in the preferred securities and dividends receivable from the VIE. The following table shows the financial information related to nonconsolidated VIEs for the year ended December 31, 2009 (in millions):

	AIA LLC	ALICO LLC	Total Non-Consolidated VIEs
Total assets	$89,100	$114,800	$203,900
Total liabilities	73,600	100,800	174,400
Maximum exposure to loss	16,068	9,038	25,106

The recorded value of the FRBNY's investment in the preferred securities, including capitalized dividends, was $16,068 million for AIA LLC and $9,038 million for ALICO LLC at December 31, 2009. The FRBNY's investment in preferred securities and capitalized dividends is reported as "Preferred securities" and dividends receivable are reported as a component of "Other assets" in the Combined Statements of Condition.

The fair value of the FRBNY's preferred interests in AIA LLC and ALICO LLC was not materially different from the amount reported as "Preferred securities" in the Combined Statements of Condition as of December, 31, 2009.

(11) Bank Premises, Equipment, And Software

Bank premises and equipment at December 31 were as follows (in millions):

	2009	2008
Bank premises and equipment:		
Land	$ 344	$ 334
Buildings	2,378	2,161
Building machinery and equipment	492	463
Construction in progress	43	160
Furniture and equipment	1,010	1,037
Subtotal	4,267	4,155
Accumulated depreciation	(1,643)	(1,583)
Bank premises and equipment, net	$ 2,624	$ 2,572
Depreciation expense, for the years ended December 31	$ 202	$ 199

Bank premises and equipment at December 31 included the following amounts for capitalized leases (in millions):

	2009	2008
Leased premises and equipment under capital leases	$10	$ 21
Accumulated depreciation	(6)	(13)
Leased premises and equipment under capital leases, net	$ 4	$ 8
Depreciation expense related to leased premises and equipment under capital leases	$ 2	$ 4

The Reserve Banks lease space to outside tenants with remaining lease terms ranging from one to fifteen years. Rental income from such leases was $32 million and $30 million for the years ended December 31, 2009 and 2008, respectively, and is reported as a component of “Other income” in the Combined Statements of Income and Comprehensive Income. Future minimum lease payments that the Reserve Banks will receive under noncancelable lease agreements in existence at December 31, 2009 were as follows (in millions):

2010	$ 28
2011	24
2012	21
2013	20
2014	19
Thereafter	54
Total	$166

The Reserve Banks had capitalized software assets, net of amortization, of $134 million and $129 million at December 31, 2009 and 2008, respectively. Amortization expense was $52 million and $67 million for the years ended December 31, 2009 and 2008, respectively. Capitalized software assets are reported as a component of “Other assets” in the Combined Statements of Condition and the related amortization is reported as a component of “Other expenses” in the Combined Statements of Income and Comprehensive Income.

Assets impaired as a result of the Reserve Banks’ restructuring plans, as discussed in Note 16, include check equipment, leasehold improvements, and furniture assets. Asset impairment losses of $2 million for the year ended December 31, 2008 were determined using fair values based on quoted fair values or other valuation techniques and are reported as a component of “Operating expenses: Other expenses” in the Combined Statements of Income and Comprehensive Income. There were no asset impairments for the year ended December 31, 2009.

(12) Commitments And Contingencies

In the normal course of operations the Reserve Banks enter into contractual commitments, normally with fixed expiration dates or termination provisions, at specific rates and for specific purposes.

At December 31, 2009, the Reserve Banks were obligated under noncancelable leases for premises and equipment with remaining terms ranging from one to approximately 14 years. These leases provide for increased rental payments based upon increases in real estate taxes, operating costs, or selected price indices.

Rental expense under operating leases for certain operating facilities, warehouses, and data processing and office equipment (including taxes, insurance, and maintenance when included in rent), net of sublease rentals, was $27 million for each of the years ended December 31, 2009 and 2008.

Future minimum rental payments under noncancelable operating leases, net of sublease rentals, with remaining terms of one year or more, at December 31, 2009 are as follows (in millions):

	Operating leases
2010	$ 11
2011	12
2012	12
2013	11
2014	11
Thereafter	95
Future minimum rental payments	$ 152

At December 31, 2009, the Reserve Banks had unrecorded unconditional purchase commitments and long-term obligations extending through the year 2017 with a remaining fixed commitment of $206 million. Purchases of $28 million and $33 million were made against these commitments during 2009 and 2008, respectively. These commitments represent maintenance of currency processing machines and have variable and/or fixed components. The variable portion of the commitments is for additional services above fixed contractual service limits. The fixed payments for the next five years under these commitments are as follows (in millions):

2010	$32
2011	23
2012	23
2013	24
2014	25

The Reserve Banks are involved in certain legal actions and claims arising in the ordinary course of business. Although it is difficult to predict the ultimate outcome of these actions, in management's opinion, based on discussions with counsel, the aforementioned litigation and claims will be resolved without material adverse effect on the financial position or results of operations of the Reserve Banks.

Other Commitments

In support of financial market stability activities, the Reserve Banks entered into commitments to provide financial assistance and backstop support to financial institutions. The contractual amount represents the Reserve Banks' maximum exposure to loss in the event that the commitments are fully funded and there is a default by the borrower or total loss in value of pledged collateral. Total commitments at December 31, 2009 and 2008 were as follows (in millions):

	2009		2008	
	Contractual amount	Unfunded amount	Contractual amount	Unfunded amount
Loan commitment (Citigroup)	$ -	$ -	$244,800	$244,800
Secured line of credit (AIG)	35,000	17,100	60,000	23,200
Commercial loan commitments (ML)	157	157	266	266
Total	$35,157	$17,257	$305,066	$268,266

The agreement with Citigroup, while legally a loan commitment, is accounted for in accordance with FASB ASC Topic 460 (ASC 460), Guarantees (previously FIN 45). This agreement was terminated effective December 23, 2009 and, as a result, the FRBNY had no contractual obligation at December 31, 2009. The termination fee of $50 million is reported as a component of "Other income" in the Combined Statements of Income.

The secured line of credit relates to the undrawn portion of the FRBNY's commitment to lend to AIG. The amount of the FRBNY's commitment to lend to AIG was reduced during the year ended December 31, 2009 as a result of the debt restructuring described in Note 3, Note 4, and Note 5. Collateral to secure the FRBNY's loan to AIG includes the equity in AIG's subsidiaries. The FRBNY does not expect to incur any losses related to the unfunded commitment as of December 31, 2009.

The undrawn portion of the FRBNY's commercial loan commitment relates to commercial mortgage loans acquired by ML.

(13) Retirement And Thrift Plans

Retirement Plans

The Reserve Banks currently offer three defined benefit retirement plans to their employees, based on length of service and level of compensation. Substantially all of the employees of the Reserve Banks, Board of Governors, and Office of Employee Benefits of the Federal Reserve System ("OEB") participate in the Retirement Plan for Employees of the Federal Reserve System ("System Plan"). In addition, employees at certain compensation levels participate in the Benefit Equalization Retirement Plan ("BEP") and certain Reserve Bank officers participate in the Supplemental Retirement Plan for Select Officers of the Federal Reserve Bank ("SERP").

The System Plan provides retirement benefits to employees of the Federal Reserve Banks, the Board of Governors, and OEB. The FRBNY, on behalf of the System, recognizes the net asset or net liability and costs associated with the System Plan in its consolidated financial statements. Costs associated with the System Plan are not reimbursed by other participating employers.

Following is a reconciliation of the beginning and ending balances of the System Plan benefit obligation (in millions):

	2009	2008
Estimated actuarial present value of projected benefit obligation at January 1	$7,031	$5,325
Service cost-benefits earned during the period	204	150
Interest cost on projected benefit obligation	427	357
Actuarial (gain) loss	(28)	599
Contributions by plan participants	3	3
Special termination benefits	9	9
Benefits paid	(291)	(280)
Plan amendments	9	868
Estimated actuarial present value of projected benefit obligation at December 31	$7,364	$7,031

Following is a reconciliation showing the beginning and ending balance of the System Plan assets, the funded status, and the accrued pension benefit costs (in millions):

	2009	2008
Estimated plan assets at January 1 (of which $5,037 million and $6,566 million is measured at fair value as of January 1, 2009 and 2008, respectively)	$ 5,053	$ 6,604
Actual return on plan assets	1,016	(1,274)
Contributions by the employer	500	-
Contributions by plan participants	3	3
Benefits paid	(291)	(280)
Estimated plan assets at December 31 (of which $6,252 million and $5,037 million is measured at fair value as of December 31, 2009 and 2008, respectively)	$ 6,281	$ 5,053
Funded status and accrued pension benefit costs	$(1,083)	$(1,978)
Amounts included in accumulated other comprehensive loss are shown below:		
Prior service cost	$ (883)	$ (989)
Net actuarial loss	(2,488)	(3,429)
Total accumulated other comprehensive loss	$(3,371)	$(4,418)

Accrued pension benefit costs are reported as “Accrued benefit costs” in the Combined Statements of Condition.

The accumulated benefit obligation for the System Plan, which differs from the estimated actuarial present value of projected benefit obligation because it is based on current rather than future compensation levels, was $6,430 million and $6,143 million at December 31, 2009 and 2008, respectively.

The weighted-average assumptions used in developing the accumulated and projected pension benefit obligations for the System Plan as of December 31 were as follows:

	2009	2008
Discount rate	6.00%	6.00%
Rate of compensation increase	5.00%	5.00%

Net periodic benefit expenses for the years ended December 31, 2009 and 2008 were actuarially determined using a January 1 measurement date. In 2008, several amendments were made to the plan. As a result, the actuarially determined net periodic benefit expenses for the year ended December 31, 2008 were remeasured as of November 1, 2008 using a 7.75% discount rate. The plan amendments, the most significant of which was to incorporate annual, rather than ad-hoc, cost-of-living adjustments to the participants’ plan benefit, resulted in a $60 million increase in net periodic benefit expenses for the year ended December 31, 2008. There were no significant benefit changes approved in 2009.

The weighted-average assumptions used in developing net periodic benefit expenses for the System Plan for the years were as follows:

	2009	2008
Discount rate	6.00%	6.50%
Expected asset return	7.75%	8.00%
Rate of compensation increase	5.00%	5.00%

Discount rates reflect yields available on high-quality corporate bonds that would generate the cash flows necessary to pay the System Plan's benefits when due. The expected long-term rate of return on assets was based on a combination of factors, including the System Plan's asset allocation strategy and historical returns; surveys of expected rates of return for other entities' plans; a projected return for equities and fixed income investments based on real interest rates, inflation expectations, and equity risk premiums; and surveys of expected returns in equity and fixed income markets.

The components of net periodic pension benefit expense for the System Plan for the years ended December 31 are shown below (in millions):

	2009	2008
Service cost-benefits earned during the period	$ 204	$ 150
Interest cost on accumulated benefit obligation	427	357
Amortization of prior service cost	116	41
Amortization of net loss	285	78
Expected return on plan assets	(389)	(497)
Net periodic pension benefit expense	643	129
Special termination benefits	9	9
Total net periodic pension benefit expense	$ 652	$ 138
Estimated amounts that will be amortized from accumulated other comprehensive loss into net periodic pension benefit expense in 2010 are shown below:		
Prior service cost	$ 112	
Net actuarial loss	181	
Total	$ 293	

The recognition of special termination benefits is primarily the result of enhanced retirement benefits provided to employees during the restructuring described in Note 16.

Following is a summary of expected benefit payments, excluding enhanced retirement benefits (in millions):

	Expected benefit payments
2010	$ 332
2011	343
2012	364
2013	388
2014	411
2015–2018	2,389
Total	$ 4,227

The System's Committee on Investment Performance ("CIP") is responsible for establishing investment policies, selecting investment managers, and monitoring the investment managers' compliance with the policies. At December 31, 2009, the System Plan's assets were held in six investment vehicles: a constant-mix asset allocation account, a liability-linked account, an indexed U.S. investment-grade bond fund, an indexed U.S. equity fund, a non-U.S. developed-markets fund, and a money market fund. The diversity in investment vehicles is to limit concentration of risk and the risk of loss related to any specific sector. The constant mix account tracks the Standard & Poor's 500 Stock Index and the Barclays Aggregate Bond Index, and is automatically rebalanced. The liability-linked account, funded in April 2008, seeks to defease a portion of the System Plan's liability related to retired lives using a Treasury securities portfolio. The policy governing this account calls for cash-matching the first two years of a portion of retiree benefits payments and immunizing the remaining obligation. The money market fund is the repository for cash balances and adheres to a constant dollar accounting methodology. Permitted and prohibited investments, as well as use of derivatives in the indexed vehicles for which the System Plan's assets are invested, are defined as part of the trust agreement for the selected investment vehicle. The CIP reviews this agreement as part of the selection of each investment to ensure that the trust agreement is consistent with the CIP's investment objectives for the System Plan's assets. In the case of the constant-mix asset allocation account, investments must be within the defined indices and the use of derivatives is permitted to the extent necessary to manage cash flows.

The System Plan's policy and actual asset allocations at December 31, by asset category, are as follows:

	Policy	2009 Actual	2008 Actual
U.S. equities	50.7%	53.0%	55.4%
International equities	11.8%	12.9%	5.9%
Fixed income	37.5%	33.8%	36.9%
Cash	0.0%	0.3%	1.8%
Total	100.0%	100.0%	100.0%

Contributions to the System Plan may be determined using different assumptions than those required for financial reporting. The System Plan's actuarial funding method is expected to produce a recommended annual funding range between $400 and $450 million. In 2010, the System will make monthly contributions of $35 million and will reevaluate upon completion of the 2010 actuarial valuation. The Reserve Banks' projected benefit obligation, funded status, and net pension expenses for the BEP and the SERP at December 31, 2009 and 2008, and for the years then ended, were not material.

The System Plan's investments are reported at fair value as required by ASC 820. ASC 820 establishes a three-level fair value hierarchy that distinguishes between market participant assumptions developed using market data obtained from independent sources (observable inputs) and the Reserve Banks' assumptions about market participant assumptions developed using the best information available in the circumstances (unobservable inputs).

The three levels established by ASC 820 are described below:

- Level 1 — Valuation is based on quoted prices for identical instruments traded in active markets.
- Level 2 — Valuation is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 — Valuation is based on inputs from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Reserve Banks' estimates of assumptions that market participants would use in pricing the asset and liability. Valuation techniques include the use of option pricing models, discounted cash flow models, and similar techniques.

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

The following tables present the financial instruments recorded at fair value as of December 31 by ASC 820 hierarchy (in millions):

	2009			
Description	Level 1	Level 2	Level 3	Total
Short-term investments	$ -	$ 24	$-	$ 24
Treasury and federal agency securities	677	38	-	715
GSE debt securities	-	156	-	156
Other fixed income securities	-	128	-	128
Common stocks	883	-	-	883
Commingled funds	-	4,346	-	4,346
Total	$1,560	$4,692	$-	$6,252

	2008			
Description	Level 1	Level 2	Level 3	Total
Short-term investments	$ 15	$ 119	$-	$ 134
Treasury and federal agency securities	852	109	-	961
GSE debt securities	-	403	-	403
Other fixed income securities	-	482	-	482
Common stocks	1,905	-	-	1,905
Commingled funds	-	1,152	-	1,152
Total	$2,772	$2,265	$-	$5,037

The System Plan enters into futures contracts, traded on regulated exchanges, to manage certain risks and to maintain appropriate market exposure in meeting the investment objectives of the System Plan. The System Plan bears the market risk that arises from any unfavorable changes in the value of the securities or indexes underlying these futures contracts. The use of futures contracts involves, to varying degrees, elements of market risk in excess of the amount recorded in the Combined Statements of Condition. The guidelines established by the CIP further reduces risk by limiting the net futures positions, for most fund managers, to 15 percent of the market value of the advisor's portfolio. No limit has been established on the futures positions of the liability-driven investments, since the fund manager only executes Treasury futures.

At December 31, 2009 and 2008, cash available for futures trading was $1 million and $2 million, respectively. At December 31, 2009, there were $1 million of Treasury securities pledged as collateral. At December 31, 2008, there were no securities pledged as collateral.

Thrift Plan

Employees of the Reserve Banks participate in the defined contribution Thrift Plan for Employees of the Federal Reserve System ("Thrift Plan"). The Reserve Banks match employee contributions based on a specified formula. For the year ended December 31, 2008 and for the first three months of the year ended December 31, 2009, the Reserve Banks matched 80 percent of the first six percent of employee contributions for employees with less than five years of service and 100 percent of the first six percent of employee contributions for employees with five or more years of service. Effective April 1, 2009, the Reserve Banks match 100 percent of the first 6 percent of employee contributions from the date of hire and provide an automatic employer contribution of one percent of eligible pay. The Reserve Banks' Thrift Plan contributions totaled $82 million and $72 million for the years ended December 31, 2009 and 2008, respectively, and are reported as a component of "Salaries and other benefits" in the Combined Statements of Income and Comprehensive Income.

(14) Postretirement Benefits Other Than Retirement Plans And Postemployment Benefits

Postretirement Benefits Other Than Retirement Plans

In addition to the Reserve Banks' retirement plans, employees who have met certain age and length-of-service requirements are eligible for both medical benefits and life insurance coverage during retirement.

The Reserve Banks fund benefits payable under the medical and life insurance plans as due and, accordingly, have no plan assets.

Following is a reconciliation of the beginning and ending balances of the benefit obligation (in millions):

	2009	2008
Accumulated postretirement benefit obligation at January 1	$1,221	$1,121
Service cost benefits earned during the period	40	38
Interest cost on accumulated benefit obligation	74	71
Net actuarial loss	54	54
Curtailment gain	-	(10)
Special termination benefits	1	-
Contributions by plan participants	16	15
Benefits paid	(79)	(72)
Medicare Part D subsidies	5	4
Plan amendments	(8)	-
Accumulated postretirement benefit obligation at December 31	$1,324	$1,221

At December 31, 2009 and 2008, the weighted-average discount rate assumptions used in developing the postretirement benefit obligation were 5.75 percent and 6.00 percent, respectively.

Discount rates reflect yields available on high-quality corporate bonds that would generate the cash flows necessary to pay the plan's benefits when due.

Following is a reconciliation of the beginning and ending balance of the plan assets, the unfunded postretirement benefit obligation, and the accrued postretirement benefit costs (in millions):

	2009	2008
Fair value of plan assets at January 1	$ -	$ -
Contributions by the employer	58	53
Contributions by plan participants	16	15
Benefits paid	(79)	(72)
Medicare Part D subsidies	5	4
Fair value of plan assets at December 31	$ -	$ -
Unfunded obligation and accrued postretirement benefit cost	$1,324	$1,221
Amounts included in accumulated other comprehensive loss are shown below:		
Prior service cost	$ 33	$ 44
Net actuarial loss	(338)	(313)
Deferred curtailment gain	-	4
Total accumulated other comprehensive loss	$ (305)	$ (265)

Accrued postretirement benefit costs are reported as a component of "Accrued benefit costs" in the Combined Statements of Condition.

For measurement purposes, the assumed health care cost trend rates at December 31 are as follows:

	2009	2008
Health care cost trend rate assumed for next year	7.50%	7.50%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.00%	5.00%
Year that the rate reaches the ultimate trend rate	2015	2014

Assumed health care cost trend rates have a significant effect on the amounts reported for health care plans. A one percentage point change in assumed health care cost trend rates would have the following effects for the year ended December 31, 2009 (in millions):

	One percentage point increase	One percentage point decrease
Effect on aggregate of service and interest cost components of net periodic postretirement benefit costs	$ 15	$ (13)
Effect on accumulated postretirement benefit obligation	135	(115)

The following is a summary of the components of net periodic postretirement benefit expense for the years ended December 31 (in millions):

	2009	2008
Service cost for benefits earned during the period	$ 40	$ 38
Interest cost on accumulated benefit obligation	74	71
Amortization of prior service cost	(20)	(20)
Amortization of net actuarial loss	29	27
Total periodic expense	123	116
Curtailment gain	(4)	(1)
Special termination benefits loss	1	-
Net periodic postretirement benefit expense	$120	$115
Estimated amounts that will be amortized from accumulated other comprehensive loss into net periodic postretirement benefit expense in 2010 are shown below:		
Prior service cost	$ (18)	
Net actuarial loss	29	
Total	$ 11	

Net postretirement benefit costs are actuarially determined using a January 1 measurement date. At January 1, 2009 and 2008, the weighted-average discount rate assumptions used to determine net periodic postretirement benefit expense were 6.00 percent and 6.25 percent, respectively.

Net periodic postretirement benefit expense is reported as a component of "Salaries and other benefits" in the Combined Statements of Income and Comprehensive Income.

The recognition of special termination benefits is primarily the result of enhanced retirement benefits provided to employees during the restructuring described in Note 16. A net curtailment gain associated with restructuring programs that are described in Note 16 was recognized in net income in the year ended December 31, 2009, related to employees who terminated employment during 2009. A deferred curtailment gain was recorded in 2008 as a component of accumulated other comprehensive loss; the gain is recognized in net income in 2009 and future years when the related employees terminate employment.

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 established a prescription drug benefit under Medicare ("Medicare Part D") and a federal subsidy to sponsors of retiree health care benefit plans that provide benefits that are at least actuarially equivalent to Medicare Part D. The benefits provided under the Reserve Banks' plan to certain participants are at least actuarially equivalent to the Medicare Part D prescription drug benefit. The estimated effects of the subsidy are reflected in actuarial loss in the accumulated postretirement benefit obligation and net periodic postretirement benefit expense.

Federal Medicare Part D subsidy receipts were $6.4 million and $3.3 million in the years ended December 31, 2009 and 2008, respectively. Expected receipts in 2010, related to benefits paid in the years ended December 31, 2009 and 2008, are $1 million.

Following is a summary of expected postretirement benefit payments (in millions):

	Without subsidy	With subsidy
2010	$ 76	$ 70
2011	82	76
2012	87	80
2013	92	85
2014	97	88
2015–2019	548	494
Total	$982	$893

Postemployment Benefits

The Reserve Banks offer benefits to former or inactive employees. Postemployment benefit costs are actuarially determined using a December 31 measurement date and include the cost of medical and dental insurance, survivor income, disability benefits, and self-insured workers' compensation expenses. The accrued postemployment benefit costs recognized by the Reserve Banks at December 31, 2009 and 2008, were $153 million and $117 million, respectively. This cost is included as a component of "Accrued benefit costs" in the Combined Statements of Condition. Net periodic postemployment benefit expense included in 2009 and 2008 operating expenses were $56 million and $10 million, respectively, and are recorded as a component of "Salaries and other benefits" in the Combined Statements of Income and Comprehensive Income.

(15) Accumulated Other Comprehensive Income and Other Comprehensive Income

Following is a reconciliation of beginning and ending balances of accumulated other comprehensive income (loss) (in millions):

	Amount related to defined benefit retirement plan	Amount related to postretirement benefits other than retirement plans	Total accumulated other comprehensive income (loss)
Balance at January 1, 2008	$(1,298)	$(226)	$(1,524)
Change in funded status of benefit plans:			
Prior service costs arising during the year	(868)	4	(864)
Net actuarial loss arising during the year	(2,371)	(48)	(2,419)
Deferred curtailment gain	-	1	1
Amortization of prior service cost	41	(20)	21
Amortization of net actuarial loss	78	27	105
Amortization of deferred curtailment gain	-	(3)	(3)
Change in funded status of benefit plans—other comprehensive loss	(3,120)	(39)	(3,159)
Balance at December 31, 2008	$(4,418)	$(265)	$(4,683)
Change in funded status of benefit plans:			
Prior service costs arising during the year	$ (10)	$ 9	$ (1)
Net actuarial gain (loss) arising during the year	656	(54)	602
Amortization of prior service cost	116	(20)	96
Amortization of net actuarial loss	285	29	314
Amortization of deferred curtailment gain	-	(4)	(4)
Change in funded status of benefit plans—other comprehensive income (loss)	1,047	(40)	1,007
Balance at December 31, 2009	$(3,371)	$(305)	$(3,676)

Additional detail regarding the classification of accumulated other comprehensive loss is included in Notes 13 and 14.

(16) Business Restructuring Charges

2009 Restructuring Plans

In 2009, the Reserve Banks continued their check restructuring initiatives to align check-processing infrastructure and operations with declining check-processing volumes. Additional announcements in 2009 included restructuring plans associated with discontinuing check print sites.

2008 Restructuring Plans

In 2008, the Reserve Banks announced the acceleration of their check-restructuring initiatives to align the check-processing infrastructure and operations with declining check-processing volumes. The new infrastructure consolidates operations into two regional Reserve Bank processing sites in Cleveland and Atlanta. Additional announcements in 2008 included restructuring plans associated with the closure of a check processing contingency center and the consolidation of check adjustments sites.

2007 and Prior Restructuring Plans

The Reserve Banks incurred various restructuring charges prior to 2008 related to aligning the check-processing infrastructure and operations with declining processing volumes. The new infrastructure would involve consolidation of operations into four regional Reserve Bank processing sites in Philadelphia, Cleveland, Atlanta, and Dallas. Additional announcements in 2007 included restructuring plans associated with the U.S. Treasury's Collections and Cash Modernization initiative. The Reserve Banks incurred various restructuring charges prior to 2007 related to the initial phases of restructuring of the System's check-processing and cash-handling infrastructure.

Following is a summary of financial information related to the restructuring plans (in millions):

	2007 and prior restructuring plans	2008 restructuring plans	2009 restructuring plans	Total
Information related to restructuring plans as of December 31, 2009:				
Total expected costs related to restructuring activity	$ 52	$ 18	$ 4	$ 74
Estimated future costs related to restructuring activity	$ 2	$ -	$ -	$ 2
Expected completion date	2012	2010	2010	
Reconciliation of liability balances:				
Balance at January 1, 2008	$ 43	$ -	$ -	$ 43
Employee separation costs	5	17	-	22
Adjustments	(4)	-	-	(4)
Payments	(21)	-	-	(21)
Balance at December 31, 2008	$ 23	$ 17	$ -	$ 40
Employee separation costs	-	-	4	4
Adjustments	(1)	(1)	-	(2)
Payments	(16)	(7)	-	(23)
Balance at December 31, 2009	$ 6	$ 9	$ 4	$ 19

Employee separation costs are primarily severance costs for identified staff reductions associated with the announced restructuring plans. Separation costs that are provided under terms of ongoing benefit arrangements are recorded based on the accumulated benefit earned by the employee. Separation costs that are provided under the terms of one-time benefit arrangements are generally measured based on the expected benefit as of the termination date and recorded ratably over the period to termination. Restructuring costs related to employee separations are reported as a component of "Salaries and other benefits" in the Combined Statements of Income and Comprehensive Income.

Adjustments to the accrued liability are primarily due to changes in the estimated restructuring costs and are shown as a component of the appropriate expense category in the Combined Statements of Income and Comprehensive Income.

Restructuring costs associated with the impairment of certain Reserve Banks' assets, including software, buildings, leasehold improvements, furniture, and equipment, are discussed in Note 11. Costs associated with enhanced pension benefits for all Reserve Banks are recorded on the books of the FRBNY as discussed in Note 13. Costs associated with enhanced postretirement benefits are disclosed in Note 14.

(17) Subsequent Events

In February 2010, the System discontinued a contractual relationship in connection with a large-scale software development program for which the Reserve Banks had recorded costs of $34.2 million as of December 31, 2009. The Reserve Banks expect that a portion of these costs, which are recorded as a component of "Other assets," will be expensed in 2010.

On March 1, 2010, AIG announced a definitive agreement with Prudential plc for the sale of the AIA Group for approximately $35.5 billion, including approximately $25 billion in cash, $8.5 billion in Prudential plc equity securities, and $2.0 billion in Prudential plc preferred stock. The cash proceeds from the sale will be used to redeem the FRBNY's preferred interests in AIA LLC of approximately $16 billion and to repay approximately $9 billion under the FRBNY's line of credit agreement with AIG. Proceeds from the orderly sale, over time, of AIG's holdings of Prudential plc equity securities, following the agreed on holding periods, will be used to repay amounts outstanding under the FRBNY's line of credit agreement with AIG.

On March 8, 2010, AIG announced a definitive agreement for the sale of ALICO to MetLife, Inc. for approximately $15.5 billion, including approximately $6.8 billion in cash and $8.7 billion in MetLife, Inc. equity securities, including common stock and convertible preferred securities. The cash proceeds from the sale will be used to redeem the FRBNY's preferred interests in ALICO LLC of approximately $9 billion. Proceeds from the orderly sale, over time, of AIG's holdings of MetLife, Inc. equity securities, following the agreed on holding periods, will be used to redeem the remainder of the FRBNY's preferred interests in ALICO LLC, and any residual proceeds will be used to repay amounts outstanding under the FRBNY's line of credit agreement with AIG.

On April 8, 2010, an agreement was reached to modify approximately $4.1 billion of commercial mortgage and mezzanine loans held in ML's investment portfolio. These loans, which represent ML's largest investment based on unpaid principal balance, are reported as hospitality loans in the table in Note 9 that discloses the concentration of unpaid principal balances in ML's investment portfolio. The key provisions of the modification include the discounted payoff of certain mezzanine loans, the conversion of most junior mezzanine loans to perferred equity, an extension of the final maturity date of the remaining loans from 2013 to 2015, and an increase in interest rates and fees. The FRBNY is evaluating the modification and does not believe that it will result in an adverse effect on the FRBNY's consolidated financial statements. Similarly, the modification is not expected to have an adverse effect on the combined financial statements.

There were no subsequent events that require adjustments to or disclosures in the combined financial statements as of December 31, 2009. Subsequent events were evaluated through April 21, 2010, which is the date that the Board issued the combined financial statements.

Office of Inspector General Activities

The Office of Inspector General (OIG) for the Federal Reserve Board operates in accordance with the Inspector General Act of 1978, as amended. The OIG conducts activities and makes recommendations to promote economy and efficiency; enhance policies and procedures; and prevent and detect waste, fraud, and abuse in Board programs and operations, including functions that the Board has delegated to the Federal Reserve Banks. Accordingly, the OIG plans and conducts audits, inspections, evaluations, investigations, and other reviews relating to Board and Board-delegated programs and operations. It also retains an independent auditor to annually audit the Board's and the Federal Financial Institutions Examination Council's financial statements. In addition, the OIG keeps the Congress and the Chairman of the Board of Governors fully informed about serious abuses and deficiencies.

During 2009, the OIG completed 13 audits, inspections, evaluations, and other reviews (table), and conducted a number of follow-up reviews to evaluate action taken on prior recommendations. Due to the sensitive nature of some of the material, certain reports were only issued internal to the Board, as indicated. The OIG also closed one investigation, issued two semiannual reports to Congress, and performed over 60 reviews of legislation and regulations related to the operations of the Board and/or the OIG.

For more information, visit the OIG website at www.federalreserve.gov/oig/.

OIG Audit, Inspection, and Evaluation Reports Issued in 2009

Report title	Month issued
Audit of Blackberry and Cell Phone Internal Controls	March
Report on the Inspection of the Board's Law Enforcement Unit (Internal Report)	March
Federal Financial Institutions Examination Council Financial Statements as of and for the Years Ended December 31, 2008, and 2007, and Independent Auditors' Report	March
Security Control Review of the Audit Logging Provided by the Information Technology General Support System (Internal Report)	March
Board of Governors of the Federal Reserve System Financial Statements as of and for the Years Ended December 31, 2008, and 2007, and Independent Auditors' Report	March
Security Control Review of the Electronic Security System (Internal Report)	June
Material Loss Review of First Georgia Community Bank	June
Material Loss Review of County Bank	September
Material Loss Review of Riverside Bank of the Gulf Coast	September
Audit of the Board's Processing of Applications for the Capital Purchase Program under the Troubled Asset Relief Program	September
Audit of Management and Accountability of Mobile Computing Devices (Internal Report)	October
Audit of the Board's Information Security Program	November
Material Loss Review of Michigan Heritage Bank	December

Government Accountability Office Reviews

Under the Federal Banking Agency Audit Act (Public Law 95–320), most Federal Reserve System operations are under the purview of the Government Accountability Office (GAO). In 2009, the GAO completed 20 reports on selected aspects of Federal Reserve operations (table). In addition, four projects concerning the Federal Reserve were in various stages of completion at year-end (table). The Federal Reserve also provided information to the GAO during the year on numerous other GAO investigations, including eight other completed reviews and two other ongoing reviews.

The reports are available directly from the GAO.

Reports Completed during 2009

Report title	Report number	Month issued (2009)
Financial Regulation: A Framework for Crafting and Assessing Proposals to Modernize the Outdated U.S. Financial Regulatory System	GAO-09-216	January
Troubled Asset Relief Program: Status of Efforts to Address Transparency and Accountability Issues	GAO-09-296	January
Bank Secrecy Act: Suspicious Activity Report Use Is Increasing, but FinCEN Needs to Further Develop and Document Its Form Revision Process	GAO-09-226	February
Bank Secrecy Act: Federal Agencies Should Take Action to Further Improve Coordination and Information-Sharing Efforts	GAO-09-227	February
Systemic Risk: Regulatory Oversight and Recent Initiatives to Address Risk Posed by Credit Default Swaps	GAO-09-397T	March
National Cybersecurity Strategy: Key Improvements Are Needed to Strengthen the Nation's Posture	GAO-09-432T	March
Financial Regulation: Review of Regulators' Oversight of Risk Management Systems at a Limited Number of Large, Complex Financial Institutions	GAO-09-499T	March
Troubled Asset Relief Program: March 2009 Status of Efforts to Address Transparency and Accountability Issues	GAO-09-504	March
Inspectors General: Independent Oversight of Financial Regulatory Agencies	GAO-09-524T	March
Designated Federal Entities: Survey of Governance Practices and the Inspector General Role	GAO-09-270	April
Federal Reserve Banks: Areas for Improvement in Information Security Controls	GAO-09-722R	May
Reverse Mortgages: Product Complexity and Consumer Protection Issues Underscore Need for Improved Controls over Counseling for Borrowers	GAO-09-606	June
Troubled Asset Relief Program: June 2009 Status of Efforts to Address Transparency and Accountability Issues	GAO-09-658	June
Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts	GAO-09-704	July
Financial Markets Regulation: Financial Crisis Highlights Need to Improve Oversight of Leverage at Financial Institutions and across System	GAO-09-739	July
Troubled Asset Relief Program: Status of Government Assistance Provided to AIG	GAO-09-975	September

Reports Completed during 2009—*continued*

Report title	Report number	Month issued (2009)
Influenza Pandemic: Key Securities Market Participants Are Making Progress, but Agencies Could Do More to Address Potential Internet Congestion and Encourage Readiness	GAO-10-8	October
Troubled Asset Relief Program: One Year Later, Actions Are Needed to Address Remaining Transparency and Accountability Challenges	GAO-10-16	October
Small Business Administration: Actions Needed to Improve the Usefulness of the Agency's Lender Risk Rating System	GAO-10-53	November
Financial Audit: Bureau of the Public Debt's Fiscal Years 2009 and 2008 Schedules of Federal Debt	GAO-10-88	November

Projects Active at Year-End 2009

Subject of project	Month initiated
Systemic risk determination	October 2008
Governance issues relating to the Troubled Asset Relief Program (TARP)	July 2009
U.S. Treasury's Capital Purchase Program	November 2009
Bank walkaways	December 2009