Federal Reserve Bank of Philadelphia | 2017 Annual Report

From Numbers to Neighborhoods

The Federal Reserve Bank of Philadelphia is one of the 12 regional Reserve Banks in the United States that, together with the Board of Governors in Washington, D.C., make up the Federal Reserve System – the nation's central bank. The System's primary role is to ensure a sound financial system and a healthy economy. The Philadelphia Fed serves the Third District, which is composed of Delaware, southern New Jersey, and central and eastern Pennsylvania.

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Introduction

In 2017, the Philadelphia Fed expanded its work to enhance the economic vitality and possibilities for all communities in the Third District, which encompasses Delaware, southern New Jersey, and central and eastern Pennsylvania. The Philadelphia Fed has long been known as a source of in-depth, unbiased research around such topics as economic mobility and consumer finance. Less is known about how Bank employees engage with partners in the region to enable residents and communities to gain access to economic opportunity and prosperity. The Philadelphia Fed's *2017 Annual Report* highlights key events and initiatives that translate numbers-related research to neighborhood-based action. The details in this report show how we are achieving that goal.

In northeast Pennsylvania, members of the Bank's Community Development and Regional Outreach Department became involved in efforts to create a transit system that meets the needs of all residents. The Northeast Pennsylvania Equitable Transit Planning Council more than tripled in size from 20 to 70 participants, a measurable sign that engagement across various specialties expanded the conversation and underscored the need for local experience to solve local problems. On a broader scale, the Consumer Finance Institute (CFI) shed light on issues related to how households earn, spend, save, and borrow. The CFI produced important research on critical privacy issues, financial health among cognitively impaired elderly people, and the economic impact of student loans.

Through the robust work done by the Bank's economists, researchers, and outreach specialists, the Philadelphia Fed creates information and data that enable policymakers to make monetary and regulatory policy decisions. Bank examiners harness data and weigh intangibles to be sure area financial institutions meet the needs of the communities they serve by managing risks, offering the right products, and using cybersecurity tools to protect consumer data.

The Philadelphia Fed places high value on the region it serves. That's why employees aim to be the best at what they do, leading both as an organization and as individuals. Philadelphia Fed President Patrick T. Harker delivered 20 public speeches this year. More than 100 employees volunteered in 2017 through PhillyFedCARES in multiple community outreach events that made visible the Bank's commitment to our communities. Over $200,000 was donated by Bank staff, and more than 1,100 pounds of food were distributed in the Third District in 2017 through employee fundraising and participation in the United Way.

The Philadelphia Fed is committed to strengthening its engagement in the Third District and to translating this leadership to outcomes that support stronger communities. This commitment is done by taking our work from numbers to neighborhoods.

President's Letter

In 2016, our annual report opened with an overview of our newly established and forthcoming initiatives. There is always some trepidation when embarking on a major new initiative, let alone several, and while the Philadelphia Fed has some of the most exceptional staff I've had the pleasure to work with, we faced a big commitment. Even the best planning and a world-class staff are no match for life's vicissitudes and the hurdles they can erect.

Not this time.

We hit the ground running and have not looked back.

The Consumer Finance Institute launched in 2017, and by the end of the year, it had already garnered widespread attention for its work in the important, but underresearched, area of elder financial abuse. Its research on subjects ranging from student loans to fintech stands out in a rich and full field, and it is already a go-to source for consumer-related data.

The Economic Growth & Mobility Project continues its work apace and launched the first Research in Action (RIA) lab in northeast Pennsylvania, working with partners across sectors to find ways to improve transportation to get residents to work, school, health care, and other amenities. The community development work at the Philadelphia Fed has always been grounded in the principle that we're most effective when we work together with a range of partners, bringing a chorus of diverse voices and ideas to the table. The RIA principles are steeped in that philosophy, and work is carried out with respect for the individual characteristics and needs of the regions we're serving. Our interest is not in imposing our own model or ideas, but to get results and improve people's lives. We do that better when we bring together multiple stakeholders, understand the specifics of the problem, and work as a team to find the best solution.

This emphasis on local understanding permeates every floor of Ten Independence Mall, as you'll see within the following pages, from keeping policymakers informed of the Fed's work and research to the appreciation for how banks throughout the District serve their communities and the economic forces that drive them.

The qualities that our team in the Third District exemplify — world-class research, a focus on results, and local understanding, to name a few — are the foundation on which we've built our strategic vision, which lets us carry out the vital mission of the Federal Reserve System.

With a big thanks to all our colleagues, I welcome you to the *2017 Annual Report*, and say, once again, that I look forward to an even more stellar report next year.

Philadelphia Fed President Patrick T. Harker on a community tour of Johnstown, PA, with Frank J. Janakovic, Johnstown's mayor

First Vice President's Letter

This year, we launched the Bank's strategic values: Innovate, Collaborate, and Be Open.

The values an organization selects say a lot about its culture. So does the spirit in which they are developed and implemented. At the Philadelphia Fed, we choose to see our values as a living, breathing set of ideals, open to both interpretation and evolution.

The core of this organizational mindset is that each value individually, and the set as a whole, will mean something slightly different to each employee at the Bank. They won't be wildly different, of course, but the minor variations reflect the underpinning philosophy that our diversity of views is one of our great strengths. Every time a colleague looks at innovation from a different angle, it makes the rest of us see things in a new light. That ability to view things from a fresh perspective is the foundation of all great organizations.

For me, innovation doesn't just mean cutting-edge technology or abandoning what works for the simple sake of change. It means taking a calculated risk when the situation calls for it. It means keeping some things, improving others, and, yes, sometimes replacing whole systems. It means rising to meet the challenges of a rapidly changing world with creativity and new ways of thinking. It means being willing to risk failure.

Collaboration means that when we work together, the sum of our combined efforts is greater than our individual parts. That means working within and across teams, across the Federal Reserve System, and with our external partners, whether we're cooperating on next-generation research or helping communities throughout the Third District find ways to become more economically mobile and sustainable.

And being open means knowing that great ideas come from all corners. One of the first things I noticed about the Philadelphia Fed was the way the executive leadership listened to colleagues at all levels, not standing on ceremony or hierarchy, but trusting in others' abilities. There are many ways for an organization to nurture and foster talent, but one of the most effective is to empower everyone to speak up and share ideas.

The Philadelphia Fed's strategic values will mean something a little different to everyone here. But at their core, they represent something universal: The way we make our Bank the strongest, most effective organization it can be to best meet the needs of our District and the nation.

The Consumer Finance Institute Studies How People Spend, Save, and Earn

Meet part of the Consumer Finance Institute's (CFI) leadership team (from left to right): Satyajit Chatterjee, Vice President, Research; Julia Cheney, Assistant Vice President and Assistant Director, CFI; and Mike Dotsey, Executive Vice President, Research, and Director, CFI.

Student loans have been the fastest growing segment of consumer debt in the past 10 years, but we know less about them than we do about other types of consumer debt such as mortgages. Hundreds of data breaches are reported in the U.S. each year, with millions of Americans affected, yet there is little research on how these incidents influence consumers. As the baby boomer generation retires, adults aged 65 and older will make up an increasingly larger share of the U.S. population. Yet no comprehensive systems are in place to help protect the elderly from financial fraud and exploitation. These are just a few examples of issues that the Federal Reserve Bank of Philadelphia's Consumer Finance Institute (CFI) examines.

The CFI launched in 2017 at the Bank's biennial conference organized jointly by the Payment Cards Center, an applied research group focusing on credit and payments, and the Economic Research Department. The CFI's mission is to increase our understanding of the way credit markets and payment systems function and how they affect the economy. These connections are critical to the Fed's mission to formulate effective monetary and regulatory policy and foster healthy household finances, a stable financial system, and a resilient economy.

The Bank is a significant source of information on the student loan market. During the year, a series of internal workshops allowed staff to learn from representatives of enterprises engaged in the private student loan markets about these firms' business models and the areas in which they operate. The sessions touched on a variety of topics, including the rise in private student lending during the Great Recession, how the increase in for-profit colleges and universities affects levels

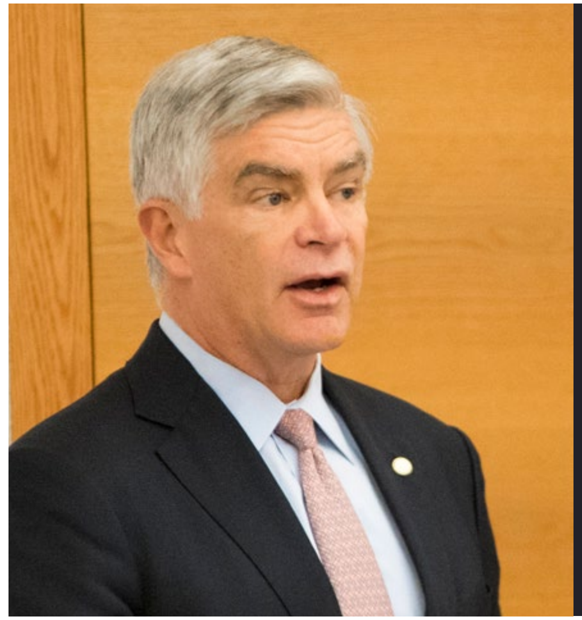
Bob Hunt, Senior Vice President and Associate Director, Consumer Finance Institute

of student debt and rates of default, and the growth of privately funded refinancing and other forms of alternative student lending. Fact-finding events such as these inform the focus of future research and help the institution better serve as a resource to industry, the regulatory community, and the general public.

As data breaches become an increasingly common occurrence for American consumers, the CFI continues to explore this issue. One CFI study examined how people responded to a data breach at the South Carolina Department of Revenue. The paper found that many individuals directly exposed to the breach took steps to protect themselves from fraud. On the other hand, most consumers who were not directly exposed but who had learned of the breach through news reports did little to protect themselves. While this research suggests that the incident did not appear to have undermined consumer confidence in the credit card system, the findings raise questions about the efficacy of breach notifications, something that may be of interest to policymakers designing future consumer privacy protection regulations.

During the year, the CFI analyzed the challenges presented by an aging population facing increased risk for financial fraud and exploitation. Together with the Penn Memory Center and University of Pennsylvania's Healthy Brain Research Center, the CFI cohosted a conference that brought together brain researchers, financial institution executives, and advocates for the elderly to discuss the latest research on cognitive impairment and the best ways to safeguard elder financial health. A CFI study explored how data sharing among financial institutions could help to detect early signs of impairment, fraud, and abuse. Because balancing suspicions of fraud against privacy rights is a chief concern in this area, the paper noted the need for a regulatory environment that enables institutions to more easily share information with family, caregivers, or other institutions while maintaining the privacy of consumers.

In his remarks announcing the launch of the CFI, Philadelphia Fed President Patrick T. Harker made the case for increasing the Bank's focus on issues around consumer finance, a vital sector that "touches every aspect of the economy." He noted that the Great Recession had perhaps brought the significance of this area of the economy into much starker relief.



> "There has never been a more important time for research on the complex ways Americans spend, save, and owe."
>
> - Philadelphia Fed President Patrick T. Harker

"There has never been a more important time for research on the complex ways Americans spend, save, and owe," Harker said. "These affect both the overall U.S. and local economies — and, of course, individuals, families, and communities."

Research into student loan debt, the fastest growing segment of consumer debt in the past 10 years, is a major focus of the Consumer Finance Institute.

Philanthropist Brooke Astor with her grandson, Philip Marshall, now a renowned elder justice advocate. Marshall, who turned in his father when he suspected financial abuse of his grandmother, shared his personal story at a November conference focusing on the financial health of older Americans.

New Initiative Promotes More Inclusive Economic Growth

Ashley Putnam, Director of the Economic Growth & Mobility Project, is leading the Bank's efforts to foster community-driven solutions to complex local problems.

With the launch of the Economic Growth & Mobility Project (EGMP) in early 2017 within the Community Development and Regional Outreach Department, the Philadelphia Fed moved beyond its strengths of convening power and research, exploring a new partnership model with leaders in the private, nonprofit, and philanthropic sectors to promote more inclusive economic growth in the region and to create pathways out of poverty in communities across the Third District.

Rather than the Bank driving that effort, the model under EGMP is intended to bring about local solutions to complex local problems, said Ashley Putnam, director of the EGMP, who embraced a similar ethos in her previous role in the New York Mayor's Office of Workforce Development.

"It has to be community driven," Putnam said. "We're hearing from communities — things they need, economic issues they're facing — and then we're bringing data to bear on those problems."

The Bank selected the Scranton–Wilkes-Barre–Hazleton area in northeast Pennsylvania as the first community of focus. The EGMP's inaugural Research in Action lab zeroed in on transportation. The Bank through its ongoing outreach had been hearing about transportation being a critical barrier to job access, quality health care, and getting children to school — holding back growth in that part of the Third District.

That effort led to the creation of the Northeast Pennsylvania Equitable Transit Planning Council, which quickly grew from 20 members at its start to more than 70 by the end of the year, with a wide cross-section

Philadelphia Fed President Patrick T. Harker and other Bank officials embarked on a series of city tours to get a firsthand look at economic conditions in the Third District, including this tour in Johnstown, PA.

of fields represented — transit agencies, health care, education, local and regional businesses, and nonprofits.

"A pioneering aspect is the community partnership model we developed, really bringing a diverse group of stakeholders to the table to come together and say, 'We know this is a challenge; how do we solve it together?'" said Erin Mierzwa, strategic outreach and engagement officer, who emphasized the ability to build deeper relationships under the EGMP model. "Everyone had their own focus areas, but everyone wanted to be part of the conversation."

The council's 2017 efforts were aided by a pair of studies — one by the Bank's Kyle DeMaria, focusing on the quantitative aspects of the issues, mapping transit barriers throughout the region, and the other from The Institute for Public Policy and Economic Development at Wilkes University, focusing on the qualitative aspects, including what locals feel about transit access and the hurdles they see — and culminated in a regional summit that drew more than 100 stakeholders and national attention.

That summit was only the midpoint of the process, though, Putnam said.

"It's great to get everyone together and talk about the problems, and we want those to lead to action," she said. "Now we can say to business leaders: 'Here's what our data are saying about the region,' and they're starting to develop strategies from those data."

As work continues in 2018 on that initial lab, the EGMP focus will turn to Philadelphia and workforce development for its next lab, while also finding ways to help others replicate the EGMP's process and initial successes to tackle similar problems across the region — potentially through a workshop event or other means.

"There are a lot of other people in the Third District who are very interested in the process," Putnam said. "The hope is not that the Bank will lead seven different labs, but create a toolkit instead."

Scranton, PA, and neighboring communities were the focus of the first EGMP Research in Action lab, which dealt with transit access.

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>
> - Ashley Putnam, Director of Economic Growth & Mobility Project

Beyond the Research in Action model, the EGMP's work extended to communities and economic sectors across the District throughout the year.

A trio of city tours gave Bank officials the chance to meet with local leaders and get a firsthand look at what cities and towns across the District are facing. In Johnstown, PA, which was hit as hard as many other single-industry economies, they talked with locals about smart planning and cross-sector approaches to encouraging growth; in Wilmington, DE, they learned about the city's efforts to revive the central business district through its Downtown Development District; and in Atlantic City, NJ, they recognized the importance of anchor institutions like Stockton University, which is partnering with South Jersey Gas to build the $220 million Gateway Project, consisting of a new campus for the university and a new headquarters for the utility.

Philadelphia Fed President Patrick T. Harker tours the operation at Philly Shipyard, Inc., one of five companies spotlighted in the Bank's Apprenticeship Guide.

Additionally, the Bank produced several special reports through the course of the year, including a comprehensive apprenticeship guide aimed at employers and workforce intermediaries throughout the region, which outlines the current state of apprenticeships, considers case studies from organizations like Philly Shipyard, Inc. and the Northeast Regional Council of Carpenters and offers paths to explore apprenticeship as a talent development strategy.

How the Bank Protects the Nation's Financial System

Jonathan Brown, Supervising Examiner, part of the team that supervises TD Bank, works every day to monitor safety and soundness for the largest bank holding company in the Third District.

When Philadelphia Fed community bank examiners head into the field, they're not just considering hard numbers on a balance sheet, financial statements, or loan figures; they're also weighing the intangibles — key additions like pieces of local context and regional characteristics.

For instance, around Souderton, PA, the home territory of one of our supervised institutions, examiners drive by farm trucks loaded with pigs destined for the local meat plant, a clear reminder of what drives the local economy.

"Not driving through the marketplace of the bank to me is a huge loss," said Mark Hall, supervising examiner. "Having that perspective really helps you understand what management's feeling is."

Examiners like Hall in the Philadelphia Fed's Supervision, Regulation, and Credit (SRC) Department supervise 21 state member banks to ensure those banks comply with governmental regulations and meet the needs of the communities in which they operate, helping maintain a robust, safe, and sound financial system. Philadelphia Fed supervision teams, like others across the other 11 Federal Reserve Districts, determine whether banks are offering consumers safe financial products and managing risks effectively.

Philadelphia Fed examiners use both onsite and offsite reviews to ensure those state member banks are in compliance; while the newer offsite review process offers flexibility and reduces the burden on both banks and examiners, the onsite process can feature more face-to-face

Meet the onsite team that supervises Synchrony Financial, located in Stamford, CT. Left to right, standing: Atul Dholakia, Examinations Specialist; Audra Grasetti, Senior Examinations Specialist; and Christie Vazquez, Senior Examinations Specialist. Left to right, seated: Melonie Sterling, Examiner, and Chung Cho, Supervising Examiner.

time with local bank officers. Regardless of the location, examiners emphasize open lines of communication to make sure they can assess a bank's strategy and ensure it is serving its community's best interests while remaining healthy, safe, and sound.

At the largest bank holding companies in the District, supervision teams maintain an onsite presence, focusing on those institutions' risk and control functions, and conduct evaluations under the Comprehensive Capital Analysis and Review (CCAR) program, a Federal Reserve System initiative that went into force in 2011 following the financial crisis.

For supervisory teams, CCAR reviews are a kind of stress test to measure what a large bank can endure in a severely adverse environment. Using quantitative and qualitative assessments, teams determine what those banks can withstand before cracks start to emerge, and what levels of capital a bank would need to absorb losses, meet obligations to creditors, and continue to issue credit — essentially to avoid a repeat of the financial crisis.

"CCAR is a direct result of that — an initiative to prevent something like that happening independently before it really happens," said Andrea Anastasio, supervising examiner.

Supervision teams also collaborate with regulatory agencies like the Office of the Comptroller of the Currency and others, which helps ensure banks' management are offering a consistent view on their operations, reduces the overall regulatory burden, and allows the agencies and the Bank to have a unified, consistent message.

Cathy Lovell, Examiner, is part of the team that supervises community banks and holding companies in the Third District.

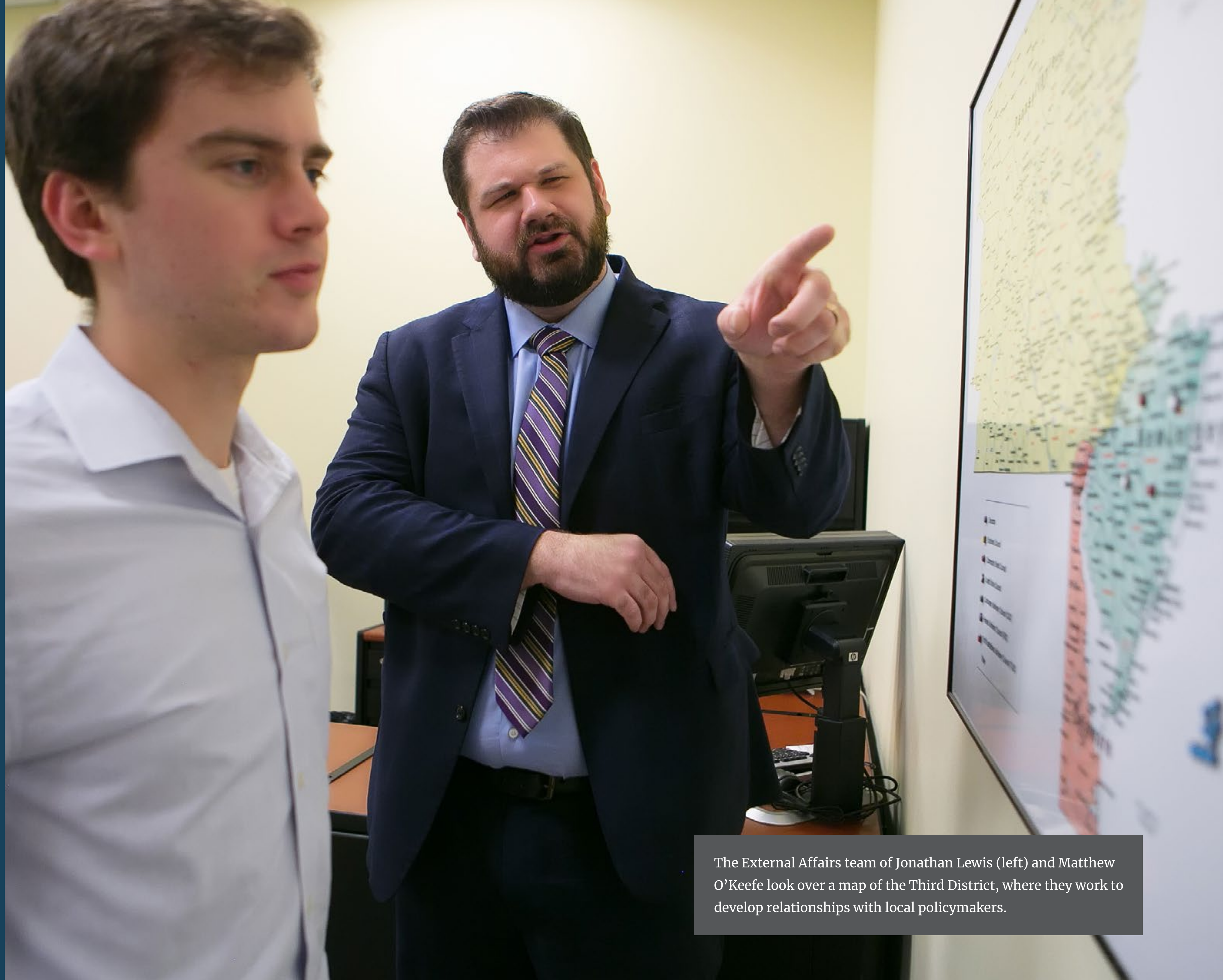
Also, following a number of high-profile data breaches around the nation in the past several years, the Philadelphia Fed's teams have stepped up efforts to protect consumers, focusing on cybersecurity to ensure banks are protecting consumer data and working to ensure similar breaches won't occur in the future.

The Philadelphia Fed continues its leadership role in the System on a pair of publications — *Community Banking Connections* and *Consumer Compliance Outlook*, focusing on safety and soundness and consumer compliance issues, respectively — that reach more than 30,000 community bankers, helping them understand and comply with applicable laws and regulations. Those publications are, in turn, part of the department's larger outreach effort, which focuses on sharing information, knowledge, and experience outside the examination environment in workshops, forums, and online training.

Philadelphia Fed supervision teams, like others across the other 11 Federal Reserve Districts, determine whether banks are offering consumers safe financial products and managing risks effectively.

Mark Hall, Supervising Examiner, highlights the value of having an onsite presence at the institution during community bank supervision.

The Bank Works to Engage Communities and Strengthen Partnerships



The External Affairs team of Jonathan Lewis (left) and Matthew O'Keefe look over a map of the Third District, where they work to develop relationships with local policymakers.

The Philadelphia Fed has long been a source of in-depth research, an advocate of community development work, and a supplier of regulations and policy for financial institutions. But a deep well of compelling knowledge matters little if the general public does not know about it. Advocacy and partnerships work best when the parties share mutual respect and commitment.

Reaching out to key stakeholders was another high-priority objective in 2017. The following stories detail how the Bank worked to build relationships with public policy stakeholders, financial institutions, and colleagues within the Federal Reserve System to safeguard the System's digital infrastructure and the nation's financial system.

External Affairs

The Federal Reserve System does not make or advocate for specific legislation or government policy. But given the Fed's goal to safeguard the economy and financial system, officials at the Philadelphia Fed and System-wide are interested in ensuring policymakers have all the information and data needed to arrive at sound policy that supports the Fed's dual mandate of promoting full employment and price stability.

The Bank's External Affairs unit of the Corporate Affairs Department was created to develop and maintain relationships with Third District policymakers and their staffs and to keep abreast of all policy developments. "Every day we're focused on legislative activities that may affect the Fed, and we monitor what's going on with the elected officials who represent the Third District on the federal, state, and local level," said Matthew O'Keefe, external affairs strategist.

In November 2017, Larry Santucci of the Bank's Consumer Finance Institute led a conference on aging and financial health, a topic that was highlighted to local officials by the External Affairs unit of Corporate Affairs.

O'Keefe and his colleague Jonathan Lewis, outreach analyst, learn as much as they can about each policymaker and staff before meeting them. "We know what our specific members are focused on, what their hot topics are," said Lewis. "We can then find Fed research related to those topics so that the policymakers have solid information when discussing legislation or regulations."

One example is the work done by Philadelphia Fed economists on cognitive impairment and financial health. When the Bank hosted a conference on aging and finances, O'Keefe made sure the staff of a local member of Congress who was interested in aging-related issues was aware of the conference and relayed to them various findings that came out of the conference.

O'Keefe and Lewis also work with the Bank's Financial Outreach team for information on state banking committees and concerns among regional financial institutions. "Cybersecurity is always an issue for many of our elected officials," said O'Keefe.

The External Affairs team also sends data and other reports to area legislative offices. The *Tri-State Trends* newsletter, distributed to Third District legislative staff eight times per year, details Bank research and events as well as economic data on the Third District states of Pennsylvania, New Jersey, and Delaware. Additionally, legislators are informed about the Bank's high-priority objectives. Lewis noted that when the Economic Growth & Mobility Project (EGMP) was rolled out in 2016, "We made sure to talk to our Congressional members who were on the Education and Workforce Committee about the research products that were coming out of EGMP."

One of the Bank's objectives is to produce compelling knowledge. O'Keefe and Lewis's task is to ensure this in-depth research is part of any discussion among policymakers. "Our goal," said O'Keefe, "is to ensure the Philadelphia Fed is viewed as the go-to source for information when our elected officials and various other stakeholders want to learn about important issues."

Financial Institution Relations

Overseeing the financial system is one of the Federal Reserve System's main missions. The geography of the Third District enables the Bank's Financial Institution Outreach group to travel across Pennsylvania, New Jersey, and Delaware to visit local banks, credit unions, and other institutions.

According to Bill Guinan, outreach specialist, going out and meeting executives is paramount. "To develop a solid relationship built on mutual respect, face-to-face meetings are critical," he said.

The face-to-face connections enable Guinan and his colleague Bond Kraemer, another Bank outreach specialist, to maintain relationships that create a two-way street of information sharing. "We design our meetings to gather information on the banking environment, on the regulatory environment, on a local economy, but also we're there to share some information on the strategic initiatives of the Federal Reserve Bank of Philadelphia," said Guinan.

Before each meeting, Guinan and Kraemer do their homework. "It's important to do research, to be current on publications and regulations so that we can answer any questions that come up," said Kraemer.

One unique facet of the Philadelphia Fed's outreach to financial institutions is the annual field meetings. These meetings are scheduled across eight cities in the Third District and bring together chief executives of local community banks with Fed senior leadership. "We also attend industry events and meetings," said Kraemer, in order to keep the conversation going throughout the year.

Another area of collaboration between the Bank and the financial sector is the Community Depository Institutions Advisory Council. This advisory council, established by the Board of Governors of the Federal Reserve System in Washington, D.C., allows financial executives to weigh in on issues related to banking and regulations. "We have 12 bankers who meet twice a year with President Harker and other senior leaders to discuss specific questions that are posed by the Board," said Kraemer. "These questions cover regulations, economic indicators, and the payments system."

Maintaining relationships with local financial institutions is the goal of the Financial Institution Relations group of (left to right) Outreach Specialists Bond Kraemer and Bill Guinan as well as Tony White, who retired in 2017.

The Philadelphia Fed has worked for decades to build these partnerships with community bankers and other financial sector executives. The relationships allow for the exchange of thoughtful questions, a store of mutual respect, and sharing of industry knowledge that help the Federal Reserve System keep the U.S. financial system robust and secure.

Information Technology and Collaboration Services

Relationship building is not solely an external-facing process. The Information Technology Services (ITS) department at the Philadelphia Fed maintains relationships within the Federal Reserve System to ensure effective internal collaboration and to ensure the Fed’s information technology infrastructure and the U.S. payments system remain secure from outside threats.

(Left to right) Joseph Dietzmann, Nancy Hunter, and Terry Harris are part of the Information Technology Services department that keeps the Fed’s IT infrastructure secure.

The bank’s Collaboration Services group has taken the lead in collaboration technology efforts with the other Reserve Banks and the Board of Governors. “Because of our decade-plus of experience and successful delivery of collaboration services, we were designated the provider for services concerning security and service delivery for the entire Fed System,” said Terry Harris, senior vice president and chief information officer.

The goal in building these System-wide relationships is not just to avoid duplicative work but to identify and exploit best practices. “Previously, IT personnel in 10 different locations were doing their own planning, building, and running in their own particular collaboration service space,” explained Joseph Dietzmann, vice president and End User Services collaborative services executive. Philadelphia Fed management either led or participated in the streamlining of those efforts so that the planning, building, and operations teams work together.

The new arrangement allows for more efficient service delivery and greater system security. “Because the Philadelphia Fed is the lead collaboration services provider, we are responsible at the end of the day for the most effective delivery and utilization of the different IT products,” said Dietzmann.

In 2017, the Philadelphia Fed took the lead on a wide array of efforts that included safeguarding the Fed System’s e-mail by instituting a new classification protocol. The Bank also developed partnerships across the System to keep sensitive data safe from hacking. That is important because the Fed handles millions of pieces of data from employees, other regulators, and financial institutions that use the Fed’s many payment systems. “Here at the Fed we’re protecting confidential supervisory information, we’re protecting sensitive, personally identifiable information, and we’re protecting monetary policy deliberations,” said Harris. “We also manage very important transactional capabilities in the economy like the ACH system, Fedwire Funds Transfers. These are some of the crown jewels of the payments systems that run our economy.”

> “We’re protecting sensitive, personally identifiable information, and we’re protecting monetary policy deliberations.”
>
> - Terry Harris, Senior Vice President and Chief Information Officer

“We are always a target,” said Nancy Hunter, special information security advisor. Indeed, cyberattacks on the Federal Reserve System number in the hundreds of thousands a day. The ITS department fights a constant battle to keep the Fed and the financial system safe and working.

The Bank doesn’t just protect information for the Federal Reserve. It also shares its knowledge of the latest in cybersecurity best practices with financial institutions in the Third District, which covers Delaware, southern New Jersey, and central and eastern Pennsylvania. These relationships help institutions better protect data and provide safe financial products to businesses and people.

“We engage very actively with the financial institutions in our District to give them our perspective on information security,” said Harris. Keith Morales, vice president of information security and data privacy officer, attended field meetings with member community bankers in the District. The Bank also holds a conference for financial institution information security officers from member and nonmember banks during which Fed experts discuss new trends in cybersecurity.

The Bank’s experts are well placed to know the latest risks and how best to protect information because Harris and his team keep in constant contact with the nation’s security agencies, including Homeland Security and the CIA, NSA, and FBI, to develop approaches to reducing insider risk and better understand and react to intelligence information in advance.

“We’re able to bring in those agencies to discuss the threats on the financial industry, and we’re able to share best practices and share incident information so that everyone can benefit in learning about what went wrong and what went right,” said Hunter. “And that has been very favorably received, both at the field meetings and in the conference we host each year.”

How the Bank Encourages Leadership from Every Chair

The Philadelphia Fed's leadership philosophy may start in the office, but the impact of our work extends far and wide into the community. Members of PhillyFedCARES frequently volunteer at Philadelphia's McCall School.

No matter where you are sitting — whether in the executive suite or in a cubicle — making a sound business decision is a critical function in every business line. It is also a philosophy that resonates at the Philadelphia Fed. The Bank extols the importance of inclusive leadership from every seat in the organization, which helps employees bridge all the solid and dotted lines on the organizational chart.

"The Bank's leadership development programs are inclusive," said Mary Ann Hood, senior vice president, Human Resources. "Whether you're an officer or someone who is just starting out in an entry-level job, this comprehensive plan creates opportunities for everyone in the Bank to achieve their best."

We strive to be a strong, performing organization known for developing its leaders, said Hood. "Our employees are our greatest assets, making significant contributions to this Bank and to the Federal Reserve System. We want to be sure we continue to give our employees development opportunities to help them succeed."

To adapt the organization into an evolving 21st century business framework, the Bank customized this leadership philosophy to its mission and adopted it as a strategic initiative, said Steve Hart, vice president, Human Resources. "For us, seeing the value in leadership at all levels of the organization is the key," said Hart.

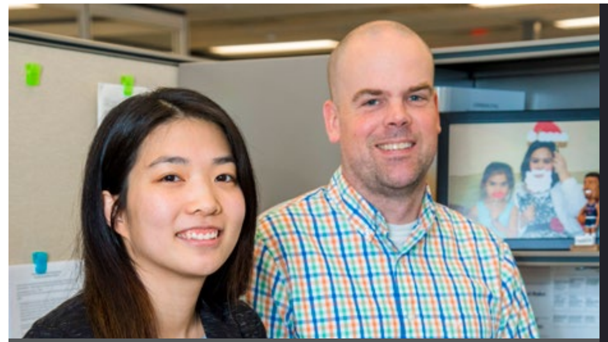
Support of this initiative came from members of the Philadelphia Fed's Management Committee.

Ron Lavish, Audit Manager, has been honored for his work on many System initiatives, especially winning the Conference of General Auditors Award for Excellence in 2017.

"By providing strong leadership in the Federal Reserve System's core functions and in all areas that support those functions, we aspire as an organization to share our subject matter expertise, thought leadership, and ability to collaborate within the Bank and in the System," said Hood. She acknowledges that the Bank has a strong foundation of System leadership in several key areas of central bank expertise: economic research, community development, and supervision and regulation. "We want to communicate the value and the impact our work has on our community and the System," she said.

Although professional development for employees has always been part of the Bank's DNA, what is driving this initiative today? Hood sees it as a combination of factors. "Our strategic priorities include an external view of how the Bank should serve the community in a positive way and contribute to economic policy and supervision at the System level," she said. "In doing so, we need to put even more focus on developing leaders and being a contributor not only in Philadelphia but in the community and the System as a whole." The keys are being leaders in our space and being the best at what we do, she said.

This cultural shift in the workplace recognizes the speed at which change is happening not only in the Bank but in the System, in technology, and in the world in general, said Hood. She points to new opportunities at the Bank for employee growth and development. For starters, the Leaders Academy (in-house management training for the next generation of leaders) is being revamped, there is a new college recruiting program, and more rotational opportunities are being offered across the Bank to promote collaboration. These new opportunities join the Bank's staples of Grow the Home Team assignments and management training programs for employees, such as the System Leadership Initiative, the Urban League, and Leadership Philadelphia. Human Resources will lead the charge, but it won't be the only channel for employee growth and development. Opportunities are available at every Bank level and in every department.



During one of their Federal Reserve System projects, Jessica Zhou and Timothy McCollum, Accounting Analysts in Financial Management Services, provided onsite reviews for the Reserve Bank Operations and Payment Systems at the Federal Reserve Bank of Minneapolis.

In years past, Bank employees Jessica Zhou, Timothy McCollum, and Ron Lavish have extended their expertise to the System via a variety of special projects. Zhou and McCollum, accounting analysts in Financial Management Services, were part of a seven-member team that provided onsite reviews for the Reserve Bank Operations and Payment Systems at the Federal Reserve Bank of Minneapolis. Following the Board of Governors of the Federal Reserve System's lead, they reviewed discretionary expenditures, operational perspectives, and financial accounting operations. In the process, the collaboration was invaluable, they said, in networking with System colleagues and comparing procedures at other Reserve Banks.

"Making good decisions is a crucial skill at every level."

– Peter Drucker, management consultant, corporate philosopher, and author

Likewise, Ron Lavish, Audit manager, has been assisting in System audits and participating in data management reviews and information technology governance for most of his 34 years at the Bank. His System work was recognized in 2017 when he won the Conference of General Auditors Award for Excellence. He was one of only two Fed employees selected from a team of more than 300 auditors. Lavish has "gone above and beyond the call of duty while continuing to be viewed as a valued advisor throughout the Bank and the System," according to Michelle Scipione, vice president and general auditor. She sees the award as not only acknowledging Lavish's many contributions, but as a tribute to the Audit Department and the Bank as well.

For Mary Ann Hood, Senior Vice President of Human Resources, and Karen Vaughn, Associate Director in the Office of Diversity & Inclusion in Human Resources, inclusive development gives everyone an opportunity to achieve their best.

For First Vice President James Narron, good ideas and good decisions come from all corners of the organization. He looks to employees who "can take a leadership role from any chair in the Bank."

Sitting, from left: Phoebe A. Haddon, Edward J. Graham, Michael J. Angelakis, Jon Evans; standing, from left: Brian M. McNeill, William S. Aichele, David R. Hunsicker, Patricia A. Hasson. Not pictured: Carol J. Johnson.

Board of Directors

As provided by the Federal Reserve Act, each of the 12 Reserve Banks is supervised by a nine-member board of directors. The directors oversee the Bank's direction and performance, and they participate in the formulation of the Fed's monetary policy through their reports on economic and financial conditions and their decisions on the Bank's discount rate.

CHAIRMAN

Michael J. Angelakis (a, d)
Chairman and CEO
Atairos Management, L.P.
Bryn Mawr, PA

Senior Advisor to the Executive
Management Committee
Comcast Corporation, Philadelphia, PA

DEPUTY CHAIRMAN

Brian M. McNeill (a, c, d)
President and CEO
TouchPoint, Inc.
Concordville, PA

BOARD MEMBERS

William S. Aichele (a, c)
Chairman
Univest Corporation of Pennsylvania
Souderton, PA

Jon Evans (a, b)
President and CEO
Atlantic Community Bankers Bank
Camp Hill, PA

Edward J. Graham (a, b, d)
Former Chairman and CEO
South Jersey Industries
Folsom, NJ

Phoebe A. Haddon (a, b)
Chancellor
Rutgers University–Camden
Camden, NJ

Patricia A. Hasson (a, c)
President and Executive Director
Clarifi
Philadelphia, PA

David R. Hunsicker (a, b, d)
Chairman, President, and CEO
New Tripoli Bank
New Tripoli, PA

Carol J. Johnson (a, c)
Former President and COO
AlliedBarton Security Services
Conshohocken, PA

(a) Member of the Bank's Executive Committee; (b) Member of the Bank's Audit Committee; (c) Member of the Bank's Management and Budget Committee; (d) Member of the Bank's Nominating and Governance Committee

Sitting, from left: Matthew P. Prosseda, Patrick L. Ryan, Christopher D. Maher, James Wang, David J. Hanrahan; standing, from left: William Wood, Rory Ritrievi, Amey R. Sgrignoli. Not pictured: Mark E. Huntley, J. Bradley Scovill, Jeane M. Vidoni, Richard Stipa.

Community Depository Institutions Advisory Council

The Community Depository Institutions Advisory Council, created in 2011, includes representatives from commercial banks, thrift institutions, and credit unions. The council provides information, advice, and recommendations to the Federal Reserve Bank of Philadelphia from the perspective of community depository institutions.

David J. Hanrahan
President and CEO
Capital Bank of New Jersey
Vineland, NJ

Mark E. Huntley
President and CEO
Artisans' Bank
Wilmington, DE

Christopher D. Maher
Chairman, President, and CEO
OceanFirst Bank
Toms River, NJ

Matthew P. Prosseda
President and CEO
First Keystone Community Bank
Berwick, PA

Rory Ritrievi
President and CEO
Mid Penn Bancorp, Inc. and Mid Penn Bank
Millersburg, PA

Patrick L. Ryan
President and CEO
First Bank
Hamilton, NJ

J. Bradley Scovill
President and CEO
Citizens & Northern Bank
Wellsboro, PA

Amey R. Sgrignoli
President and CEO
Belco Community Credit Union
Harrisburg, PA

Richard Stipa
CEO
TruMark Financial Credit Union
Fort Washington, PA

Jeane M. Vidoni
President and CEO
Penn Community Bank
Bristol, PA

James Wang
President and CEO
Asian Bank
Philadelphia, PA

William Wood
Chairman
CBT Financial Corporation
Chairman CBT Bank
Clearfield, PA

Economic and Community Advisory Council

The Economic Advisory Council, created in 2008, was expanded and renamed the Economic and Community Advisory Council in 2016. It is now composed of up to 15 leaders who represent businesses of different sizes and industry sectors as well as nonprofit and philanthropic organizations, academic institutions, the public sector, and organized labor. The council advises Federal Reserve officials on emerging trends, market conditions, and economic growth opportunities in the Third District and the nation.

Madeline Bell
President and CEO
The Children's Hospital of Philadelphia
Philadelphia, PA

Staci Berger
President and CEO
Housing and Community Development Network of New Jersey
Trenton, NJ

Daniel Betancourt
President and CEO
Community First Fund
Lancaster, PA

Edward L. Dandridge
Chief Marketing and Communications Officer
Marsh & McLennan Companies
New York, NY

Patrick J. Eiding
President
Philadelphia Council AFL-CIO
Philadelphia, PA

John A. Fry
President
Drexel University
Philadelphia, PA

Chris Gheysens
President and CEO
Wawa, Inc.
Wawa, PA

Terry Kelly
President and CEO
W. L. Gore & Associates, Inc.
Newark, DE

Sharmain Matlock-Turner
President and CEO
Urban Affairs Coalition
Philadelphia, PA

Michael A. Nutter
David N. Dinkins Professor of Professional Practice of Urban and Public Policy
Columbia University
Former Mayor of the City of Philadelphia
Philadelphia, PA

Devesh Raj
Senior Vice President of Strategic and Financial Planning
Comcast Corporation
Philadelphia, PA

Maria Rodale
Chairman and CEO
Rodale Inc.
Emmaus, PA

Donald F. Schwarz
Vice President, Program
Robert Wood Johnson Foundation
Princeton, NJ

Linda Thomson
President and CEO
JARI
Johnstown, PA

Management Committee

The Management Committee is composed of the Bank's President and CEO, the first vice president and COO, the chief of staff, and senior vice presidents. Members advise the president and first vice president on matters of Bank policy and strategy.

Patrick T. Harker
President and Chief Executive Officer

James D. Narron
First Vice President and Chief Operating Officer

Michael Dotsey
Executive Vice President, Director of Research, and Director of the Consumer Finance Institute

Donna L. Franco
Senior Vice President and Chief Financial Officer

Terry E. Harris
Senior Vice President and Chief Information Officer, Information Technology Services

Deborah L. Hayes
Senior Vice President, Corporate Affairs

Mary Ann Hood
Senior Vice President and EEO Officer, Human Resources; Director, Office of Diversity and Inclusion

Arun K. Jain
Senior Vice President, Treasury and Financial Services

Jeanne R. Rentezelas
Senior Vice President and General Counsel, Legal

William G. Spaniel
Senior Vice President and Lending Officer, Supervision, Regulation, and Credit

Patricia Wilson
Senior Vice President, Chief of Staff, and Corporate Secretary

Additional Bank Officers

SENIOR VICE PRESIDENTS

Robert Hunt
Senior Vice President and Associate Director
Consumer Finance Institute

Keith Sill
Senior Vice President and Director
Real-Time Data Research Center
Research

Theresa Y. Singleton
Senior Vice President and Community Affairs Officer
Community Development and Regional Outreach

VICE PRESIDENTS

John D. Ackley Sr.
Vice President
Cash Services

Roc Armenter
Vice President and Economist
Research

Mitchell S. Berlin
Vice President and Economist
Research

Donna L. Brenner
Vice President
Enterprise Risk Management

Paul S. Calem
Vice President
Supervision, Regulation, and Credit

Jennifer E. Cardy
Vice President
Financial Management Services

Satyajit Chatterjee
Vice President and Economist
Research

Kori Ann Connelly
Vice President and Deputy General Counsel
Legal

Larry Cordell
Vice President
Supervision, Regulation, and Credit

Joseph O. Dietzmann
Vice President and Collaborations Services Executive
End Users Services

Michael T. Doyle
Vice President
Treasury Payments

Gregory Fanelli
Vice President
Information Technology Services

Stephen G. Hart
Vice President
Human Resources

Charles Kirkland
Vice President
Financial Statistics

Deming Love
Vice President
Digital Strategy

Keith Morales
Vice President and Information Security Officer
Information Technology Services

Robert F. Mucerino
Vice President
Treasury Services

Robin P. Myers
Vice President
Supervision, Regulation, and Credit

Leonard Nakamura
Vice President and Economist
Research

Gregory A. Ramick
Vice President
Cash Services

Michelle S. Reardon
Vice President
Public Affairs

Perry Santacecilia
Vice President
Supervision, Regulation, and Credit

Michelle Scipione
Vice President and General Auditor
Audit

Stanley J. Sienkiewicz
Vice President
Research Support
Research

Kimberly J. Taylor
Vice President
Human Resources

Patrick F. Turner
Vice President and Managing Officer
End User Services

Linda Van Valkenburg
Vice President
Information Technology Services

James K. Welch
Vice President
Law Enforcement and Facilities Management

William T. Wisser
Vice President
Supervision, Regulation, and Credit

ASSISTANT VICE PRESIDENTS

Joanne M. Branigan
Assistant Vice President
Supervision, Regulation, and Credit

Brian W. Calderwood
Assistant Vice President
Groupware Leadership Center

Julia Cheney
Assistant Vice President and Assistant Director
Consumer Finance Institute

Maryann T. Connelly
Assistant Vice President and Counsel
Legal

Michael T. Costello
Assistant Vice President
Supervision, Regulation, and Credit

Heather C. Derbyshire
Assistant Vice President
Financial Statistics

Suzanne W. Furr
Assistant Vice President and General Auditor
Audit

Christopher C. Henderson
Assistant Vice President
Supervision, Regulation, and Credit

Jill Hettinger
Assistant Vice President
Supervision, Regulation, and Credit

Christopher L. Ivanoski
Assistant Vice President
Facilities

John P. Kelly
Assistant Vice President
Financial Management Services

Anjanette Kichline
Assistant Vice President
Supervision, Regulation, and Credit

Andrew A. Kish
Assistant Vice President
Supervision, Regulation, and Credit

James K. Lofton
Assistant Vice President
Cash Services

John J. Munera III
Assistant Vice President
Supervision, Regulation, and Credit

Wanda Preston
Assistant Vice President
Supervision, Regulation, and Credit

Chellappan Ramasamy
Assistant Vice President
Supervision, Regulation, and Credit

Anthony T. Scafide Jr.
Assistant Vice President
Financial Institutions Relations

Stephen J. Smith
Assistant Vice President and Counsel
Legal

H. Robert Tillman
Assistant Vice President
Supervision, Regulation, and Credit

Gail L. Todd
Assistant Vice President and Credit Officer
Supervision, Regulation, and Credit

OFFICERS

Kimberly Caruso
Officer
Collateral Data Administration Support Group

Kenneth Chin
Officer
Cash Services

James W. Corkery Jr.
Officer
Supervision, Regulation, and Credit

Daniel W. Crouthamel
Research Information Technology Support
Officer
Research

Jeff Fries
Officer
End Users Services

Yilin Huang
Officer
Supervision, Regulation, and Credit

Erin Mierzwa
Officer
Community Development and Regional
Outreach

Michael O'Brien
Officer
Law Enforcement

Tom Stark
Officer
Research

Includes promotions through January 2018.

Statement of Auditor Independence

The Federal Reserve Board engaged KPMG to audit the 2017 combined and individual financial statements of the Reserve Banks.[1]

In 2017, KPMG also conducted audits of internal controls over financial reporting for each of the Reserve Banks. Fees for KPMG services totaled $6.8 million. To ensure auditor independence, the Board of Governors requires that KPMG be independent in all matters relating to the audits. Specifically, KPMG may not perform services for the Reserve Banks or others that would place it in a position of auditing its own work, making management decisions on behalf of the Reserve Banks, or in any other way impairing its audit independence. In 2017, the Bank did not engage KPMG for any non-audit services.

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1 In addition, KPMG audited the Office of Employee Benefits of the Federal Reserve System (OEB), the Retirement Plan for Employees of the Federal Reserve System (System Plan), and the Thrift Plan for Employees of the Federal Reserve System (Thrift Plan). The System Plan and the Thrift Plan provide retirement benefits to employees of the Board, the Federal Reserve Banks, the OEB, and the Consumer Financial Protection Bureau.

2017 Financial Statement Contents

Management's Report on Internal Control over Financial Reporting

FEDERAL RESERVE BANK
OF PHILADELPHIA

March 8, 2018

To the Board of Directors

The management of the Federal Reserve Bank of Philadelphia (Bank) is responsible for the preparation and fair presentation of the Statements of Condition as of December 31, 2017 and 2016, and the Statements of Operations, and Statements of Changes in Capital for the years then ended (the financial statements). The financial statements have been prepared in conformity with the accounting principles, policies, and practices established by the Board of Governors of the Federal Reserve System as set forth in the *Financial Accounting Manual for Federal Reserve Banks* (FAM), and, as such, include some amounts that are based on management judgments and estimates. To our knowledge, the financial statements are, in all material respects, fairly presented in conformity with the accounting principles, policies and practices documented in the FAM and include all disclosures necessary for such fair presentation.

The management of the Bank is responsible for establishing and maintaining effective internal control over financial reporting as it relates to the financial statements. The Bank's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with the FAM. The Bank's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the Bank's assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with FAM, and that the Bank's receipts and expenditures are being made only in accordance with authorizations of its management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Bank's assets that could have a material effect on its financial statements.

Even effective internal control, no matter how well designed, has inherent limitations, including the possibility of human error, and 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 controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The management of the Bank assessed its internal control over financial reporting based upon the criteria established in the *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, we believe that the Bank maintained effective internal control over financial reporting.

Patrick T. Harker
President and Chief Executive Officer

James D. Narron
First Vice President and Chief Operating Officer

Donna L. Franco
Senior Vice President and Chief Financial Officer

KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report

To the Board of Governors of the Federal Reserve System
and the Board of Directors of the Federal Reserve Bank of Philadelphia:

We have audited the accompanying statements of condition of the Federal Reserve Bank of Philadelphia ("FRB Philadelphia") as of December 31, 2017 and 2016, and the related statements of operations and changes in capital for the years then ended. We also have audited the FRB Philadelphia's internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The FRB Philadelphia's management is responsible for these financial statements, 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 Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the FRB Philadelphia's internal control over financial reporting based on our audits.

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

The FRB Philadelphia's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the accounting principles established by the Board of Governors of the Federal Reserve System (the "Board") as described in Note 3 of the financial statements and as set forth in the *Financial Accounting Manual for Federal Reserve Banks* ("FAM"). The FRB Philadelphia'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 FRB Philadelphia; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with the FAM, and that receipts and expenditures of the FRB Philadelphia are being made only in accordance with authorizations of management and directors of the FRB Philadelphia; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the FRB Philadelphia's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As described in Note 3 to the financial statements, the FRB Philadelphia has prepared these financial statements in conformity with the accounting principles established by the Board, as set forth in the FAM, which is a basis of accounting other than U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the FRB Philadelphia as of December 31, 2017 and 2016, and the results of its operations for the years then ended, on the basis of accounting described in Note 3. Also, in our opinion, the FRB Philadelphia maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

KPMG LLP

Philadelphia, Pennsylvania
March 8, 2018

Abbreviations

ACH	Automated clearinghouse
ASC	Accounting Standards Codification
ASU	Accounting Standards Update
BEP	Benefit Equalization Retirement Plan
Budget Act	Bipartisan Budget Act of 2018
Bureau	Bureau of Consumer Financial Protection
FAM	*Financial Accounting Manual for Federal Reserve Banks*
FASB	Financial Accounting Standards Board
FOMC	Federal Open Market Committee
FRBNY	Federal Reserve Bank of New York
GAAP	Accounting principles generally accepted in the United States of America
GSE	Government-sponsored enterprise
IMF	International Monetary Fund
MAPD	Medicare Advantage and Prescription Drug
MBS	Mortgage-backed securities
OEB	Office of Employee Benefits of the Federal Reserve System
SDR	Special drawing rights
SERP	Supplemental Retirement Plan for Select Officers of the Federal Reserve Banks
SOMA	System Open Market Account
TBA	To be announced
TDF	Term Deposit Facility

Statements of Condition | As of December 31, 2017 and December 31, 2016 (in millions)

		2017	2016
ASSETS			
Gold certificates		$ 348	$ 359
Special drawing rights certificates		210	210
Coin		187	159
System Open Market Account:	Note 5		
Treasury securities, net (of which $724 and $684 is lent as of December 31, 2017 and 2016, respectively)		65,730	69,711
Government-sponsored enterprise debt securities, net (of which $0 and $1 is lent as of December 31, 2017 and 2016, respectively)		123	452
Federal agency and government-sponsored enterprise mortgage-backed securities, net		46,932	48,738
Foreign currency denominated investments, net		1,146	1,070
Central bank liquidity swaps		649	306
Accrued interest receivable		641	697
Bank premises and equipment, net	Note 6	85	85
Interdistrict settlement account		5,003	-
Other assets		17	31
Total assets		$ 121,071	$ 121,818
LIABILITIES AND CAPITAL			
Federal Reserve notes outstanding, net		$ 47,730	$ 45,544
System Open Market Account:	Note 5		
Securities sold under agreements to repurchase		14,561	19,691
Other liabilities		14	27
Deposits:			
Depository institutions		56,228	52,334
Other deposits		2	2
Interest payable to depository institutions and others		25	11
Accrued benefit costs	Notes 8 and 9	123	121
Accrued remittances to the Treasury		21	75
Interdistrict settlement account		-	1,824
Other liabilities		16	14
Total liabilities		118,720	119,643
Capital paid-in		1,783	1,637
Surplus (including accumulated other comprehensive loss of $11 and $14 at December 31, 2017 and 2016, respectively)		568	538
Total capital		2,351	2,175
Total liabilities and capital		$ 121,071	$ 121,818

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

Statements of Operations | For the years ended December 31, 2017 and December 31, 2016 (in millions)

		2017	2016
INTEREST INCOME			
System Open Market Account:	Note 5		
Treasury securities, net		$ 1,684	$ 1,694
Government-sponsored enterprise debt securities, net		11	25
Federal agency and government-sponsored enterprise mortgage-backed securities, net		1,283	1,223
Foreign currency denominated investments, net		(1)	-
Central bank liquidity swaps		1	-
Total interest income		2,978	2,942
INTEREST EXPENSE			
System Open Market Account:	Note 5		
Securities sold under agreements to repurchase		88	30
Deposits:			
Depository institutions and others		613	314
Term Deposit Facility		3	6
Total interest expense		704	350
Net interest income		2,274	2,592
NON-INTEREST INCOME (LOSS)			
System Open Market Account:	Note 5		
Treasury securities gains, net		1	-
Federal agency and government-sponsored enterprise mortgage-backed securities gains, net		-	1
Foreign currency translation gains (losses), net		103	(5)
Other		1	1
Compensation received for service costs provided		-	2
Reimbursable services to government agencies		16	24
Other		4	3
Total non-interest income		125	26
OPERATING EXPENSES			
Salaries and benefits		136	127
Occupancy		16	15
Equipment		5	5
Other		31	46
Assessments:			
Board of Governors operating expenses and currency costs		72	69
Bureau of Consumer Financial Protection		31	33
Total operating expenses		291	295
Net income before providing for remittances to the Treasury		2,108	2,323
Earnings remittances to the Treasury	Note 3m	2,038	2,300
Net income after providing for remittances to the Treasury		70	23
Change in prior service costs related to benefit plans	Note 9	4	2
Change in actuarial losses related to benefit plans	Note 9	(1)	-
Total other comprehensive income		3	2
Comprehensive income		$ 73	$ 25

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

Statements of Changes in Capital | For the years ended December 31, 2017 and December 31, 2016 (in millions, except share data)

	Capital paid-in	Surplus: Net income retained	Surplus: Accumulated other comprehensive income (loss)	Surplus: Total surplus	Total capital
Balance at December 31, 2015 (32,472,211 shares)	$ 1,624	$ 566	$ (16)	$ 550	$ 2,174
Net change in capital stock issued (263,257 shares)	13	-	-	-	13
Comprehensive income:					
Net income	-	23	-	23	23
Other comprehensive income	-	-	2	2	2
Dividends on capital stock	-	(37)	-	(37)	(37)
Net change in capital	13	(14)	2	(12)	1
Balance at December 31, 2016 (32,735,468 shares)	$ 1,637	$ 552	$ (14)	$ 538	$ 2,175
Net change in capital stock issued (2,922,570 shares)	146	-	-	-	146
Comprehensive income:					
Net income	-	70	-	70	70
Other comprehensive income	-	-	3	3	3
Dividends on capital stock	-	(43)	-	(43)	(43)
Net change in capital	146	27	3	30	176
Balance at December 31, 2017 (35,658,038 shares)	$ 1,783	$ 579	$ (11)	$ 568	$ 2,351

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

(1) STRUCTURE

The Federal Reserve Bank of Philadelphia (Bank) is part of the Federal Reserve System (System) and is one of the 12 Federal Reserve Banks (Reserve Banks) 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. The Bank serves the Third Federal Reserve District, which includes Delaware and portions of New Jersey and Pennsylvania.

In accordance with the Federal Reserve Act, supervision and control of the 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 nationally-chartered 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 director 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 payment system, including 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 participants in programs or facilities with broad-based eligibility 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, savings and loan holding companies, U.S. offices of foreign banking organizations, edge and agreement corporations, and certain financial market utilities that have been designated as systemically important. Certain services are provided to foreign official and international account holders, primarily by the FRBNY.

The FOMC, in conducting monetary policy, establishes policy regarding domestic open market operations and oversees these operations. The FOMC has selected the FRBNY to execute open market transactions for the System Open Market Account (SOMA) as provided in its annual authorization. The FOMC authorizes and directs the FRBNY to conduct operations in domestic markets, including the direct purchase and sale of Treasury securities, government-sponsored enterprise (GSE) debt securities, and 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 holds the resulting securities and agreements in a portfolio known as the SOMA. The FRBNY is authorized and directed to lend the Treasury securities and GSE debt securities that are held in the SOMA.

To be prepared to meet the needs specified by the FOMC to carry out the System's central bank responsibilities, the FOMC authorized and directed the FRBNY to execute standalone spot and forward foreign exchange transactions in the resultant foreign currencies, to hold balances in those currencies, and to invest such foreign currency holdings, while maintaining adequate liquidity. The FRBNY holds these securities and agreements in the SOMA. The FOMC also authorized and directed the FRBNY to maintain reciprocal currency arrangements with the Bank of Canada and the Bank of Mexico in the maximum amounts of $2 billion and $3 billion, respectively, and at the request of the Treasury to conduct swap transactions with the United States Exchange Stabilization Fund in the maximum amount of $5 billion, also known as warehousing.

Because of the global character of bank funding markets, the System has, at times, coordinated with other central banks to provide liquidity. The FOMC authorized and directed the FRBNY to maintain standing U.S. dollar liquidity swap arrangements and standing foreign currency liquidity swap arrangements with the Bank of Canada, the Bank of England, the Bank of Japan, the European Central Bank, and the Swiss National Bank. The FRBNY holds amounts outstanding under these liquidity swap lines in the SOMA. These liquidity swap lines, which were originally established as temporary arrangements, were converted to standing arrangements on October 31, 2013, and are subject to annual review and approval by the FOMC.

The FOMC has authorized and directed the FRBNY to conduct small-value exercises periodically for the purpose of testing operational readiness.

Although the Reserve Banks are separate legal entities, they collaborate on 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 among 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. Major services provided by the Bank on behalf of the System for which the costs were not reimbursed by the other Reserve Banks include Collateral Management System; Risk Assessment, Data Analysis, and Research; and Supervision Team Site Support Office.

(3) SIGNIFICANT ACCOUNTING POLICIES

Accounting principles for entities with the unique powers and responsibilities of the nation's central bank have not been formulated by accounting standard-setting bodies. The Board of Governors has developed specialized accounting principles and practices that it considers to be appropriate for the nature and function of a central bank. These accounting principles and practices are documented in the *Financial Accounting Manual for Federal Reserve Banks* (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. The financial statements and associated disclosures have been prepared in accordance with the FAM.

Due to the unique nature of the Bank's powers and responsibilities as part of the nation's central bank and given the System's unique responsibility to conduct monetary policy, the Board has adopted accounting principles and practices in the FAM that differ from accounting principles generally accepted in the United States of America (GAAP). The more significant differences are the presentation of all SOMA securities holdings at amortized cost, adjusted for credit impairment, if any, and the recording of all SOMA securities on a settlement-date basis. Amortized cost, rather than the fair value presentation, more appropriately reflects the financial position associated with the Bank's securities holdings given the System's unique responsibility to conduct monetary policy. Although the application of fair value measurements to the securities holdings may result in values substantially greater or less than 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 ability of the Reserve Banks, as the central bank, to meet their financial obligations and responsibilities. Both the domestic and foreign components of the SOMA portfolio may involve transactions that result in gains or losses when holdings are sold before maturity. Decisions regarding securities and foreign currency transactions, including their purchase and sale, are primarily motivated by monetary policy and financial stability objectives rather than profit. Accordingly, fair values, earnings, and gains or losses resulting from the sale of such securities and currencies are incidental to open market operations and do not motivate decisions related to policy or open market activities. Accounting for these securities on a settlement-date basis, rather than the trade-date basis required by GAAP, better reflects the timing of the transaction's effect on the quantity of reserves in the banking system.

In addition, the Bank does not present a Statement of Cash Flows as required by GAAP because the liquidity and cash position of the Bank are not a primary concern given the Reserve Bank's unique powers and responsibilities as a central bank. Other information regarding the Bank's activities is provided in, or may be derived from, the Statements of Condition, Operations, and Changes in Capital, and the accompanying notes to the financial statements. Other than those described above, the accounting policies described in FAM are generally consistent with those in GAAP and the references to GAAP in the notes to the financial statements highlight those areas where FAM is consistent with GAAP.

Preparing the 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.

Significant accounts and accounting policies are explained below.

a. Consolidation

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) established the Bureau of Consumer Financial Protection (Bureau) as an independent bureau within the System that has supervisory authority over some institutions previously supervised by the Reserve Banks in connection with those institutions' compliance with consumer protection statutes. Section 1017 of the Dodd-Frank Act provides that the financial statements of the Bureau are not to be consolidated with those of the Board of Governors or the System. The Board of Governors funds the Bureau through assessments on the Reserve Banks as required by the Dodd-Frank Act. The Reserve Banks reviewed the law and evaluated the design of and their relationship to the Bureau and determined that it should not be consolidated in the Bank's financial statements.

b. Gold and Special Drawing Rights Certificates

The Secretary of the Treasury is authorized to issue gold certificates to the Reserve Banks. Upon authorization, the Reserve Banks acquire gold certificates by crediting equivalent amounts in dollars to the account established for the Treasury. The gold certificates held by the Reserve Banks are required to be backed by the gold owned by 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. Gold certificates are recorded by the Reserve Banks at original cost. The Board of Governors allocates the gold certificates among the Reserve Banks once a year based on each Reserve Bank's average Federal Reserve notes outstanding during the preceding 12 months.

Special drawing rights (SDR) are issued by the International Monetary Fund (IMF) to its members in proportion to each member's quota in the IMF at the time of issuance. SDRs serve as a supplement to international monetary reserves and may be transferred from one national monetary authority to another. Under the law providing for U.S. participation in the SDR system, the Secretary of the Treasury is authorized to issue SDR certificates 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 certificate transactions occur, the Board of Governors allocates the SDR certificates among the Reserve Banks based upon each Reserve Bank's Federal Reserve notes outstanding at the end of the preceding calendar year. SDR certificates are recorded by the Reserve Banks at original cost.

c. Coin

The amount reported as coin in the Statements of Condition represents the face value of all United States coin held by the Bank. The Bank buys coin at face value from the U.S. Mint in order to fill depository institution orders.

d. Loans

Loans to depository institutions are reported at their outstanding principal balances and interest income is recognized on an accrual basis.

Loans are impaired when current information and events indicate that it is probable that the Bank will not receive the principal and interest that are due in accordance with the contractual terms of the loan agreement. Impaired loans are evaluated to determine whether an allowance for loan loss is required. The Bank has developed procedures for assessing the adequacy of any allowance for loan losses using all available information to identify incurred losses. 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. Generally, the Bank would discontinue recognizing interest income on impaired loans until the borrower's repayment performance demonstrates principal and interest would be received in accordance with the terms of the loan agreement. If the 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.

e. Securities Purchased Under Agreements to Resell, Securities Sold Under Agreements to Repurchase, and Securities Lending

The FRBNY may engage in purchases of securities under agreements to resell (repurchase agreements) with primary dealers. Transactions under these repurchase agreements are typically settled through a tri-party arrangement. In the United States, there are currently two commercial custodial banks that provide these services. In a tri-party arrangement, a commercial custodial bank manages the collateral clearing, settlement, pricing, and pledging, and provides cash and securities custodial services for and on behalf of the FRBNY and counterparty. The collateral pledged must exceed the principal amount of the transaction by a margin determined by the FRBNY for each class and maturity of acceptable collateral. Collateral designated by the FRBNY as acceptable under repurchase agreements primarily includes Treasury securities (including Treasury Inflation-Protected Securities, Separate Trading of Registered Interest and Principal of Securities Treasury securities, and Treasury Floating Rate Notes); direct obligations of several federal and GSE-related agencies, including Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, and Federal Home Loan Banks; and pass-through federal agency and GSE MBS. The repurchase agreements are accounted for as financing transactions with the associated interest income recognized over the life of the transaction. These repurchase agreements are reported at their contractual amounts as "System Open Market Account: Securities purchased under agreements to resell" and the related accrued interest receivable is reported as a component of "System Open Market Account: Accrued interest receivable" in the Statements of Condition. Interest income is reported as a component of "System Open Market Account: Securities purchased under agreements to resell" in the Statements of Operations.

The FRBNY may engage in sales of securities under agreements to repurchase (reverse repurchase agreements) with primary dealers and with a set of expanded counterparties that includes banks, savings associations, GSEs, and domestic money market funds. Transactions under these reverse repurchase agreements are designed to have a margin of zero and are settled through a tri-party arrangement, similar to repurchase agreements. Reverse repurchase agreements may also be executed with foreign official and international account holders as part of a service offering. Reverse repurchase agreements are collateralized by a pledge of an amount of Treasury securities, GSE debt securities, or federal agency and GSE MBS that are held in the SOMA. Reverse repurchase agreements are accounted for as financing transactions, and the associated interest expense is recognized over the life of the transaction. These reverse repurchase agreements are reported at their contractual amounts as “System Open Market Account: Securities sold under agreements to repurchase” and the related accrued interest payable is reported as a component of “System Open Market Account: Other liabilities” in the Statements of Condition. Interest expense is reported as a component of “System Open Market Account: Securities sold under agreements to repurchase” in the Statements of Operations.

Treasury securities and GSE debt securities held in the SOMA may be lent to primary dealers, typically overnight, to facilitate the effective functioning of the domestic securities markets. The amortized cost basis of securities lent continues to be reported as “System Open Market Account: Treasury securities, net” and “System Open Market Account: Government-sponsored enterprise debt securities, net,” as appropriate, in the Statements of Condition. Securities lending transactions are fully collateralized by Treasury securities based on the fair values of the securities lent increased by a margin determined by the FRBNY. The FRBNY charges the primary dealer a fee for borrowing securities, and these fees are reported as a component of “Non-interest income (loss): System Open Market Account: Other” in the Statements of Operations.

Activity related to repurchase agreements, reverse repurchase agreements, 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 the second quarter of each year.

f. Treasury Securities, Government-Sponsored Enterprise Debt Securities, Federal Agency and Government-Sponsored Enterprise Mortgage-Backed Securities, and Foreign Currency Denominated Investments

Interest income on Treasury securities, GSE debt securities, and foreign currency denominated investments included in the SOMA is recorded when earned and includes amortization of premiums and accretion of discounts. The Board of Governors approved, effective January 1, 2017, accounting for Treasury securities, GSE debt securities, and foreign government debt instruments held in the SOMA using the effective interest method. Previously, the cost bases of these securities were adjusted for amortization of premiums or accretion of discounts on a straight-line basis. This change was applied prospectively and did not have a material effect on the Bank’s financial statements for the year ended December 31, 2017.

Interest income on federal agency and GSE MBS is accrued using the effective interest method and includes amortization of premiums, accretion of discounts, and gains or losses associated with principal paydowns. Premiums and discounts related to federal agency and GSE MBS are amortized or accreted over the term of the security to stated maturity, and the amortization of premiums and accretion of discounts are accelerated when principal payments are received.

Gains and losses resulting from sales of securities are determined by specific issue based on average cost. Treasury securities, GSE debt securities, and federal agency and GSE MBS are reported net of premiums and discounts in the Statements of Condition and interest income on those securities is reported net of the amortization of premiums and accretion of discounts in the Statements of Operations.

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 for delivery in the current month combined with a simultaneous agreement to sell or purchase TBA MBS on a specified future date. During the years ended December 31, 2017 and 2016, the FRBNY executed dollar rolls to facilitate settlement of outstanding purchases of federal agency and GSE MBS. The FRBNY accounts for dollar rolls as individual purchases and sales, on a settlement-date basis. Accounting for these transactions as purchases and sales, rather than as financing transactions, is appropriate because the purchase or sale component of the MBS TBA dollar roll is paired off or assigned prior to settlement and, as a result, there is no transfer and return of securities. Net gains (losses) resulting from MBS transactions are reported as a component of "Non-interest income (loss): System Open Market Account: Federal agency and government-sponsored enterprise mortgage-backed securities gains, net" in the Statements of Operations.

Foreign currency denominated investments, which can include foreign currency deposits, repurchase agreements, and government debt instruments, are revalued daily at current foreign currency market exchange rates in order to report these assets in U.S. dollars. Any negative interest associated with these foreign currency denominated investments is included as a component of "Interest income: System Open Market Account: Foreign currency denominated investments, net" in the Statements of Operations. Foreign currency translation gains and losses that result from the daily revaluation of foreign currency denominated investments are reported as "Non-interest income (loss): System Open Market Account: Foreign currency translation gains (losses), net" in the Statements of Operations.

Because the FRBNY enters into commitments to buy Treasury securities, federal agency and GSE MBS, and foreign government debt instruments and records the related securities on a settlement-date basis in accordance with the FAM, the related outstanding commitments are not reflected in the Statements of Condition.

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 the second quarter of each year. Activity related to foreign currency denominated investments, including the premiums, discounts, and realized and unrealized gains and losses, is allocated to each Reserve Bank on a percentage basis, adjusted annually in the second quarter of each year, calculated as the ratio of each Reserve Bank's capital and surplus to the Reserve Banks' aggregate capital and surplus at the preceding December 31.

g. Central Bank Liquidity Swaps

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

Central bank liquidity swaps activity, including the related income and expense, is allocated to each Reserve Bank based on a percentage basis, adjusted annually in the second quarter of each year, calculated as the ratio of each Reserve Bank's capital and surplus to the Reserve Banks' aggregate capital and surplus at the preceding December 31.

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 Bank's allocated portion of the foreign currency amounts that the FRBNY acquires are reported as "System Open Market Account: Central bank liquidity swaps" in the Statements of Condition. Because the swap transaction will be unwound at the same U.S. dollar amount and exchange rate that were 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 amount outstanding and the rate under the swap agreement. The Bank's allocated portion of the amount of compensation received during the term of the swap transaction is reported as "Interest income: System Open Market Account: Central bank liquidity swaps" in the Statements of Operations.

Foreign currency liquidity swaps

Foreign currency liquidity swap transactions involve the transfer by the FRBNY, at the prevailing market exchange rate, of a specified amount of U.S. dollars to an account for the foreign central bank in exchange for its currency. The foreign currency amounts that the FRBNY receives are recorded as a liability.

h. 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 2 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. Reserve Banks may transfer assets to other Reserve Banks or may lease property of other Reserve Banks.

Costs incurred to acquire software are capitalized based on the purchase price. Costs incurred during the application development stage to develop internal-use software are capitalized based on 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 generally range from two to five years. Maintenance costs and minor replacements related to software are charged to operating 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.

i. Interdistrict Settlement Account

Each Reserve Bank aggregates the payments due to or from other Reserve Banks. These payments result from transactions between the Reserve Banks and transactions that involve depository institution accounts held by other Reserve Banks, such as Fedwire funds and securities transfers and check and ACH transactions. The cumulative net amount due to or from the other Reserve Banks is reflected in the "Interdistrict settlement account" in the Statements of Condition.

An annual settlement of the interdistrict settlement account occurs in the second quarter of each year. As a result of the annual settlement, the balance in each Bank's interdistrict settlement account is adjusted by an amount equal to the average balance in the account during the previous twelve-month period ended March 31. An equal and offsetting adjustment is made to each Bank's allocated portion of SOMA assets and liabilities.

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. All of the Bank's assets are eligible to be pledged as collateral. 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 reverse repurchase agreements is deducted from the eligible collateral value.

The Board of Governors may, at any time, call upon a Reserve Bank for additional security to adequately collateralize 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.

"Federal Reserve notes outstanding, net" in the Statements of Condition represents the Bank's Federal Reserve notes outstanding, reduced by the Bank's currency holdings of $6,451 million and $6,254 million at December 31, 2017 and 2016, respectively.

At December 31, 2017 and 2016, all Federal Reserve notes outstanding, net, were fully collateralized. At December 31, 2017, all gold certificates, all SDR certificates, and $1,554 billion of domestic securities held in the SOMA were pledged as collateral. At December 31, 2017, no investments denominated in foreign currencies were pledged as collateral.

k. Deposits

Depository institutions

Depository institutions' deposits represent the reserve and service-related balances in the accounts that depository institutions hold at the Bank. Required reserve balances are those that a depository institution must hold to satisfy its reserve requirement. Reserve requirements are the amount of funds that a depository institution must hold in reserve against specified deposit liabilities. Excess reserves are those held by the depository institutions in excess of their required reserve balances. 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 federal funds rate. Interest expense on depository institutions' deposits is accrued daily at the appropriate rate. Interest payable is reported as a component of "Interest payable to depository institutions and others" in the Statements of Condition.

The Term Deposit Facility (TDF) consists of deposits with specific maturities held by eligible institutions at the Reserve Banks. The Reserve Banks pay interest on these deposits at interest rates determined by auction. Interest expense on depository institutions' deposits is accrued daily at the appropriate rate. Interest payable is reported as a component of "Interest payable to depository institutions and others" in the Statements of Condition. There were no deposits held by the Bank under the TDF at December 31, 2017 and 2016.

Other

Other deposits include the Bank's allocated portion of foreign central bank and foreign government deposits held at the FRBNY.

l. 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 6 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.

The Federal Reserve Act requires each Reserve Bank to pay each member bank an annual dividend based on the amount of the member bank's paid-in capital stock and a rate determined by the member bank's total consolidated assets. Member banks with total consolidated assets in excess of a threshold established in the Federal Reserve Act receive a dividend equal to the smaller of 6 percent or the rate equal to the high yield of the 10-year Treasury note auctioned at the last auction held prior to the payment of the dividend. Member banks with total consolidated assets equal to or less than the threshold receive a dividend of 6 percent.

The threshold for total consolidated assets was $10.1 billion and $10.0 billion for the years ended December 31, 2017 and 2016, respectively. This threshold is adjusted annually based on the Gross Domestic Product Price Index, which is published by the Bureau of Economic Analysis. The dividend is paid semiannually and is cumulative.

m. Surplus

The Federal Reserve Act limits aggregate Reserve Bank surplus to $10 billion, which is allocated among the Reserve Banks based on the ratio of each Bank's capital paid-in to total Reserve Bank capital paid-in as of December 31 of each year. The amount reported as surplus by the Bank as of December 31, 2017 and 2016 represents the Bank's allocated portion of surplus.

Accumulated other comprehensive loss is reported as a component of "Surplus" in the Statements of Condition and the Statements of Changes in Capital. Additional information regarding the classifications of accumulated other comprehensive loss is provided in Notes 9 and 10.

n. Earnings Remittances to the Treasury

The Federal Reserve Act requires that any amounts of the surplus funds of the Reserve Banks that exceed, or would exceed, the aggregate surplus limitation of $10 billion shall be transferred to the Board of Governors for transfer to the Treasury. The Bank remits excess earnings to the Treasury after providing for the cost of operations, payment of dividends, and reservation of an amount necessary to maintain surplus at the Bank's allocated portion of the $10 billion aggregate surplus limitation. Remittances to the Treasury are made on a weekly basis. The amount of the remittances to the Treasury is reported as "Earnings remittances to the Treasury" in the Statements of Operations. The amount due to the Treasury is reported as "Accrued remittances to the Treasury" in the Statements of Condition. See Note 12 for additional information on earnings remittances to the Treasury.

If earnings during the year are not sufficient to provide for the costs of operations, payment of dividends, and maintaining surplus at an amount equal to the Bank's allocated portion of the $10 billion aggregate surplus limitation, remittances to the Treasury are suspended. This decrease in earnings remittances to the Treasury results in a deferred asset that represents the amount of net earnings a Reserve Bank will need to realize before remittances to the Treasury resume.

o. Income and Costs Related to Treasury Services

When directed by the Secretary of the Treasury, the Bank is required by the Federal Reserve Act to serve as fiscal agent and depositary of the United States Government. By statute, the Treasury has appropriations to pay for these services. During the years ended December 31, 2017 and 2016, the Bank was reimbursed for all services provided to the Treasury as its fiscal agent.

p. Compensation Received for Service Costs Provided

The Federal Reserve Bank of Atlanta has overall responsibility for managing the Reserve Banks' provision of check and ACH services to depository institutions, the FRBNY has overall responsibility for managing the Reserve Banks' provision of Fedwire funds and securities services, and the Federal Reserve Bank of Chicago has overall responsibility for managing the Reserve Banks' provision of electronic access services to depository institutions. The Reserve Bank that has overall responsibility for managing these services recognizes the related total System revenue in its Statements of Operations. The Bank is compensated for costs incurred to provide these services by the Reserve Banks responsible for managing these services and reports this compensation as "Non-interest income (loss): Compensation received for service costs provided" in its Statements of Operations.

q. Assessments

The Board of Governors assesses the Reserve Banks to fund its operations and the operations of the Bureau. These assessments are allocated to each Reserve Bank based on each Reserve Bank's capital and surplus balances. The Board of Governors also assesses each Reserve Bank for expenses related to producing, issuing, and retiring 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.

The Dodd-Frank Act requires that, after the transfer of its responsibilities to the Bureau on July 21, 2011, the Board of Governors fund the Bureau in an amount not to exceed a fixed percentage of the total operating expenses of the System as reported in the Board of Governor's 2009 annual report, which totaled $4.98 billion. After 2013, the amount will be adjusted annually in accordance with the provisions of the Dodd-Frank Act. The percentage of total operating expenses of the System for the years ended December 31, 2017 and 2016 was 12.98 percent ($646.2 million) and 12.68 percent ($631.7 million), respectively. The Bank's assessment for Bureau funding is reported as "Operating expenses: Assessments: Bureau of Consumer Financial Protection" in the Statements of Operations.

r. Taxes

The Reserve Banks are exempt from federal, state, and local taxes, except for taxes on real property. The Bank's real property taxes were $1 million for each of the years ended December 31, 2017 and 2016, and are reported as a component of "Operating expenses: Occupancy" in the Statements of Operations.

s. 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 Bank commits to a formalized restructuring plan or executes the specific actions contemplated in the plan and all criteria for financial statement recognition have been met.

In 2014, the Treasury announced plans to consolidate the provision of substantially all fiscal agent services for the U.S. Treasury at the Federal Reserve Bank of Cleveland, the Federal Reserve Bank of Kansas City, the FRBNY, and the Federal Reserve Bank of St. Louis. The consolidation is expected to be completed in future years.

Note 11 describes the Bank's restructuring initiatives and provides information about the costs and liabilities associated with employee separations and contract terminations. 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.

The Bank had no significant restructuring activities in 2017 and 2016.

t. Recently Issued Accounting Standards

Other than the significant differences described in Note 3, the accounting policies described in FAM are generally consistent with those in GAAP. The following items represent recent GAAP accounting standards and describe how FAM was or will be revised to be consistent with these standards.

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This update was issued to create common revenue recognition guidance for U.S. GAAP and International Financial Reporting Standards. The guidance is applicable to all contracts for the transfer of goods or services regardless of industry or type of transaction. This update requires recognition of revenue in a manner that reflects the consideration that the entity expects to receive in return for the transfer of goods or services to customers. Subsequently, the FASB issued a number of related ASUs including ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*; ASU 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*; ASU 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*; ASU 2016-12, *Revenue from Contracts with Customers (Topic 606):*

Narrow-Scope Improvements and Practical Expedients; and ASU 2016-20, *Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers*. This revenue recognition accounting guidance is effective for the Bank for the year ending December 31, 2019, although the Bank may elect to adopt the guidance earlier. The Bank is continuing to evaluate the effect of this new guidance on its financial statements.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. The amendments in this update eliminate the requirement to disclose methods and significant assumptions used to estimate the fair value for financial instruments measured at amortized cost on the balance sheet. This update is effective for the Bank for the year ending December 31, 2019 and is not expected to have a material effect on the Bank's financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. This update revises the model to assess how a lease should be classified and provides guidance for lessees, requiring lessees to present right-of-use assets and lease liabilities on the balance sheet. The update is effective for the Bank for the year ending December 31, 2020, although earlier adoption is permitted. The Bank is continuing to evaluate the effect of this new guidance on its financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. This update revises the methodology for assessing expected credit losses and requires consideration of reasonable and supportable information to inform credit loss estimates. The update is effective for the Bank for the year ending December 31, 2021, although earlier adoption is permitted. The Bank is continuing to evaluate the effect of this new guidance on its financial statements.

In December 2016, the FASB issued ASU 2016-19, *Technical Corrections and Improvements*. This update covers a wide range of topics in the accounting standard codification and addresses differences between original guidance and the codification. It provides clarification of certain guidance including reference corrections and makes minor improvements to accounting standards. This update was effective for the Bank for the year ended December 31, 2016 and did not have an impact on the Bank's financial statements.

In March 2017, the FASB issued ASU 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This update requires an employer to disaggregate the service cost component from the other components of net benefit cost. It also provides explicit guidance on how to present the service cost component and the other components of net benefit cost in the income statement and allows only the service cost component of net benefit cost to be eligible for capitalization. This update is effective for the Bank for the year ending December 31, 2019, and the Bank is continuing to evaluate the effect of this new guidance on its financial statements.

(4) LOANS

Loans to Depository Institutions

The Bank offers primary, secondary, and seasonal loans to eligible borrowers (depository institutions that maintain reservable transaction accounts or nonpersonal time deposits and have established discount window borrowing privileges). Each program has its own interest rate and interest is accrued using the applicable interest rate established at least every 14 days by the Bank's board of directors, subject to review and determination by the Board of Governors. Primary and secondary loans are extended on a short-term basis, typically overnight, whereas seasonal loans may be extended for a period of up to nine months.

Primary, secondary, and seasonal loans are collateralized to the satisfaction of the Bank 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; asset-backed securities; 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 Bank, which is typically fair value reduced by a margin. Loans to depository institutions are monitored daily to ensure that borrowers continue to meet eligibility requirements for these programs. If a borrower no longer qualifies for these programs, the Bank will generally request full repayment of the outstanding loan or, for primary or seasonal loans, 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.

The Bank had no loans outstanding as of December 31, 2017 and 2016.

At December 31, 2017 and 2016, the Bank did not have any loans that were impaired, restructured, past due, or on non-accrual status, and no allowance for loan losses was required. There were no impaired loans during the years ended December 31, 2017 and 2016. Interest income attributable to loans to depository institutions was immaterial during the years ended December 31, 2017 and 2016.

(5) SYSTEM OPEN MARKET ACCOUNT

a. Domestic Securities Holdings

The FRBNY executes domestic open market operations and, on behalf of the Reserve Banks, holds the resulting securities in the SOMA.

Pursuant to FOMC directives, during the year ended December 31, 2016 and through September 30, 2017, the FRBNY continued to reinvest all principal payments from the SOMA's holdings of GSE debt securities and federal agency and GSE MBS in federal agency and GSE MBS and to roll over maturing Treasury securities at auction. In October 2017, the FOMC initiated a balance sheet normalization program intended to reduce gradually the SOMA holdings by decreasing reinvestment of the principal payments received from securities held in the SOMA through the implementation of monthly caps. Effective from October 2017 and through December 2017, the FOMC directed the FRBNY to roll over principal payments from the SOMA holdings of Treasury securities maturing during each calendar month that exceeded a $6 billion cap, and to reinvest in federal agency and GSE MBS the amount of principal payments from the SOMA holdings of GSE debt securities and federal agency and GSE MBS received during each calendar month that exceeded a $4 billion cap. According to the balance sheet normalization plan, the FOMC anticipates that it will increase the monthly cap on Treasury redemptions in steps of $6 billion at three-month intervals over 12 months until it reaches $30 billion per month, and that it will increase the monthly cap on GSE debt securities and federal agency and GSE MBS paydowns in steps of $4 billion at three-month intervals over 12 months until it reaches $20 billion per month. The FOMC also anticipates that the caps will remain in place once they reach their respective maximums so that the SOMA holdings will continue to decline in a gradual and predictable manner until the FOMC judges that the SOMA is holding no more securities than necessary to implement monetary policy efficiently and effectively.
The Bank's allocated share of activity related to domestic open market operations was 2.582 percent and 2.715 percent at December 31, 2017 and 2016, respectively.

The Bank's allocated share of Treasury securities, GSE debt securities, and federal agency and GSE MBS, net, excluding accrued interest, held in the SOMA at December 31, 2017 and 2016 was as follows (in millions):

	2017			
	Par	Unamortized premiums	Unaccreted discounts	Total amortized cost
Treasury securities				
Notes	$ 41,947	$ 250	$ (122)	$ 42,075
Bonds	21,420	2,467	(232)	23,655
Total Treasury securities	$ 63,367	$ 2,717	$ (354)	$ 65,730
GSE debt securities	$ 113	$ 10	$ -	$ 123
Federal agency and GSE MBS	$ 45,570	$ 1,372	$ (10)	$ 46,932

	2016			
	Par	Unamortized premiums	Unaccreted discounts	Total amortized cost
Treasury securities				
Notes	$ 44,480	$ 401	$ (152)	$ 44,729
Bonds	22,413	2,816	(247)	24,982
Total Treasury securities	$ 66,893	$ 3,217	$ (399)	$ 69,711
GSE debt securities	$ 439	$ 13	$ -	$ 452
Federal agency and GSE MBS	$ 47,283	$ 1,466	$ (11)	$ 48,738

There were no material transactions related to repurchase agreements during the years ended December 31, 2017 and 2016.

During the years ended December 31, 2017 and 2016, the FRBNY entered into reverse repurchase agreements as part of its monetary policy activities. These operations have been undertaken as necessary to maintain the federal funds rate in a target range. In addition, reverse repurchase agreements are entered into as part of a service offering to foreign official and international account holders. Financial information related to reverse repurchase agreements allocated to the Bank and held in the SOMA for the years ended December 31, 2017 and 2016 was as follows (in millions):

	Allocated to the Bank		Total SOMA	
	2017	2016	2017	2016
Primary dealers and expanded counterparties:				
Contract amount outstanding, end of year	$ 8,252	$ 12,717	$ 319,595	$ 468,355
Average daily amount outstanding, during the year	3,834	2,817	145,959	105,648
Maximum balance outstanding, during the year	12,717	12,717	468,355	474,592
Securities pledged (par value), end of year	7,815	12,050	302,690	443,799
Securities pledged (fair value), end of year	8,263	12,742	320,048	469,282
Foreign official and international accounts:				
Contract amount outstanding, end of year	$ 6,309	$ 6,974	$ 244,363	$ 256,855
Average daily amount outstanding, during the year	6,332	6,414	241,581	241,848
Maximum balance outstanding, during the year	7,176	7,196	264,290	265,041
Securities pledged (par value), end of year	6,214	6,772	240,660	249,417
Securities pledged (fair value), end of year	6,311	6,975	244,417	256,897
Total contract amount outstanding, end of year	$ 14,561	$ 19,691	$ 563,958	$ 725,210
Supplemental information - interest expense:				
Primary dealers and expanded counterparties	$ 32	$ 8	$ 1,224	$ 303
Foreign official and international accounts	56	22	2,141	819
Total interest expense - securities sold under agreements to repurchase	$ 88	$ 30	$ 3,365	$ 1,122

Securities pledged as collateral, at December 31, 2017 and 2016, consisted solely of Treasury securities. The contract amount outstanding as of December 31, 2017 of reverse repurchase agreements that were transacted with primary dealers and expanded counterparties had a term of one business day and matured on January 2, 2018. The contract amount outstanding as of December 31, 2017 of reverse repurchase agreements that were transacted with foreign official and international account holders had a term of one business day and matured on January 2, 2018.

The remaining maturity distribution of Treasury securities, GSE debt securities, federal agency and GSE MBS bought outright, and reverse repurchase agreements that were allocated to the Bank at December 31, 2017 and 2016 was as follows (in millions):

	Within 15 days	16 days to 90 days	91 days to 1 year	Over 1 year to 5 years	Over 5 years to 10 years	Over 10 years	Total
December 31, 2017:							
Treasury securities (par value)	$ 532	$ 2,780	$ 8,144	$ 27,815	$ 8,014	$ 16,082	$ 63,367
GSE debt securities (par value)	-	-	51	2	-	60	113
Federal agency and GSE MBS (par value)[1]	-	-	-	4	517	45,049	45,570
Securities sold under agreements to repurchase (contract amount)	14,561	-	-	-	-	-	14,561
December 31, 2016:							
Treasury securities (par value)	$ 402	$ 1,120	$ 4,094	$ 33,244	$ 10,841	$ 17,192	$ 66,893
GSE debt securities (par value)	-	77	243	55	-	64	439
Federal agency and GSE MBS (par value)[1]	-	-	-	2	287	46,994	47,283
Securities sold under agreements to repurchase (contract amount)	19,691	-	-	-	-	-	19,691

[1] The par amount shown for federal agency and GSE MBS is the remaining principal balance of the securities.

Federal agency and GSE MBS are reported at stated maturity in the table above. The estimated weighted-average life of these securities, which differs from the stated maturity primarily because it factors in scheduled payments and prepayment assumptions, was approximately 6.9 and 7.2 years as of December 31, 2017 and 2016, respectively.

The amortized cost and par value of Treasury securities and GSE debt securities that were loaned from the SOMA under securities lending agreements allocated to the Bank and held in the SOMA at December 31, 2017 and 2016 were as follows (in millions):

	Allocated to the Bank		Total SOMA	
	2017	2016	2017	2016
Treasury securities (amortized cost)	$ 724	$ 684	$ 28,053	$ 25,195
Treasury securities (par value)	697	671	26,990	24,698
GSE debt securities (amortized cost)	-	1	-	44
GSE debt securities (par value)	-	1	-	44

Securities pledged as collateral by the counterparties in the securities lending arrangements at December 31, 2017 and 2016 consisted solely of Treasury securities. The securities lending agreements outstanding as of December 31, 2017 had a term of one business day and matured on January 2, 2018.

The FRBNY enters into commitments to buy and sell Treasury securities and records the related securities on a settlement-date basis. As of December 31, 2017, the total purchase price of the Treasury securities under outstanding commitments was $11,447 million of which $296 million was allocated to the Bank. These commitments had contractual settlement dates extending through January 2, 2018.

The FRBNY enters into commitments to buy and sell federal agency and GSE MBS and records the related securities on a settlement-date basis. As of December 31, 2017, the total purchase price of the federal agency and GSE MBS under outstanding purchase commitments was $19,257 million, none of which was related to dollar rolls. The total purchase price of outstanding purchase commitments allocated to the Bank was $497 million, none of which was related to dollar rolls. These commitments, which had contractual settlement dates extending through January 2018, are 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. As of December 31, 2017, there were no outstanding sales commitments for federal agency and GSE MBS. MBS commitments are subject to varying degrees of off-balance-sheet market risk and counterparty credit risk that result from their future settlement. The FRBNY requires the posting of cash collateral for MBS commitments as part of its risk management practices used to mitigate the counterparty credit risk.

Other liabilities, which are primarily related to federal agency and GSE MBS purchases and sales, include the FRBNY's obligation to return cash margin posted by counterparties as collateral under commitments to purchase and sell federal agency and GSE MBS. In addition, other liabilities include obligations that arise from the failure of a seller to deliver MBS 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 included in other liabilities represents the FRBNY's obligation to pay for the securities when delivered. The amount of other liabilities allocated to the Bank and held in the SOMA at December 31, 2017 and 2016 was as follows (in millions):

	Allocated to the Bank		Total SOMA	
	2017	2016	2017	2016
Other liabilities:				
Cash margin	$ 12	$ 27	$ 481	$ 983
Obligations from MBS transaction fails	-	-	14	9
Other	2	-	63	20
Total other liabilities	$ 14	$ 27	$ 558	$ 1,012

Accrued interest receivable on domestic securities holdings held in the SOMA was $24,655 million and $25,517 million as of December 31, 2017 and 2016, respectively, of which $637 million and $693 million, respectively, was allocated to the Bank. These amounts are reported as a component of "System Open Market Account: Accrued interest receivable" in the Statements of Condition.

Information about transactions related to Treasury securities, GSE debt securities, and federal agency and GSE MBS allocated to the Bank and held in the SOMA during the years ended December 31, 2017 and 2016, is summarized as follows (in millions):

	Allocated to the Bank				
	Notes	Bonds	Total Treasury securities	GSE debt securities	Federal agency and GSE MBS
Balance at December 31, 2015	$ 41,019	$ 23,167	$ 64,186	$ 839	$ 44,780
Purchases[1]	5,052	368	5,420	-	10,318
Sales[1]	(15)	(2)	(17)	-	(6)
Realized gains (losses), net[2]	(1)	1	-	-	1
Principal payments and maturities	(4,964)	(445)	(5,409)	(446)	(10,147)
Amortization of premiums and accretion of discounts, net	(133)	(267)	(400)	(9)	(358)
Inflation adjustment on inflation-indexed securities	16	40	56	-	-
Annual reallocation adjustment[3]	3,755	2,120	5,875	68	4,150
Balance at December 31, 2016	$ 44,729	$ 24,982	$ 69,711	$ 452	$ 48,738
Purchases[1]	4,237	414	4,651	-	8,532
Sales[1]	(3)	(8)	(11)	-	(9)
Realized gains (losses), net[2]	-	1	1	-	-
Principal payments and maturities	(4,617)	(346)	(4,963)	(308)	(7,608)
Amortization of premiums and accretion of discounts, net	(100)	(207)	(307)	(3)	(276)
Inflation adjustment on inflation-indexed securities	19	48	67	-	-
Annual reallocation adjustment[3]	(2,190)	(1,229)	(3,419)	(18)	(2,445)
Balance at December 31, 2017	$ 42,075	$ 23,655	$ 65,730	$ 123	$ 46,932
Year-ended December 31, 2016					
Supplemental information - par value of transactions:					
Purchases[4]	$ 5,059	$ 368	$ 5,427	$ -	$ 9,945
Sales	(15)	(1)	(16)	-	(6)
Year-ended December 31, 2017					
Supplemental information - par value of transactions:					
Purchases[4]	$ 4,248	$ 417	$ 4,665	$ -	$ 8,277
Sales	(3)	(7)	(10)	-	(8)

[1] Purchases and sales may include payments and receipts related to principal, premiums, discounts, and inflation compensation adjustments to the basis of inflation-indexed securities. The amount reported as sales includes the realized gains and losses on such transactions. Purchases and sales exclude MBS TBA transactions that are settled on a net basis.
[2] Realized gains (losses), net is the offset of the amount of realized gains and losses included in the reported sales amount.
[3] Reflects the annual adjustment to the Bank's allocated portion of the related SOMA securities that results from the annual settlement of the interdistrict settlement account, as discussed in Note 3i.
[4] Includes inflation compensation.

	Total SOMA				
	Notes	Bonds	Total Treasury securities	GSE debt securities	Federal agency and GSE MBS
Balance at December 31, 2015	$ 1,649,228	$ 931,448	$ 2,580,676	$ 33,748	$ 1,800,449
Purchases[1]	190,992	13,882	204,874	-	387,210
Sales[1]	(534)	(62)	(596)	-	(213)
Realized gains (losses), net[2]	(22)	7	(15)	-	6
Principal payments and maturities	(187,843)	(16,597)	(204,440)	(16,764)	(379,065)
Amortization of premiums and accretion of discounts, net	(5,049)	(10,033)	(15,082)	(336)	(13,384)
Inflation adjustment on inflation-indexed securities	567	1,438	2,005	-	-
Balance at December 31, 2016	$ 1,647,339	$ 920,083	$ 2,567,422	$ 16,648	$ 1,795,003
Purchases[1]	161,378	15,849	177,227	-	324,524
Sales[1]	(124)	(326)	(450)	-	(331)
Realized gains (losses), net[2]	(2)	30	28	-	2
Principal payments and maturities	(175,933)	(13,402)	(189,335)	(11,789)	(290,939)
Amortization of premiums and accretion of discounts, net	(3,796)	(7,917)	(11,713)	(107)	(10,559)
Inflation adjustment on inflation-indexed securities	709	1,845	2,554	-	-
Balance at December 31, 2017	$ 1,629,571	$ 916,162	$ 2,545,733	$ 4,752	$ 1,817,700
Year-ended December 31, 2016					
Supplemental information - par value of transactions:					
Purchases[3]	$ 191,231	$ 13,868	$ 205,099	$ -	$ 373,197
Sales	(555)	(45)	(600)	-	(203)
Year-ended December 31, 2017					
Supplemental information - par value of transactions:					
Purchases[3]	$ 161,796	$ 15,976	$ 177,772	$ -	$ 314,797
Sales	(125)	(275)	(400)	-	(320)

[1] Purchases and sales may include payments and receipts related to principal, premiums, discounts, and inflation compensation adjustments to the basis of inflation-indexed securities. The amount reported as sales includes the realized gains and losses on such transactions. Purchases and sales exclude MBS TBA transactions that are settled on a net basis.
[2] Realized gains (losses), net is the offset of the amount of realized gains and losses included in the reported sales amount.
[3] Includes inflation compensation.

b. Foreign Currency Denominated Investments

The FRBNY conducts foreign currency operations and, on behalf of the Reserve Banks, holds the resulting foreign currency denominated investments in the SOMA.

The FRBNY holds foreign currency deposits with foreign central banks and invests in foreign government debt instruments of France, Germany, the Netherlands, and Japan. These foreign government debt instruments are backed by the full faith and credit of the issuing foreign governments. In addition, the FRBNY may enter into repurchase agreements to purchase government debt securities for which the accepted collateral is the debt instruments issued by a foreign government.

At December 31, 2017 and 2016, there were no repurchase agreements outstanding and, consequently, no related foreign securities held as collateral.

The Bank's allocated share of activity related to foreign currency operations was 5.377 percent and 5.502 percent at December 31, 2017 and 2016, respectively.

Information about foreign currency denominated investments recorded at amortized cost and valued at foreign currency market exchange rates allocated to the Bank and held in the SOMA at December 31, 2017 and 2016 was as follows (in millions):

	Allocated to the Bank		Total SOMA	
	2017	2016	2017	2016
Euro:				
Foreign currency deposits	$ 326	$ 231	$ 6,070	$ 4,205
French government debt instruments	166	214	3,089	3,892
German government debt instruments	120	104	2,239	1,884
Dutch government debt instruments	88	81	1,626	1,462
Japanese yen:				
Foreign currency deposits	364	257	6,765	4,668
Japanese government debt instruments	82	183	1,527	3,331
Total	$ 1,146	$ 1,070	$ 21,316	$ 19,442

Net interest income earned on foreign currency denominated investments for the years ended December 31, 2017 and 2016 was immaterial for the Bank and held in the SOMA as follows (in millions):

	Total SOMA	
	2017	2016
Net interest income:[1]		
Euro	$ (19)	$ (11)
Japanese yen	2	4
Total net interest income	$ (17)	$ (7)

[1] As a result of negative interest rates in certain foreign currency denominated investments held in the SOMA, interest income on foreign currency denominated investments, net contains negative interest of $36 million and $32 million for the years ended December 31, 2017 and 2016, respectively.

Accrued interest receivable on foreign currency denominated investments, net was $82 million and $79 million as of December 31, 2017 and 2016, respectively, of which $4 million was allocated to the Bank. These amounts are reported as a component of "System Open Market Account: Accrued interest receivable" in the Statements of Condition.

The remaining maturity distribution of foreign currency denominated investments that were allocated to the Bank at December 31, 2017 and 2016 was as follows (in millions):

	Within 15 days	16 days to 90 days	91 days to 1 year	Over 1 year to 5 years	Over 5 years to 10 years	Total
December 31, 2017:						
Euro	$ 331	$ 5	$ 66	$ 168	$ 130	$ 700
Japanese yen	364	3	14	65	-	446
Total	$ 695	$ 8	$ 80	$ 233	$ 130	$ 1,146
December 31, 2016:						
Euro	$ 234	$ 18	$ 64	$ 175	$ 139	$ 630
Japanese yen	266	19	74	81	-	440
Total	$ 500	$ 37	$ 138	$ 256	$ 139	$ 1,070

There were no foreign exchange contracts related to foreign currency operations outstanding as of December 31, 2017.

The FRBNY enters into commitments to buy foreign government debt instruments and records the related securities on a settlement-date basis. As of December 31, 2017, there were no outstanding commitments to purchase foreign government debt instruments. During 2017, there were purchases and maturities of foreign government debt instruments of $576 million and $3,567 million, respectively, of which $31 million and $193 million, respectively, were allocated to the Bank. There were immaterial sales of foreign government debt instruments in 2017.

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

Foreign currency working balances held and foreign exchange contracts executed by the Bank to facilitate international payments and currency transactions made on behalf of foreign central banks and U.S. official institution customers were immaterial as of December 31, 2017 and 2016.

c. Central Bank Liquidity Swaps

U.S. Dollar Liquidity Swaps

The Bank's allocated share of U.S. dollar liquidity swaps was 5.377 percent and 5.502 percent at December 31, 2017 and 2016, respectively.

The total foreign currency held in the SOMA under U.S. dollar liquidity swaps at December 31, 2017 and 2016 was $12,067 million and $5,563 million, respectively, of which $649 million and $306 million, respectively, was allocated to the Bank.

The remaining maturity distribution of U.S. dollar liquidity swaps that were allocated to the Bank at December 31, 2017 and 2016 was as follows (in millions):

	2017	2016
	Within 15 days	Within 15 days
Euro	$ 640	$ 239
Japanese yen	9	67
Total	$ 649	$ 306

Foreign Currency Liquidity Swaps

At December 31, 2017 and 2016, there was no balance outstanding related to foreign currency liquidity swaps.

d. Fair Value of SOMA Assets and Liabilities

The fair value amounts below are presented solely for informational purposes and are not intended to comply with the fair value disclosures required by FASB Accounting Standards Codification (ASC) Topic 820 (ASC 820), *Fair Value Measurement*. Although the fair value of SOMA 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. Because SOMA securities are recorded at amortized cost, cumulative unrealized gains (losses) are not recognized in the Statements of Condition and the changes in cumulative unrealized gains (losses) are not recognized in the Statements of Operations.

The fair value of the Treasury securities, GSE debt securities, federal agency and GSE MBS, and foreign government debt instruments held in the SOMA is subject to market risk, arising from movements in market variables such as interest rates and credit risk. The fair value of federal agency and GSE MBS is also affected by the expected rate of prepayments of mortgage loans underlying the securities. The fair value of foreign government debt instruments is also affected by currency risk. Based on evaluations performed as of December 31, 2017 and 2016, there are no credit impairments of SOMA securities holdings.

The following table presents the amortized cost, fair value, and cumulative unrealized gains (losses) on the Treasury securities, GSE debt securities, and federal agency and GSE MBS allocated to the Bank and held in the SOMA at December 31, 2017 and 2016 (in millions):

	Allocated to the Bank					
	2017			2016		
	Amortized cost	Fair value	Cumulative unrealized gains (losses), net	Amortized cost	Fair value	Cumulative unrealized gains (losses), net
Treasury securities:						
Notes	$ 42,075	$ 41,945	$ (130)	$ 44,729	$ 44,992	$ 263
Bonds	23,655	26,038	2,383	24,982	26,709	1,727
Total Treasury securities	65,730	67,983	2,253	69,711	71,701	1,990
GSE debt securities	123	139	16	452	474	22
Federal agency and GSE MBS	46,932	46,731	(201)	48,738	48,533	(205)
Total domestic SOMA portfolio securities holdings	$ 112,785	$ 114,853	$ 2,068	$ 118,901	$ 120,708	$ 1,807
Memorandum - Commitments for:						
Purchases of Treasury securities	$ 296	$ 296	$ -	$ 317	$ 318	$ 1
Purchases of Federal agency and GSE MBS	497	498	1	972	977	5

	Total SOMA					
	2017			2016		
	Amortized cost	Fair value	Cumulative unrealized gains (losses), net	Amortized cost	Fair value	Cumulative unrealized gains (losses), net
Treasury securities:						
Notes	$ 1,629,571	$ 1,624,540	$ (5,031)	$ 1,647,339	$ 1,657,026	$ 9,687
Bonds	916,162	1,008,468	92,306	920,083	983,680	63,597
Total Treasury securities	2,545,733	2,633,008	87,275	2,567,422	2,640,706	73,284
GSE debt securities	4,752	5,383	631	16,648	17,442	794
Federal agency and GSE MBS	1,817,700	1,809,918	(7,782)	1,795,003	1,787,484	(7,519)
Total domestic SOMA portfolio securities holdings	$ 4,368,185	$ 4,448,309	$ 80,124	$ 4,379,073	$ 4,445,632	$ 66,559
Memorandum - Commitments for:						
Purchases of Treasury securities	$ 11,447	$ 11,467	$ 20	$ 11,679	$ 11,719	$ 40
Purchases of Federal agency and GSE MBS	19,257	19,285	28	35,787	35,974	187

The fair value of Treasury securities and GSE debt securities was determined using pricing services that provide market consensus prices based on indicative quotes from various market participants. The fair value of federal agency and GSE MBS was determined using a pricing service that utilizes a model-based approach that considers observable inputs for similar securities.

The cost bases of repurchase agreements, reverse repurchase agreements, central bank liquidity swaps, and other investments held in the SOMA portfolio approximate fair value. Due to the short-term nature of these agreements and the defined amount that will be received upon settlement, the cost basis is estimated to approximate fair value.

At December 31, 2017 and 2016, the fair value of foreign currency denominated investments held in the SOMA was $21,348 million and $19,510 million, respectively, of which $1,148 million and $1,073 million, respectively, was allocated to the Bank. The fair value of foreign government debt instruments was determined using pricing services that provide market consensus prices based on indicative quotes from various market participants. The fair value of foreign currency deposits was determined by reference to market interest rates.

The following table provides additional information on the amortized cost and fair value of the federal agency and GSE MBS portfolio held in the SOMA and allocated to the Bank at December 31, 2017 and 2016 (in millions):

Distribution of MBS holdings by coupon rate	2017		2016	
	Amortized cost	Fair value	Amortized cost	Fair value
Allocated to the Bank:				
2.0%	$ 232	$ 226	$ 287	$ 278
2.5%	2,852	2,798	3,294	3,221
3.0%	17,406	17,065	18,831	18,370
3.5%	16,282	16,273	15,240	15,219
4.0%	7,483	7,536	7,484	7,599
4.5%	1,758	1,856	2,345	2,501
5.0%	732	776	997	1,063
5.5%	163	174	225	243
6.0%	22	24	31	34
6.5%	2	3	4	5
Total	$ 46,932	$ 46,731	$ 48,738	$ 48,533
Total SOMA:				
2.0%	$ 8,968	$ 8,739	$ 10,556	$ 10,243
2.5%	110,452	108,371	121,326	118,641
3.0%	674,138	660,939	693,524	676,572
3.5%	630,590	630,245	561,271	560,510
4.0%	289,819	291,868	275,650	279,877
4.5%	68,069	71,896	86,351	92,111
5.0%	28,352	30,048	36,708	39,159
5.5%	6,318	6,739	8,298	8,939
6.0%	870	939	1,155	1,253
6.5%	124	134	164	179
Total	$ 1,817,700	$ 1,809,918	$ 1,795,003	$ 1,787,484

The following tables present the realized gains (losses) and the change in the cumulative unrealized gains (losses) related to SOMA domestic securities holdings allocated to the Bank and held in the SOMA during the years ended December 31, 2017 and 2016 (in millions):

	Allocated to Bank			
	2017		2016	
	Realized gains, net[1]	Change in cumulative unrealized gains (losses)[2, 4]	Realized gains, net[3]	Change in cumulative unrealized gains (losses)[2, 4]
Treasury securities	$ 1	$ 398	$ -	$ (797)
GSE debt securities	-	(4)	-	(17)
Federal agency and GSE MBS	-	9	1	(540)
Total	$ 1	$ 403	$ 1	$ (1,354)

	Total SOMA			
	2017		2016	
	Realized gains, net[1,3]	Change in cumulative unrealized gains (losses)[2]	Realized (losses) gains, net[1,3]	Change in cumulative unrealized gains (losses)[2]
Treasury securities	$ 28	$ 13,991	$ (15)	$ (21,949)
GSE debt securities	-	(163)	-	(623)
Federal agency and GSE MBS	8	(263)	19	(17,326)
Total	$ 36	$ 13,565	$ 4	$ (39,898)

[1] Realized gains (losses) for Treasury securities are reported in "Non-interest income (loss): System Open Market Account: Treasury securities gains, net" in the Statements of Operations.

[2] Because SOMA securities are recorded at amortized cost, the change in the cumulative unrealized gains (losses) is not reported in the Statements of Operations.

[3] Realized gains for federal agency and GSE MBS are reported in "Non-interest income (loss): System Open Market Account: Federal agency and government-sponsored enterprise mortgage-backed securities gains, net" in the Statements of Operations.

[4] The amount reported as change in cumulative unrealized gains (losses) allocated to the Bank is affected by the annual adjustment to the Bank's allocated portion of the related SOMA securities, as discussed in Note 3f.

The amount of change in cumulative unrealized gains (losses) position, net related to foreign currency denominated investments was a loss of $36 million and a gain of $5 million for the years ended December 31, 2017 and 2016, respectively, of which $2 million and $277 thousand, respectively, were allocated to the Bank. Realized gains, net related to foreign currency denominated investments was an immaterial amount for the year ended December 31, 2017 and zero for the year ended December 31, 2016.

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 establishes a three-level fair value hierarchy that distinguishes between assumptions developed using market data obtained from independent sources (observable inputs) and the Bank's assumptions developed using the best information available in the circumstances (unobservable inputs). The three levels established by ASC 820 are described as follows:

- 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 model-based techniques that use significant inputs and assumptions not observable in the market. These unobservable inputs and assumptions reflect the Bank's estimates of inputs and assumptions that market participants would use in pricing the assets and liabilities. Valuation techniques include the use of option pricing models, discounted cash flow models, and similar techniques.

Treasury securities, GSE debt securities, federal agency and GSE MBS, and foreign government debt instruments are classified as Level 2 within the ASC 820 hierarchy because the fair values are based on indicative quotes and other observable inputs obtained from independent pricing services. The fair value hierarchy level of SOMA financial assets is not necessarily an indication of the risk associated with those assets.

(6) BANK PREMISES, EQUIPMENT, AND SOFTWARE

Bank premises and equipment at December 31, 2017 and 2016 were as follows (in millions):

	2017	2016
Bank premises and equipment:		
Land and land improvements	$ 8	$ 8
Buildings	120	116
Building machinery and equipment	28	29
Construction in progress	3	1
Furniture and equipment	43	47
Subtotal	202	201
Accumulated depreciation	(117)	(116)
Bank premises and equipment, net	$ 85	$ 85
Depreciation expense, for the years ended December 31	$ 9	$ 9

The Bank leases space to outside tenants with remaining lease terms ranging from five to nine years. Rental income from such leases was $3 million and $2 million for the years ended December 31, 2017 and 2016, respectively, and is reported as a component of "Non-interest income (loss): Other" in the Statements of Operations. Future minimum lease payments that the Bank will receive under non-cancelable lease agreements in existence at December 31, 2017, are as follows (in millions):

2018	$ 3
2019	3
2020	3
2021	3
2022	3
Thereafter	7
Total	$ 22

The Bank had capitalized software assets, net of amortization, of $6 million and $15 million at December 31, 2017 and 2016, respectively. Amortization expense was $2 million and $3 million for the years ended December 31, 2017 and 2016, respectively. Capitalized software assets are reported as a component of "Other assets" in the Statements of Condition and the related amortization is reported as a component of "Operating expenses: Other" in the Statements of Operations.

(7) COMMITMENTS AND CONTINGENCIES

In conducting its operations, the Bank enters into contractual commitments, normally with fixed expiration dates or termination provisions, at specific rates and for specific purposes.

At December 31, 2017, the Bank was obligated under non-cancelable leases for premises and equipment with remaining terms ranging from one to approximately two years. These leases provide for increased lease payments based upon increases in real estate taxes, operating costs, or selected price indexes.

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), was $2 million and $1 million for the years ended December 31, 2017 and 2016, respectively.

Future minimum lease payments under non-cancelable operating leases with remaining terms of one year or more, at December 31, 2017, are as follows (in thousands):

	Operating leases
2018	$ 492
2019	41
Future minimum lease payments	$ 533

At December 31, 2017, there were no material unrecorded unconditional purchase commitments or obligations in excess of one year.

Under the Insurance Agreement of the Reserve Banks, each of the Reserve Banks has agreed to bear, on a per-incident basis, a share of certain losses in excess of 1 percent of the capital paid-in of the claiming Reserve Bank, up to 50 percent of the total capital paid-in of all Reserve Banks. Losses are borne in the ratio of a Reserve Bank's capital paid-in to the total capital paid-in of all Reserve Banks at the beginning of the calendar year in which the loss is shared. No claims were outstanding under the agreement at December 31, 2017 and 2016.

The Bank is 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 legal actions and claims will be resolved without material adverse effect on the financial position or results of operations of the Bank.

(8) RETIREMENT AND THRIFT PLANS

Retirement Plans

The Bank currently offers three defined benefit retirement plans to its 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).[1] Under the Dodd-Frank Act, newly hired Bureau employees are eligible to participate in the System Plan and, during the years ended December 31, 2017 and 2016, certain costs associated with the System Plan were reimbursed by the Bureau. 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 Banks (SERP).

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. The Bank reports the net cost related to the BEP and SERP as a component of "Operating expenses: Salaries and benefits" in its Statements of Operations and reports the net liability as a component of "Accrued benefit costs" in its Statements of Condition.

The Bank's projected benefit obligation, funded status, and net pension expenses for the BEP and the SERP at December 31, 2017 and 2016, and for the years then ended, were immaterial.

Thrift Plan

Employees of the Bank participate in the defined contribution Thrift Plan for Employees of the Federal Reserve System (Thrift Plan). The Bank matches 100 percent of the first 6 percent of employee contributions from the date of hire and provides an automatic employer contribution of 1 percent of eligible pay. The Bank's Thrift Plan contributions totaled $6 million and $5 million for the years ended December 31, 2017 and 2016, respectively, and are reported as a component of "Operating expenses: Salaries and benefits" in the Statements of Operations.

[1] The OEB was established by the System to administer selected System benefit plans.

(9) POSTRETIREMENT BENEFITS OTHER THAN RETIREMENT PLANS AND POSTEMPLOYMENT BENEFITS

Postretirement Benefits Other Than Retirement Plans

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

The Bank and plan participants fund benefits payable under the medical and life insurance plans as due and the plans have no assets.

Following is a reconciliation of the beginning and ending balances of the benefit obligation for the years ended December 31, 2017 and 2016 (in millions):

	2017	2016
Accumulated postretirement benefit obligation at January 1	$ 105.3	$ 103.8
Service cost benefits earned during the period	3.5	3.2
Interest cost on accumulated benefit obligation	4.4	4.3
Net actuarial loss	1.5	0.5
Contributions by plan participants	2.0	2.0
Benefits paid	(6.9)	(6.5)
Medicare Part D subsidies	0.3	0.4
Plan amendments	(4.2)	(2.4)
Accumulated postretirement benefit obligation at December 31	$ 105.9	$ 105.3

At December 31, 2017 and 2016, the weighted-average discount rate assumptions used in developing the postretirement benefit obligation were 3.59 percent and 4.07 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. The System Plan discount rate assumption setting convention uses an unrounded rate.

Following is a reconciliation of the beginning and ending balance of the plan assets, and the unfunded postretirement benefit obligation and accrued postretirement benefit costs for the years ended December 31, 2017 and 2016 (in millions):

	2017	2016
Fair value of plan assets at January 1	$ -	$ -
Contributions by the employer	4.6	4.1
Contributions by plan participants	2.0	2.0
Benefits paid	(6.9)	(6.5)
Medicare Part D subsidies	0.3	0.4
Fair value of plan assets at December 31	$ -	$ -
Unfunded obligation and accrued postretirement benefit cost	$ 105.9	$ 105.3
Amounts included in accumulated other comprehensive loss are shown below:		
Prior service cost	$ 5.9	$ 2.2
Net actuarial loss	(16.5)	(15.8)
Total accumulated other comprehensive loss	$ (10.6)	$ (13.6)

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

For measurement purposes, the assumed health-care cost trend rates at December 31, 2017 and 2016 are provided in the table below:

	2017	2016
Health-care cost trend rate assumed for next year	6.20%	6.60%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	4.75%	4.75%
Year that the rate reaches the ultimate trend rate	2022	2022

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, 2017 (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	$ 0.5	$ (1.1)
Effect on accumulated postretirement benefit obligation	6.9	(12.0)

The following is a summary of the components of net periodic postretirement benefit expense for the years ended December 31, 2017 and 2016 (in millions):

	2017	2016
Service cost-benefits earned during the period	$ 3.5	$ 3.2
Interest cost on accumulated benefit obligation	4.4	4.4
Amortization of prior service cost	(0.4)	0.1
Amortization of net actuarial loss	0.7	0.2
Net periodic postretirement benefit expense	$ 8.2	$ 7.9

Estimated amounts that will be amortized from accumulated other comprehensive loss into net periodic postretirement benefit expense in 2018 are shown below:

Prior service cost	$	(1.3)
Net actuarial loss		0.8
Total	$	(0.5)

Net postretirement benefit costs are actuarially determined using a January 1 measurement date. At January 1, 2017 and 2016, the weighted-average discount rate assumptions used to determine net periodic postretirement benefit costs were 4.07 percent and 4.31 percent, respectively.

Net periodic postretirement benefit expense is reported as a component of "Operating expenses: Salaries and benefits" in the Statements of Operations.

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 Bank's 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 the actuarial loss in the accumulated postretirement benefit obligation and net periodic postretirement benefit expense.

During 2017, the Bank adopted an amendment to the health benefits program that eliminated the Aetna Golden Medicare Plan (Health Maintenance Organization) effective January 1, 2018. The plan amendment resulted in a change in the Bank's accumulated postretirement benefit obligation in the amount of $4.2 million as of December 31, 2017, with an equivalent change in the prior service component of accumulated other comprehensive income.

During 2016, the Reserve Banks adopted an amendment to their health benefits program that added a Medicare Advantage and Prescription Drug (MAPD) plan to the program effective January 1, 2017. The MAPD plan is a fully insured product that combines into one integrated benefit Medicare and Medicare Supplement coverages, as well as prescription drug coverage. The plan amendment resulted in a change in the Bank's accumulated postretirement benefit obligation in the amount of $2.4 million as of December 31, 2016, with an equivalent change in the prior service component of accumulated other comprehensive income.

Federal Medicare Part D subsidy receipts were $261 thousand and $351 thousand in the years ended December 31, 2017 and 2016, respectively. Expected receipts in 2018, related to benefits paid in the years ended December 31, 2017 and 2016, are $82 thousand and $32 thousand, respectively.

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

	Without subsidy		With subsidy	
2018	$	4.9	$	4.7
2019		5.1		4.8
2020		5.3		5.0
2021		5.5		5.1
2022		5.7		5.4
2023 - 2027		32.3		30.2
Total	$	58.8	$	55.2

Postemployment Benefits

The Bank offers benefits to former qualifying or inactive employees. Postemployment benefit costs are actuarially determined using a December 31 measurement date and include the cost of providing disability; medical, dental, and vision insurance; and survivor income benefits. The accrued postemployment benefit costs recognized by the Bank at December 31, 2017 and 2016 were $5.3 million and $5.5 million, respectively. This cost is included as a component of "Accrued benefit costs" in the Statements of Condition. Net periodic postemployment benefit expense (credit) included in 2017 and 2016 operating expenses were $432 thousand and ($469) thousand, respectively, and are recorded as a component of "Operating expenses: Salaries and benefits" in the Statements of Operations.

(10) ACCUMULATED OTHER COMPREHENSIVE INCOME AND OTHER COMPREHENSIVE INCOME

Following is a reconciliation of beginning and ending balances of accumulated other comprehensive income (loss) as of December 31, 2017 and 2016 (in millions):

	2017	2016
	Amount related to postretirement benefits other than retirement plans	Amount related to postretirement benefits other than retirement plans
Balance at January 1	$ (13.6)	$ (15.8)
Change in funded status of benefit plans:		
Prior service costs arising during the year	4.2	2.4
Amortization of prior service cost	(0.4) [1]	0.1 [1]
Change in prior service costs related to benefit plans	3.8	2.5
Net actuarial loss arising during the year	(1.5)	(0.5)
Amortization of net actuarial loss	0.7 [1]	0.2 [1]
Change in actuarial loss related to benefit plans	(0.8)	(0.3)
Change in funded status of benefit plans - other comprehensive income	3.0	2.2
Balance at December 31	$ (10.6)	$ (13.6)

[1] Reclassification is reported as a component of "Operating expenses: Salaries and benefits" in the Statements of Operations.

Additional detail regarding the classification of accumulated other comprehensive loss is included in Note 9.

(11) BUSINESS RESTRUCTURING CHARGES

In 2014, the Treasury announced a plan to consolidate the number of Reserve Banks providing fiscal agent services to the Treasury from 10 to 4. As a result of this initiative, the Government Entity Accounting and Reporting System and Treasury Collection Management and Monitoring operations performed by the Federal Reserve Bank of Philadelphia were transitioned to the Federal Reserve Bank of St. Louis in 2015. The Post Payment System and related Treasury Software Quality Assurance functions were transitioned to the Federal Reserve Bank of Kansas City in 2017. The remaining Treasury function is expected to be decommissioned by the end of 2019.

The Bank had no business restructuring charges in 2017 and 2016.

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

	2015 and prior restructuring plans
Information related to restructuring plans as of December 31, 2017:	
Total expected costs related to restructuring activity	$ 2.2
Expected completion date	2014
Reconciliation of liability balances:	
Balance at December 31, 2015	$ 2.4
Adjustments	(0.2)
Payments	(0.2)
Balance at December 31, 2016	$ 2.0
Adjustments	(0.3)
Payments	(0.3)
Balance at December 31, 2017	$ 1.4

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 “Operating expenses: Salaries and benefits” in the Statements of Operations.

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 Statements of Operations.

(12) RECONCILIATION OF TOTAL DISTRIBUTION OF COMPREHENSIVE INCOME

In accordance with the Federal Reserve Act, the Bank remits excess earnings to the Treasury after providing for the cost of operations, payment of dividends, and reservation of an amount necessary to maintain surplus at the Bank’s allocated portion of the $10 billion aggregate surplus limitation, which was $568 million and $538 million for the years ending December 31, 2017 and 2016, respectively.

The following table presents the distribution of the Bank’s and System total comprehensive income for the years ended December 31, 2017 and 2016 (in millions):

	Bank’s portion		System total	
	2017	2016	2017	2016
Net income before providing for remittances to Treasury	$ 2,108	$ 2,323	$ 80,692	$ 92,361
Other comprehensive income (loss)	3	2	651	(183)
Comprehensive income - available for distribution	$ 2,111	$ 2,325	$ 81,343	$ 92,178
Distribution of comprehensive income (loss):				
Transfer to (from) surplus	$ 30	$ (12)	$ -	$ -
Dividends	43	37	784	711
Earnings remittances to the Treasury	2,038	2,300	80,559	91,467
Total distribution of comprehensive income	$ 2,111	$ 2,325	$ 81,343	$ 92,178

(13) SUBSEQUENT EVENTS

The following subsequent event took place after the balance sheet date but was not present at the balance sheet date. In accordance with FASB ASC Topic 855 *Subsequent Events*, the Bank’s 2017 financial statements were not updated for the impact of this event.

Effective February 9, 2018, the Bipartisan Budget Act of 2018 (Budget Act) reduced the statutory limit on aggregate Reserve Bank surplus from $10 billion to $7.5 billion, which required the Reserve Banks to make a lump-sum payment to the Treasury in the amount of $2.5 billion. The Bank’s share of this remittance was $142 million. The payment was remitted to the Treasury on February 22, 2018. Reserve Bank surplus is allocated among Reserve Banks as described in Note 3(m). After making the transfer required by the Budget Act, the Bank’s allocated portion of the aggregate $7.5 billion surplus is $426 million.

There were no other subsequent events that required adjustments to or disclosures in the financial statements as of December 31, 2017. Subsequent events were evaluated through March 8, 2018, which is the date that the financial statements were available to be issued.

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