The Federal Reserve Banks

Combined Financial Statements as of and for the Years Ended December 31, 2013 and 2012 and Independent Auditors' Report

THE FEDERAL RESERVE BANKS
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INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying combined financial statements of the Federal Reserve Banks (the "Reserve Banks"), which are comprised of the combined statements of condition as of December 31, 2013 and 2012, and the related combined statements of income and comprehensive income, and changes in capital for the years then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Combined Financial Statements

Management is responsible for the preparation and fair presentation of these combined financial statements in accordance with accounting principles established by the Board of Governors of the Federal Reserve System (the "Board") as described in Note 3 to the combined financial statements; this includes determining that the basis of accounting established by the Board is an acceptable basis for the preparation of the combined financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the combined financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these combined financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the preparation and fair presentation of the combined financial statements of the Federal Reserve Banks' in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Federal Reserve Banks' internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the combined financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of the Reserve Banks as of December 31, 2013 and 2012, and the results of their operations for the years then ended in accordance with the basis of accounting described in Note 3 to the combined financial statements.

Basis of Accounting

We draw attention to Note 3 to the combined financial statements, which describes the basis of accounting. The Division of Reserve Bank Operations and Payment Systems has prepared these combined financial statements in conformity with accounting principles established by the Board, as set forth in the *Financial Accounting Manual for Federal Reserve Banks*, which is a basis of accounting other than accounting principles generally accepted in the United States of America. The effects on the combined financial statements of the differences between the accounting principles established by the Board and accounting principles generally accepted in the United States of America are also described in Note 3 to the combined financial statements. Our opinion is not modified with respect to this matter.

Deloitte & Touche LLP

March 14, 2014

FEDERAL RESERVE BANKS

Abbreviations:

ABS	Asset-backed securities
ACH	Automated clearinghouse
AIG	American International Group, Inc.
ASC	Accounting Standards Codification
ASU	Accounting Standards Update
BEP	Benefit Equalization Retirement Plan
Bureau	Bureau of Consumer Financial Protection
CDO	Collateralized debt obligation
CDS	Credit default swaps
CIP	Committee on Investment Performance (related to System Retirement Plan)
CMBS	Commercial mortgage-backed securities
FAM	*Financial Accounting Manual for Federal Reserve Banks*
FASB	Financial Accounting Standards Board
Fannie Mae	Federal National Mortgage Association
Freddie Mac	Federal Home Loan Mortgage Corporation
FOMC	Federal Open Market Committee
FRBA	Federal Reserve Bank of Atlanta
FRBC	Federal Reserve Bank of Cleveland
FRBNY	Federal Reserve Bank of New York
FRBSF	Federal Reserve Bank of San Francisco
GAAP	Accounting principles generally accepted in the United States of America
GSE	Government-sponsored enterprise
IMF	International Monetary Fund
JPMC	JPMorgan Chase & Co.
LLC	Limited liability company
MBS	Mortgage-backed securities
ML	Maiden Lane LLC
ML II	Maiden Lane II LLC
ML III	Maiden Lane III LLC
MTM	Mark-to-market
OFR	Office of Financial Research
RMBS	Residential mortgage-backed securities
SBA	Small Business Administration
SDR	Special drawing rights
SERP	Supplemental Retirement Plan for Select Officers of the Federal Reserve Banks
SOMA	System Open Market Account
STRIPS	Separate Trading of Registered Interest and Principal Securities
TALF	Term Asset-Backed Securities Loan Facility
TBA	To be announced
TDF	Term Deposit Facility
TRS	Total return swap
VIE	Variable interest entity

FEDERAL RESERVE BANKS
COMBINED STATEMENTS OF CONDITION
As of December 31, 2013 and December 31, 2012
(in millions)

	2013	2012
ASSETS		
Gold certificates	$ 11,037	$ 11,037
Special drawing rights certificates	5,200	5,200
Coin	1,955	2,108
Loans:		
Depository institutions	74	70
Term Asset-Backed Securities Loan Facility (measured at fair value)	98	560
System Open Market Account:		
Treasury securities, net (of which $17,153 and $9,139 is lent as of December 31, 2013 and 2012, respectively)	2,359,434	1,809,188
Government-sponsored enterprise debt securities, net (of which $1,099 and $697 is lent as of December 31, 2013 and 2012, respectively)	59,122	79,479
Federal agency and government-sponsored enterprise mortgage-backed securities, net	1,533,860	950,321
Foreign currency denominated investments, net	23,724	24,873
Central bank liquidity swaps	272	8,889
Accrued interest receivable	23,493	19,031
Other investments	2	23
Investments held by consolidated variable interest entities (of which $1,774 and $2,266 is measured at fair value as of December 31, 2013 and 2012, respectively)	1,926	2,750
Bank premises and equipment, net	2,653	2,676
Items in process of collection	165	216
Other assets	1,134	713
Total assets	$ 4,024,149	$ 2,917,134
LIABILITIES AND CAPITAL		
Federal Reserve notes outstanding, net	$ 1,197,920	$ 1,126,661
System Open Market Account:		
Securities sold under agreements to repurchase	315,924	107,188
Other liabilities	1,331	3,177
Consolidated variable interest entities:		
Beneficial interest in consolidated variable interest entities (measured at fair value)	116	803
Other liabilities (of which $73 and $71 is measured at fair value as of December 31, 2013 and 2012, respectively)	158	415
Deposits:		
Depository institutions	2,249,070	1,491,045
Treasury, general account	162,399	92,720
Other deposits	34,150	33,903
Interest payable to depository institutions	99	199
Accrued benefit costs	1,823	3,964
Deferred credit items	1,127	702
Accrued remittances to Treasury	4,791	1,407
Other liabilities	227	230
Total liabilities	3,969,135	2,862,414
Capital paid-in	27,507	27,360
Surplus (including accumulated other comprehensive loss of $2,556 and $4,845 at December 31, 2013 and 2012, respectively)	27,507	27,360
Total capital	55,014	54,720
Total liabilities and capital	$ 4,024,149	$ 2,917,134

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

FEDERAL RESERVE BANKS
COMBINED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

For the years ended December 31, 2013 and December 31, 2012
(in millions)

	2013	2012
INTEREST INCOME		
Loans:		
Term Asset-Backed Securities Loan Facility	$ 6	$ 80
System Open Market Account:		
Treasury securities, net	51,591	46,416
Government-sponsored enterprise debt securities, net	2,166	2,626
Federal agency and government-sponsored enterprise mortgage-backed securities, net	36,628	31,429
Foreign currency denominated assets, net	96	139
Central bank liquidity swaps	22	241
Other investments	-	9
Investments held by consolidated variable interest entities	6	1,110
Total interest income	90,515	82,050
INTEREST EXPENSE		
System Open Market Account:		
Securities sold under agreements to repurchase	60	142
Beneficial interest in consolidated variable interest entities	-	153
Deposits:		
Depository institutions	5,212	3,871
Term Deposit Facility	11	4
Total interest expense	5,283	4,170
Net interest income	85,232	77,880
NON-INTEREST INCOME		
System Open Market Account:		
Treasury securities gains, net	-	13,255
Federal agency and government-sponsored enterprise mortgage-backed securities gains, net	51	241
Foreign currency translation losses, net	(1,257)	(1,116)
Consolidated variable interest entities:		
Investments held by consolidated variable interest entities gains, net	183	7,451
Beneficial interest in consolidated variable interest entities gains (losses), net	1	(2,345)
Income from services	441	449
Reimbursable services to government agencies	530	506
Other	76	35
Total non-interest income	25	18,476
OPERATING EXPENSES		
Salaries and benefits	3,225	3,084
Occupancy	314	314
Equipment	169	193
Other	563	597
Assessments:		
Board of Governors operating expenses and currency costs	1,282	1,212
Bureau of Consumer Financial Protection	563	385
Office of Financial Research	-	2
Total operating expenses	6,116	5,787
Net income before providing for remittances to Treasury	79,141	90,569
Earnings remittances to Treasury	79,633	88,418
Net (loss) income	(492)	2,151
Change in prior service costs related to benefit plans	97	171
Change in actuarial gains (losses) related to benefit plans	2,192	(224)
Total other comprehensive income (loss)	2,289	(53)
Comprehensive income	$ 1,797	$ 2,098

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

FEDERAL RESERVE BANKS
COMBINED STATEMENTS OF CHANGES IN CAPITAL
For the years ended December 31, 2013 and December 31, 2012
(in millions, except share data)

		Surplus			
	Capital paid-in	Net income retained	Accumulated other comprehensive loss	Total surplus	Total capital
Balance at December 31, 2011 (537,984,621 shares)	$ 26,899	$ 31,691	$ (4,792)	$ 26,899	$ 53,798
Net change in capital stock issued (9,210,524 shares)	461	-	-	-	461
Comprehensive income:					
Net income	-	2,151	-	2,151	2,151
Other comprehensive loss	-	-	(53)	(53)	(53)
Dividends on capital stock	-	(1,637)	-	(1,637)	(1,637)
Net change in capital	461	514	(53)	461	922
Balance at December 31, 2012 (547,195,145 shares)	$ 27,360	$ 32,205	$ (4,845)	$ 27,360	$ 54,720
Net change in capital stock issued (2,941,791 shares)	147	-	-	-	147
Comprehensive income:					
Net loss	-	(492)	-	(492)	(492)
Other comprehensive income	-	-	2,289	2,289	2,289
Dividends on capital stock	-	(1,650)	-	(1,650)	(1,650)
Net change in capital	147	(2,142)	2,289	147	294
Balance at December 31, 2013 (550,136,936 shares)	$ 27,507	$ 30,063	$ (2,556)	$ 27,507	$ 55,014

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

FEDERAL RESERVE BANK
NOTES TO COMBINED FINANCIAL STATEMENTS

1. STRUCTURE

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

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

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

2. OPERATIONS AND SERVICES

The Reserve Banks perform a variety of services and operations. These functions include participating in formulating and conducting monetary policy; participating in the payment system, including large-dollar transfers of funds, automated clearinghouse (ACH) operations, and check collection; distributing coin and currency; performing fiscal agency functions for the U.S. Department of the Treasury (Treasury), certain federal agencies, and other entities; serving as the federal government's bank; providing short-term loans to depository institutions; providing loans to 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, and designated financial market utilities pursuant to authority delegated by the Board of Governors. Certain services are provided to foreign and international monetary authorities, primarily by the FRBNY.

The FOMC, in conducting monetary policy, establishes policy regarding domestic open market operations, oversees these operations, and issues authorizations and directives to the FRBNY to execute transactions. The FOMC authorizes and directs the FRBNY to conduct operations in domestic markets, including the direct purchase and sale of Treasury securities, 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 System Open Market Account (SOMA). The FRBNY is authorized and directed to lend the Treasury securities and GSE debt securities that are held in the SOMA.

To counter disorderly conditions in foreign exchange markets or to meet other needs specified by the FOMC to carry out the System's central bank responsibilities, the FOMC has authorized and directed the FRBNY to execute spot and forward foreign exchange transactions in 14 foreign currencies, to hold balances in those currencies, and to invest such foreign currency holdings, while maintaining adequate liquidity. The FOMC has also authorized 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 to warehouse foreign currencies for the Treasury and the Exchange Stabilization Fund in the maximum amount of $5 billion.

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 establish temporary U.S. dollar liquidity swap lines with the Bank of Canada, the Bank of England, the European Central Bank, the Bank of Japan, and the Swiss National Bank. In addition, as a contingency measure, the FOMC authorized and directed the FRBNY to establish temporary foreign currency liquidity swap arrangements with these five central banks to allow for the System to access liquidity, if necessary, in any of the foreign central banks' currencies. On October 31, 2013, the Federal Reserve and these five central banks agreed to convert their existing temporary liquidity swap arrangements to standing agreements which will remain in effect until further notice.

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 between the Reserve Banks. In some cases, costs incurred by a Reserve Bank for services provided to other Reserve Banks are not shared; in other cases, the Reserve Banks are reimbursed for costs incurred in providing services to other Reserve Banks.

3. 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 combined financial statements have been prepared in accordance with the FAM.

Limited differences exist between the accounting principles and practices in the FAM and accounting principles generally accepted in the United States of America (GAAP), due to the unique nature of the Reserve Banks' powers and responsibilities as part of the nation's central bank and given the System's unique responsibility to conduct monetary policy. The primary 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 Reserve Banks' 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 motivated by monetary policy objectives rather than profit. Accordingly, fair values, earnings, and gains or losses resulting from the sale of such securities and currencies are incidental to 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. The cost bases of Treasury securities, GSE debt securities, and foreign government debt instruments are adjusted for amortization of premiums or accretion of discounts on a straight-line basis, rather than using the interest method required by GAAP.

In addition, the Reserve Banks do not present a Combined Statement of Cash Flows as required by GAAP because the liquidity and cash position of the Reserve Banks are not a primary concern given the Reserve Banks' unique powers and responsibilities as a central bank. Other information regarding the Reserve Banks' activities is provided in, or may be derived from, the Combined Statements of Condition, Income and Comprehensive Income, and Changes in Capital, and the accompanying notes to the combined financial statements. Other than those described above, there are no significant differences between the policies outlined in the FAM and GAAP.

Preparing the combined financial statements in conformity with the FAM requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the combined financial statements, and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

In 2013, the description of certain line items presented in the Combined Statements of Income and Comprehensive Income and the Combined Statements of Condition have been revised to better reflect the nature of these items. Amounts related to these line items were not changed from the prior year, only the nomenclature for the line item was revised, as further noted below:

- The line item, "Accrued interest on Federal Reserve notes," has been revised in the Combined Statements of Condition to "Accrued remittances to Treasury."

- The line item, "Net income before interest on Federal Reserve notes expense remitted to Treasury," has been revised in the Combined Statements of Income and Comprehensive Income to "Net income before providing for remittances to Treasury."

- The line item, "Interest on Federal Reserve notes expense remitted to Treasury," has been revised in the Combined Statements of Income and Comprehensive Income to "Earnings remittances to Treasury."

Certain amounts relating to the prior year have been reclassified in the Combined Statements of Condition to conform to the current year presentation. The amount reported as "System Open Market Account: Accrued interest receivable" for the year ended December 31, 2012 ($19,031 million) was previously reported as a component of "System Open Market Account: Foreign currency denominated assets, net" ($99 million) and "Accrued interest receivable" ($18,932 million).

Certain immaterial amounts relating to the prior year have been reclassified in the Combined Statements of Income and Comprehensive Income to conform to the current year presentation. $34 million previously reported for the year ended December 31, 2012 as "Non-interest income: Term Asset-Back Securities Loan Facility, unrealized losses" have been reclassified to "Non-interest income: Other," and $25 million previously reported as "Operating expenses: Professional fees related to consolidated variable interest entities" have been reclassified to "Operating expenses: Other."

Significant accounts and accounting policies are explained below.

a. *Consolidation*

The combined financial statements include the accounts and results of operations of the Reserve Banks as well as several variable interest entities (VIEs), which include Maiden Lane LLC (ML), Maiden Lane II LLC (ML II), Maiden Lane III LLC (ML III), and TALF LLC. The consolidation of the VIEs was assessed in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 810 (ASC 810) *Consolidation*, which requires a VIE to be consolidated by its controlling financial interest holder. Intercompany balances and transactions have been eliminated in consolidation. See Note 6 for additional information on the VIEs. The combined financial statements of the Reserve Banks also include accounts and results of operations of Maiden and Nassau LLC, a Delaware limited liability company (LLC) wholly-owned by the Bank, which was formed to own and operate the 33 Maiden Lane building, which was purchased on February 28, 2012.

A Reserve Bank consolidates a VIE if it has a controlling financial interest, which is defined as the power to direct the significant economic activities of the entity and the obligation to absorb losses or the right to receive benefits of the entity that could potentially be significant to the VIE. To determine whether it is the controlling financial interest holder of a VIE, the Reserve Bank evaluates the VIE's design, capital structure, and relationships with the variable interest holders. The Reserve Bank reconsiders whether it has a controlling financial interest in a VIE, as required by ASC 810, at each reporting date or if there is an event that requires consideration.

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. Section 152 of the Dodd-Frank Act established the Office of Financial Research (OFR) within the Treasury and required the Board of Governors to fund the OFR for the two-year period ended July 21, 2012. The Reserve Banks reviewed the law and evaluated the design of and their relationships to the Bureau and the OFR and determined that neither should be consolidated in the Reserve Banks' comibined 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 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 twelve 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 Banks at original cost. There were no SDR certificate transactions during the years ended December 31, 2013 and 2012.

c. *Coin*

The amount reported as coin in the Combined Statements of Condition represents the face value of all United States coin held by the Reserve Banks. The Reserve Banks buy 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.

The FRBNY has elected the fair value option for all Term Asset-Backed Securities Loan Facility (TALF) loans in accordance with ASC 825. Recording all TALF loans at fair value, rather than at the remaining principal amount outstanding, provides the most appropriate presentation on the financial statements by matching the change in fair value of TALF loans, the related put agreement with TALF LLC, and the valuation of the beneficial interests in TALF LLC. Information regarding the TALF LLC's assets and liabilities is presented in Note 6. Unrealized losses on TALF loans that are recorded at fair value are reported as a component of "Non-interest income: Other" in the Combined Statements of Income and Comprehensive Income. The interest income on TALF loans is recognized based on the contracted rate and is reported as "Interest Income: Term Asset-Backed Securities Loan Facility" in the Combined Statements of Income and Comprehensive Income.

Loans, other than those recorded at fair value, are impaired when current information and events indicate that it is probable that the Reserve Banks 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 Reseve Banks have 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 Reserve Banks 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 Reserve Banks discontinue recording interest on an impaired loan, cash payments are first applied to principal until the loan balance is reduced to zero; subsequent payments are applied as recoveries of amounts previously deemed uncollectible, if any, and then as interest income.

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

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

The FRBNY may engage in purchases of securities with primary dealers under agreements to resell (repurchase transactions). These repurchase transactions are settled through a tri-party arrangement. In a tri-party arrangement, two commercial custodial banks manage the collateral clearing, settlement, pricing, and pledging, and provide cash and securities custodial services for and on behalf of the FRBNY and counterparty. 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 transactions primarily includes Treasury securities (including Treasury Inflation-Protected Securities and Separate Trading of Registered Interest and Principal of

Securities (STRIPS) Treasury securities); direct obligations of several federal and GSE-related agencies, including Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac), and Federal Home Loan Banks; and pass-through federal agency and GSE MBS. The repurchase transactions are accounted for as financing transactions with the associated interest income recognized over the life of the transaction. These transactions 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 Combined Statements of Condition.

The FRBNY may engage in sales of securities under agreements to repurchase (reverse repurchase transactions) with primary dealers and with the set of expanded counterparties which includes banks, savings associations, GSEs, and domestic money market funds. These reverse repurchase transactions, when arranged as open market operations, are settled through a tri-party arrangement, similar to repurchase transactions. Reverse repurchase transactions 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, and federal agency and GSE MBS that are held in the SOMA. Reverse repurchase transactions are accounted for as financing transactions, and the associated interest expense is recognized over the life of the transaction. These transactions are reported at their contractual amounts as "System Open Market Account: Securities sold under agreements to repurchase" and the related accrued interest payable is reported as a component of "Other liabilities" in the Combined Statements of Condition.

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 "Treasury securities, net" and "Government-sponsored enterprise debt securities, net," as appropriate, in the Combined Statements of Condition. Securities lending transactions are fully collateralized by Treasury securities that have fair values in excess of the securities lent. The FRBNY charges the primary dealer a fee for borrowing securities, and these fees are reported as a component of "Non-interest income: Other" in the Combined Statements of Income and Comprehensive Income.

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

f. ***Treasury Securities; Government-Sponsored Enterprise Debt Securities; Federal Agency and Government-Sponsored Enterprise Mortgage-Backed Securities; Foreign Currency Denominated Assets; and Warehousing Agreements***

Interest income on Treasury securities, GSE debt securities, and foreign currency denominated assets included in the SOMA is accrued on a straight-line basis. Interest income on federal agency and GSE MBS is accrued using the interest method and includes amortization of premiums, accretion of discounts, and 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 Combined Statements of Condition and interest income on those securities is reported net of the amortization of premiums and accretion of discounts in the Combined Statements of Income and Comprehensive Income.

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, 2013 and 2012, the FRBNY executed dollar rolls primarily to facilitate settlement of outstanding purchases of federal agency and GSE MBS. The FRBNY accounts for dollar rolls as purchases or sales on a settlement-date basis. In addition, TBA MBS transactions may be paired off or assigned prior to settlement. Net gains resulting from these MBS transactions are reported as "Non-interest income: System Open Market Account: Federal agency and government-sponsored enterprise mortgage-backed securities gains, net" in the Combined Statements of Income and Comprehensive Income.

Foreign currency denominated assets, which can include foreign currency deposits, securities purchased under agreements to resell, and government debt instruments, are revalued daily at current foreign currency market exchange rates in order to report these assets in U.S. dollars. Foreign currency translation gains and losses that result from the daily revaluation of foreign currency denominated assets are reported as "Non-interest income: System Open Market Account: Foreign currency translation losses, net" in the Combined Statements of Income and Comprehensive Income.

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 assets, including the premiums, discounts, and realized and unrealized gains and losses, is allocated to each Reserve Bank based on the ratio of each Reserve Bank's capital and surplus to the Reserve Banks' aggregate capital and surplus at the preceding December 31.

Warehousing is an arrangement under which the FOMC has approved the exchange, at the request of the Treasury, of U.S. dollars for foreign currencies held by the Treasury over a limited period. The purpose of the warehousing facility is to supplement the U.S. dollar resources of the Treasury for financing purchases of foreign currencies and related international operations. Warehousing agreements are valued daily at current market exchange rates. Activity related to these agreements is allocated to each Reserve Bank based on the ratio of each Reserve Bank's capital and surplus to the Reserve Banks' aggregate capital and surplus at the preceding December 31.

The FRBNY is authorized to hold foreign currency working balances and execute foreign exchange contracts to facilitate international payments and currency transactions it makes on behalf of foreign central bank and U.S. official institution customers. These foreign currency working balances and contracts are not related to the FRBNY's monetary policy operations. Foreign currency working balances are reported as a component of "Other assets" in the Combined Statements of Condition and the related foreign currency translation gains and losses that result from the daily revaluation of the foreign currency working balances and contracts are reported as a component of "Non-interest income: Other" in the Combined Statements of Income and Comprehensive Income.

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 the ratio of each Reserve Bank's capital and surplus to aggregate capital and surplus at the preceding December 31. The foreign currency amounts associated with these central bank liquidity swap arrangements are revalued daily at current foreign currency market exchange rates.

U.S. dollar liquidity swaps

At the initiation of each U.S. dollar liquidity swap transaction, the foreign central bank transfers a specified amount of its currency to a restricted account for the FRBNY in exchange for U.S. dollars at the prevailing market exchange rate. Concurrent with this transaction, the FRBNY and the foreign central bank agree to a second transaction that obligates the foreign central bank to return the U.S. dollars and the FRBNY to return the foreign currency on a specified future date at the same exchange rate as the initial transaction. The foreign currency amounts that the FRBNY acquires are reported as "System Open Market Account: Central bank liquidity swaps" in the Combined 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 FRBNY recognizes compensation during the term of the swap transaction, which is reported as "Interest income: System Open Market Account: Central bank liquidity swaps" in the Combined Statements of Income and Comprehensive Income.

Foreign currency liquidity swaps

The structure of foreign currency liquidity swap transactions involves the transfer by the FRBNY, at the prevailing market exchange rate, of a specified amount of U.S. dollars to an account for the foreign central bank in exchange for its currency. The foreign currency amount received would be reported as a liability by the Reserve Banks.

h. *Investments Held by Consolidated Variable Interest Entities*

The investments held by consolidated VIEs consist primarily of cash and cash equivalents, short-term investments with maturities of greater than three months and less than one year, commercial mortgage loans, and swap contracts. Investments are reported as "Investments held by consolidated variable interest entities" in the Combined Statements of Condition. These investments are accounted for and classified as follows:

- ML's investments in debt securities are accounted for in accordance with FASB ASC Topic 320 (ASC 320*) Investments – Debt and Equity Securities*, and ML elected the fair value option for all eligible assets and liabilities in accordance with ASC 825. Other financial instruments, including swap contracts in ML, are recorded at fair value in accordance with FASB ASC Topic 815 (ASC 815) *Derivatives and Hedging*.

- ML II and ML III qualify as nonregistered investment companies under the provisions of FASB ASC Topic 946 (ASC 946) *Financial Services – Investment Companies*, and therefore, all investments are recorded at fair value in accordance with ASC 946.

- TALF LLC follows the guidance in ASC 320 when accounting for any acquired asset-backed securities (ABS) investments and has elected the fair value option for all eligible assets in accordance with ASC 825.

i. *Bank Premises, Equipment, and Software*

Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, which range from 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.

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 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.

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 Reseve Banks' 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 securities sold under agreements to repurchase 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 Combined Statements of Condition represents the Reserve Banks' Federal Reserve notes outstanding, reduced by the Reserve Banks' currency holdings of $203 billion and $228 billion at December 31, 2013 and 2012, respectively.

At December 31, 2013 and 2012, all Federal Reserve notes outstanding, reduced by the Reserve Banks' currency holdings, were fully collateralized. At December 31, 2013, all gold certificates, all special drawing rights certificates, and $1,182 billion of domestic securities held in the SOMA were pledged as collateral. At December 31, 2013, no investments denominated in foreign currencies were pledged as collateral.

k. *Beneficial Interest in Consolidated Variable Interest Entities*

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

l. *Deposits*

Depository Institutions

Depository institutions' deposits represent the reserve and service-related balances in the accounts that depository institutions hold at the Reserve Banks. The interest rates paid on required reserve balances and excess balances are determined by the Board of Governors, based on an FOMC-established target range for the federal funds rate. Interest payable is reported as a component of "Interest payable to depository institutions" in the Combined 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 payable is reported as a component of "Interest payable to depository institutions" in the Combined Statements of Condition. There were no deposits held by the Reserve Banks under the TDF at December 31, 2013 and 2012.

Treasury

The Treasury general account is the primary operational account of the Treasury and is held at the FRBNY.

Other

Other deposits include foreign central bank and foreign government deposits held at the FRBNY. Other deposits also include GSE deposits held by the Reserve Banks.

m. *Items in Process of Collection and Deferred Credit Items*

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

n. *Capital Paid-in*

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

By law, each Reserve Bank is required to pay each member bank an annual dividend of six percent on the paid-in capital stock. This cumulative dividend is paid semiannually.

o. *Surplus*

The Board of Governors requires the Reserve Banks to maintain a surplus equal to the amount of capital paid-in. On a daily basis, surplus is adjusted to equate the balance to capital paid-in. Accumulated other comprehensive income is reported as a component of "Surplus" in the Combined Statements of Condition and the Combined Statements of Changes in Capital. Additional information regarding the classifications of accumulated other comprehensive income is provided in Notes 9, 10, and 11.

p. ***Remittances to Treasury***

The Board of Governors requires the Reserve Banks to transfer excess earnings to the Treasury as interest on Federal Reserve notes after providing for the costs of operations, payment of dividends, and reservation of an amount necessary to equate surplus with capital paid-in. Currently, remittances to Treasury are made on a weekly basis. This amount is reported as "Earnings remittances to Treasury" in the Combined Statements of Income and Comprehensive Income. The amount due to the Treasury is reported as "Accrued remittances to Treasury" in the Combined Statements of Condition. See Note 13 for additional information on remittances to Treasury.

If earnings during the year are not sufficient to provide for the costs of operations, payment of dividends, and equating surplus and capital paid-in, remittances to the Treasury are suspended. A deferred asset is recorded that represents the amount of net earnings a Reserve Bank will need to realize before remittances to the Treasury resume. This deferred asset is periodically reviewed for impairment.

q. ***Income and Costs Related to Treasury Services***

When directed by the Secretary of the Treasury, the Reserve Banks are required by the Federal Reserve Act to serve as fiscal agent and depositary of the United States Government. By statute, the Treasury has appropriations to pay for these services. During the years ended December 31, 2013 and 2012, the Bank was reimbursed for all services provided to the Treasury as its fiscal agent.

r. ***Assessments***

The Board of Governors assesses the Reserve Banks to fund its operations, the operations of the Bureau and, for a two-year period following the July 21, 2010 effective date of the Dodd-Frank Act, the OFR. 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 date of 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 Governors' 2009 annual report, which totaled $4.98 billion. The fixed percentage of total operating expenses of the System for the years ended December 31, 2013 and 2012 was 12 percent ($597.6 million) and 11 percent ($547.8 million), respectively. After 2013, the amount will be adjusted in accordance with the provisions of the Dodd-Frank Act. The Reserve Banks' assessment for Bureau funding is reported as "Assessments: Bureau of Consumer Financial Protection" in the Combined Statements of Income and Comprehensive Income.

The Board of Governors assessed the Reserve Banks to fund the operations of the OFR for the two-year period ended July 21, 2012, following enactment of the Dodd-Frank Act; thereafter, the OFR is funded by fees assessed on bank holding companies and nonbank financial companies that meet the criteria specified in the Dodd-Frank Act.

s. ***Fair Value***

Certain assets and liabilities reported on the Reserve Banks' Combined Statements of Condition are measured at fair value in accordance with ASC 820, including TALF loans, investments and beneficial interests of the consolidated VIEs, and assets of the Retirement Plan for Employees of the System. 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 Reserve Banks' 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 Reserve Banks' 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.

The inputs or methodology used for valuing assets and liabilities are not necessarily an indication of the risk associated with those assets and liabilities.

t. ***Taxes***

The Reserve Banks are exempt from federal, state, and local taxes, except for taxes on real property. The Reserve Banks' real property taxes were $48 million and $47 million for the years ended December 31, 2013 and 2012, respectively, and are reported as a component of "Operating expenses: Occupancy" in the Combined Statements of Income and Comprehensive Income.

u. ***Restructuring Charges***

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

Note 12 describes the Reserve Banks' restructuring initiatives and provides information about the costs and liabilities associated with employee separations and contract terminations. The costs associated with the impairment of certain Reserve Banks' assets are discussed in Note 7. 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 and discussed in Note 9. Costs and liabilities associated with enhanced postretirement benefits are discussed in Note 10.

v. ***Recently Issued Accounting Standards***

In December 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-11, *Balance Sheet* (Topic 210): *Disclosures about Offsetting Assets and Liabilities*. This update requires a reporting entity to present enhanced disclosures for financial instruments and derivative instruments that are offset or subject to master netting agreements or similar such agreements. In January 2013, the FASB issued ASU 2013-01, *Balance Sheet* (Topic 210): *Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*. This update clarifies that the scope of ASU 2011-11 applies to derivatives accounted for in accordance with Topic 815. These updates are effective for the Reserve Banks for the year ended December 31, 2013, and the required disclosures are included in Note 6.

In December 2011, the FASB issued ASU 2011-12, *Comprehensive Income* (Topic 220): *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05*. This update indefinitely deferred the requirements of ASU 2011-05, which required an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective net income line items. Subsequently, in February 2013, the FASB issued ASU 2013-02, *Comprehensive Income* (Topic 220): *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income,* which established an effective date for the requirements of ASU 2011-05 related to reporting of significant reclassification adjustments from accumulated other comprehensive income. This update improves the transparency of changes in other comprehensive income and items reclassified out of accumulated other comprehensive income in the combined financial statements. These presentation requirements of ASU 2011-05 and required disclosures in ASU 2013-02 are effective for the Reserve Banks for the year ending December 31, 2013, and are reflected in the Bank's 2013 combined financial statements and Note 11.

In April 2013, the FASB issued ASU 2013-07, *Presentation of Financial Statements* (Topic 205): *Liquidation Basis of Accounting*. This update clarifies when entities in liquidation should apply the liquidation basis of accounting and provides guidance on financial statement presentation. This update is effective for an entity that determines liquidation is imminent during annual reporting periods beginning after December 15, 2013. During 2012, ML II and ML III sold their remaining portfolio assets; however, the financial statement presentations for ML II and ML III were not modified to the liquidation basis as the standard does not apply to entities whose liquidation follows a plan for liquidation that was specified in the entity's governing documents at inception.

In June 2013, the FASB issued ASU 2013-08, *Financial Services – Investment Companies* (Topic 946): *Amendments to the Scope, Measurement, and Disclosure Requirements*. This update changes the assessment of whether an entity is an investment company by developing a new two-tiered approach for that assessment, which requires an entity to possess certain fundamental characteristics while allowing judgment in assessing other typical characteristics. This update, which is applicable to ML II and ML III, is effective for the Bank for the year ending December 31, 2014 and is not expected to have a material effect on the Reserve Banks' combined financial statements.

4. LOANS

Loans to Depository Institutions

The Reserve Banks offers primary, secondary, and seasonal loans to eligible borrowers, and each program has its own interest rate. Interest is accrued using the applicable interest rate established at least every 14 days by the Reserve Banks' 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 each Reserve 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; ABS; corporate bonds; commercial paper; and bank-issued assets, such as certificates of deposit, bank notes, and deposit notes. Collateral is assigned a lending value that is deemed appropriate by each Reserve 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 Reserve 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 remaining maturity distribution of loans to depository institutions outstanding as of December 31, 2013, and 2012, was as follows (in millions):

	Within 15 days	16 days to 90 days	Total
December 31, 2013	$ 69	$ 5	$ 74
December 31, 2012	$ 67	$ 3	$ 70

At December 31, 2013 and 2012, the Reserve Banks 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, 2013 and 2012.

TALF

The TALF assisted financial markets in accommodating the credit needs of consumers and businesses of all sizes by facilitating the issuance of ABS collateralized by a variety of consumer and business loans. Each TALF loan had an original maturity of three years, except loans secured by Small Business Administration (SBA) Pool Certificates, loans secured by SBA Development Company Participation Certificates, or ABS backed by student loans or commercial mortgage loans, which had an original maturity of five years if the borrower so elected. The loans are secured by eligible collateral, with the FRBNY having lent an amount equal to the value of the collateral, as determined by the FRBNY, less a margin.

The TALF loans were extended on a nonrecourse basis. If the borrower does not repay the loan, the FRBNY will enforce its rights in the collateral and may sell the collateral to TALF LLC, a Delaware LLC, established for the purpose of purchasing such assets. As of December 31, 2013, the FRBNY has not enforced its rights to the collateral because there have been no defaults.

Pursuant to a put agreement with the FRBNY, TALF LLC has committed to purchase assets that secure a TALF loan at a price equal to the principal amount outstanding plus accrued but unpaid interest, regardless of the fair value of the collateral. Funding for TALF LLC's purchases of these securities is derived first through the fees received by TALF LLC from the FRBNY for this commitment and any interest earned on its investments. In the event that such funding proved insufficient for the asset purchases that TALF LLC has committed to make under the put agreement, the Treasury originally committed to lend up to $20 billion, and on March 25, 2009, the Treasury funded $100 million. In addition to the Treasury's commitment, the FRBNY originally committed to lend up to $180 billion to TALF LLC if it needed the funding to purchase assets pursuant to the put agreement and provided that the Treasury had fully funded its commitment. Subsequently, the Treasury and FRBNY commitments to lend to TALF LLC were eliminated, because the cash equivalents and short-term investments held by TALF LLC exceeded the remaining amount of TALF loans outstanding, and the credit protection from the Treasury was no longer deemed necessary. The TALF remains a joint Treasury-Federal Reserve program, and the Treasury and Federal Reserve will continue to consult on the administration of the program.

TALF LLC has repaid in full the outstanding principal and accrued interest on the initial funding previously provided by the Treasury. The Board of Governors has also authorized TALF LLC to begin distributions from the accumulated fees and income earned by TALF LLC since inception to the Treasury and the FRBNY in the amount by which such accumulated fees and income exceeds the current outstanding TALF loan balance plus funds reserved for future expenses of TALF LLC. Treasury receives 90 percent of the distributions and the FRBNY receives 10 percent.

As of December 31, 2013, TALF loans were classified within Level 2 of the valuation hierarchy. TALF loans were transferred from Level 3 to Level 2 because they were valued at December 31, 2013 using model-based techniques for which all significant inputs were considered observable (Level 2). Previously, TALF loans were valued using significant unobservable inputs (level 3).

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

	2013	2012
Level 2	$ 98	$ -
Level 3	-	560
Total fair value	$ 98	$ 560

The following table presents a reconciliation of TALF loans measured at fair value using significant unobservable inputs (Level 3) during the years ended December 31, 2013 and 2012 (in millions):

	TALF loans
Fair value at December 31, 2011	$ 9,059
Loan repayments and prepayments	(8,465)
Total realized and unrealized gains (losses)	(34)
Fair value at December 31, 2012	$ 560
Gross transfers out[1]	(560)
Fair value at December 31, 2013	$ -

[1] The amount of transfers is based on fair values of the transferred assets at the beginning of the reporting period.

The fair value of TALF loans reported in the Combined Statements of Condition as of December 31, 2013 and 2012, includes $1 million and $3 million in unrealized gains, respectively. The FRBNY attributes substantially all changes in fair value of loans to changes in instrument-specific credit spreads.

Eligible collateral includes U.S. dollar-denominated ABS that are backed by student loans, insurance premium financial loans, or commercial mortgage loans. The following table presents the collateral concentration and remaining maturity distribution measured at fair value as of December 31, 2013 and 2012 (in millions):

	Time to maturity			
Collateral type[1]	Within 90 days	91 days to 1 year	Over 1 year to 5 years	Total
December 31, 2013:				
Student loan	$ -	$ 14	$ 33	$ 47
CMBS	-	51	-	51
Total	$ -	$ 65	$ 33	$ 98
December 31, 2012:				
Student loan	$ -	$ -	$ 382	$ 382
CMBS	3	-	129	132
Other[2]	46	-	-	46
Total	$ 49	$ -	$ 511	$ 560

[1] All credit ratings are AAA unless otherwise indicated.
[2] Includes insurance premium financial loans.

The aggregate remaining principal amount outstanding on TALF loans as of December 31, 2013 and 2012, was $97 million and $556 million, respectively.

At December 31, 2013 and 2012, no TALF loans were over 90 days past due or on nonaccrual status.

Earnings reported by the FRBNY related to the TALF include interest income and unrealized gains and losses on TALF loans as well as the FRBNY's allocated share of the TALF LLC's net income. Additional information regarding the income of TALF LLC is presented in Note 6. The following table presents the components of TALF earnings recorded by the FRBNY for the years ended December 31 (in millions):

	2013	2012
Interest income	$ 6	$ 80
Unrealized gains (losses)	(3)	(34)
Subtotal - TALF loans	$ 3	$ 46
Allocated share of TALF LLC	-	(7)
Total TALF	$ 3	$ 39

5. SYSTEM OPEN MARKET ACCOUNT

a. *Domestic Securities Holdings*

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

During the years ended December 31, 2013 and 2012, the FRBNY continued the purchase of Treasury securities and federal agency and GSE MBS under the large-scale asset purchase programs authorized by the FOMC. In September 2011, the FOMC announced that the Federal Reserve would reinvest principal payments from the SOMA portfolio holdings of GSE debt securities and federal agency and GSE MBS in federal agency and GSE MBS. In June 2012, the FOMC announced that it would continue the existing policy of reinvesting principal payments from the SOMA portfolio holdings of GSE debt securities and federal agency and GSE MBS in federal agency and GSE MBS. In September 2012, the FOMC announced that the Federal Reserve would purchase additional federal agency and GSE MBS at a pace of $40 billion per month. In December 2012, the FOMC announced that the Federal Reserve would purchase longer-term Treasury securities initially at a pace of $45 billion per month after its program to extend the average maturity of its holdings of Treasury securities was completed at the end of 2012. In December 2012, the FOMC announced that the Federal Reserve would continue the policy of rolling over maturing Treasury securities into new issues at auction.

During the year ended December 31, 2012, the FRBNY also continued the purchase and sale of SOMA portfolio holdings under the maturity extension programs authorized by the FOMC. In September 2011, the FOMC announced that the Federal Reserve would extend the average maturity of the SOMA portfolio holdings of securities by purchasing $400 billion par value of Treasury securities with maturities of six to thirty years and selling or redeeming an equal par amount of Treasury securities with remaining maturities of three years or less by the end of June 2012. In June 2012, the FOMC announced that the Federal Reserve would continue through the end of 2012 its program to extend the average maturity of securities by purchasing $267 billion par value of Treasury securities with maturities of six to thirty years and selling or redeeming an equal par amount of Treasury securities with maturities of three and a quarter years or less by the end of 2012.

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

	2013			
	Par	Unamortized premiums	Unaccreted discounts	Total amortized cost
Notes	$ 1,467,427	$ 33,385	$ (5,697)	$ 1,495,115
Bonds	741,348	128,541	(5,570)	864,319
Total Treasury securities	$ 2,208,775	$ 161,926	$ (11,267)	$ 2,359,434
GSE debt securities	$ 57,221	$ 1,903	$ (2)	$ 59,122
Federal agency and GSE MBS	$ 1,490,162	$ 44,781	$ (1,083)	$ 1,533,860

	2012			
	Par	Unamortized premiums	Unaccreted discounts	Total amortized cost
Notes	$ 1,110,398	$ 32,532	$ (711)	$ 1,142,219
Bonds	555,747	111,360	(138)	666,969
Total Treasury securities	$ 1,666,145	$ 143,892	$ (849)	$ 1,809,188
GSE debt securities	$ 76,783	$ 2,703	$ (7)	$ 79,479
Federal agency and GSE MBS	$ 926,662	$ 24,367	$ (708)	$ 950,321

The FRBNY enters into transactions for the purchase of securities under agreements to resell and transactions to sell securities under agreements to repurchase as part of its monetary policy activities. In addition, transactions to sell securities under to repurchase agreements are entered into as part of a service offering to foreign official and international account holders.

There were no material transactions related to securities purchased under agreements to resell during the years ended December 31, 2013 and 2012. Financial information related to securities sold under agreements to repurchase for the years ended December 31 was as follows (in millions):

	2013	2012
Contract amount outstanding, end of year	$ 315,924	$ 107,188
Average daily amount outstanding, during the year	99,681	91,898
Maximum balance outstanding, during the year	315,924	122,541
Securities pledged (par value), end of year	310,452	93,547
Securities pledged (market value), end of year	314,901	107,188

The remaining maturity distribution of Treasury securities, GSE debt securities, federal agency and GSE MBS bought outright, and securities sold under agreements to repurchase at December 31, 2013 and 2012 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, 2013:							
Treasury securities (par value)	$ -	$ 298	$ 176	$ 763,329	$ 864,700	$ 580,272	$ 2,208,775
GSE debt securities (par value)	2,310	7,568	8,666	36,268	62	2,347	57,221
Federal agency and GSE MBS (par value)[1]	-	-	-	5	2,549	1,487,608	1,490,162
Securities sold under agreements to repurchase (contract amount)	315,924	-	-	-	-	-	315,924
December 31, 2012:							
Treasury securities (par value)	$ -	$ 5	$ 16	$ 378,476	$ 862,410	$ 425,238	$ 1,666,145
GSE debt securities (par value)	1,565	2,795	15,202	52,830	2,044	2,347	76,783
Federal agency and GSE MBS (par value)[1]	-	-	2	1	2,365	924,294	926,662
Securities sold under agreements to repurchase (contract amount)	107,188	-	-	-	-	-	107,188

[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 6.5 and 3.3 years as of December 31, 2013 and 2012, respectively.

The amortized cost and par value of Treasury securities and GSE debt securities that were loaned from the SOMA at December 31 was as follows (in millions):

	2013	2012
Treasury securities (amortized cost)	$ 17,153	$ 9,139
Treasury securities (par value)	15,447	8,460
GSE debt securities (amortized cost)	1,099	697
GSE debt securities (par value)	1,055	676

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, 2013, there were no outstanding commitments.

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, 2013, the total purchase price of the federal agency and GSE MBS under outstanding purchase commitments was $59,350 million, of which $479 million was related to dollar rolls. As of December 31, 2013, there were no outstanding sales commitments for federal agency and GSE MBS. These commitments, which had contractual settlement dates extending through February 2014, 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. These 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 commitments as part of the risk management practices used to mitigate the counterparty credit risk.

Other investments consist of cash and short-term investments related to the federal agency and GSE MBS portfolio. Other liabilities, which are related to federal agency and GSE MBS purchases and sales, includes 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 includes obligations that arise from the failure of a seller to deliver securities to the FRBNY on the settlement date. Although the FRBNY has ownership of and records its investments in the MBS as of the contractual settlement date, it is not obligated to make payment until the securities are delivered, and the amount included in other liabilities represents the obligation to pay for the securities when delivered. The amount of other investments and other liabilities held in the SOMA at December 31 was as follows (in millions):

	2013	2012
Other investments	$ 2	$ 23
Other liabilities:		
Cash margin	$ 1,320	$ 3,092
Obligations from MBS transaction fails	11	85
Total other liabilities	$ 1,331	$ 3,177

Accrued interest receivable on domestic securities holdings was $23,405 million and $18,924 million as of December 31, 2013 and 2012, respectively. These amounts are reported as a component of "System Open Market Account: Accrued interest receivable" in the Combined Statements of Condition.

Information about transactions related to Treasury securities, GSE debt securities, and federal agency and GSE MBS during the years ended December 31, 2013 and 2012, is summarized as follows (in millions):

	Bills	Notes	Bonds	Total Treasury securities	GSE debt securities	Federal agency and GSE MBS
Balance at December 31, 2011	$ 18,423	$1,311,917	$ 419,937	$1,750,277	$ 107,828	$ 848,258
Purchases[1]	118,886	397,999	263,991	780,876	-	431,487
Sales[1]	-	(507,420)	(11,727)	(519,147)	-	-
Realized gains, net[2]	-	12,003	1,252	13,255	-	-
Principal payments and maturities	(137,314)	(67,462)	-	(204,776)	(27,211)	(324,181)
Amortization of premiums and accretion of discounts, net	5	(5,461)	(7,531)	(12,987)	(1,138)	(5,243)
Inflation adjustment on inflation-indexed securities	-	643	1,047	1,690	-	-
Balance at December 31, 2012	$ -	$1,142,219	$ 666,969	$1,809,188	$ 79,479	$ 950,321
Purchases[1]	-	358,656	206,208	564,864	-	864,538
Sales[1]	-	-	-	-	-	-
Realized gains, net[2]	-	-	-	-	-	-
Principal payments and maturities	-	(21)	-	(21)	(19,562)	(273,991)
Amortization of premiums and accretion of discounts, net	-	(6,024)	(9,503)	(15,527)	(795)	(7,008)
Inflation adjustment on inflation-indexed securities	-	285	645	930	-	-
Balance at December 31, 2013	$ -	$1,495,115	$ 864,319	$2,359,434	$ 59,122	$1,533,860
Year-ended December 31, 2012						
Supplemental information - par value of transactions:						
Purchases[3]	$ 118,892	$ 383,106	$ 205,115	$ 707,113	$ -	$ 413,160
Sales[3]	-	(492,234)	(9,094)	(501,328)	-	-
Year-ended December 31, 2013						
Supplemental information - par value of transactions:						
Purchases[3]	$ -	$ 356,766	$ 184,956	$ 541,722	$ -	$ 837,490
Sales[3]	-	-	-	-	-	-

[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, net offset 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 assets in the SOMA.

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

Information about foreign currency denominated investments valued at amortized cost and foreign currency market exchange rates at December 31 was as follows (in millions):

	2013	2012
Euro:		
Foreign currency deposits	$ 7,530	$ 8,925
Securities purchased under agreements to resell	2,549	659
German government debt instruments	2,397	2,133
French government debt instruments	2,397	2,421
Japanese yen:		
Foreign currency deposits	2,926	3,553
Japanese government debt instruments	5,925	7,182
Total	$ 23,724	$ 24,873

Accrued interest receivable on foreign currency denominated assets was $88 million and $99 million as of December 31, 2013 and 2012, respectively. These amounts are reported as a component of "System Open Market Account: Accrued interest receivable" in the Combined Statements of Condition.

The remaining maturity distribution of foreign currency denominated investments at December 31, 2013 and 2012, was as follows (in millions):

	Within 15 days	16 days to 90 days	91 days to 1 year	Over 1 year to 5 years	Total
December 31, 2013:					
Euro	$ 7,037	$ 1,803	$ 2,161	$ 3,872	$ 14,873
Japanese yen	3,116	380	1,870	3,485	8,851
Total	$ 10,153	$ 2,183	$ 4,031	$ 7,357	$ 23,724
December 31, 2012:					
Euro	$ 6,593	$ 1,726	$ 2,151	$ 3,668	$ 14,138
Japanese yen	3,801	490	2,138	4,306	10,735
Total	$ 10,394	$ 2,216	$ 4,289	$ 7,974	$ 24,873

There were no foreign exchange contracts related to open market operations outstanding as of December 31, 2013.

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, 2013, there were no outstanding commitments to purchase foreign government debt instruments During 2013, there were purchases, sales, and maturities of foreign government debt instruments of $3,539 million, $0, and $3,431 million, respectively.

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 daily monitoring procedures.

At December 31, 2013 and 2012, there was no balance outstanding under the authorized warehousing facility.

There were no transactions related to the authorized reciprocal currency arrangements with the Bank of Canada and the Bank of Mexico during the years ended December 31, 2013 and 2012.

Foreign currency working balances held and foreign exchange contracts executed by the Bank to facilitate its international payments and currency transactions it made on behalf of foreign central banks and U.S. official institution customers were not material as of December 31, 2013 and 2012.

c. *Central Bank Liquidity Swaps*

U.S. Dollar Liquidity Swaps

The total foreign currency held under U.S. dollar liquidity swaps in the SOMA at December 31, 2013 and 2012, was $272 million and $8,889 million, respectively.

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

	2013			2012		
	Within 15 days	16 days to 90 days	Total	Within 15 days	16 days to 90 days	Total
Euro	$ 113	$ 159	$ 272	$ 1,741	$ 7,147	$ 8,888
Japanese yen	-	-	-	1	-	1
Total	$ 113	$ 159	$ 272	$ 1,742	$ 7,147	$ 8,889

Foreign Currency Liquidity Swaps

There were no transactions related to the foreign currency liquidity swaps during the years ended December 31, 2013 and 2012.

d. *Fair Value of SOMA Assets*

The fair value amounts below are presented solely for informational purposes. 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.

The fair value of the Treasury securities, GSE debt securities, federal agency and GSE MBS, and foreign government debt instruments in the SOMA's holdings 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, 2013, there are no credit impairments of SOMA securities holdings.

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

	2013			2012		
	Amortized cost	Fair value	Cumulative unrealized gains (losses)	Amortized cost	Fair value	Cumulative unrealized gains (losses)
Treasury securities:						
Notes	$ 1,495,115	$ 1,499,000	$ 3,885	$ 1,142,219	$ 1,213,177	$ 70,958
Bonds	864,319	842,336	(21,983)	666,969	761,138	94,169
Total Treasury securities	**$ 2,359,434**	**$ 2,341,336**	**$ (18,098)**	**$ 1,809,188**	**$ 1,974,315**	**$ 165,127**
GSE debt securities	59,122	62,236	3,114	79,479	85,004	5,525
Federal agency and GSE MBS	1,533,860	1,495,572	(38,288)	950,321	993,990	43,669
Total domestic SOMA portfolio securities holdings	**$ 3,952,416**	**$ 3,899,144**	**$ (53,272)**	**$ 2,838,988**	**$ 3,053,309**	**$ 214,321**
Memorandum - Commitments for:						
Purchases of Treasury securities	$ -	$ -	$ -	$ -	$ -	$ -
Purchases of Federal agency and GSE MBS	59,350	59,129	(221)	118,215	118,397	182
Sales of Federal agency and GSE MBS	-	-	-	-	-	-

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.

At December 31, 2013 and 2012, the fair value of foreign currency denominated investments, was $23,802 million and $25,042 million, respectively. The fair value of 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 and securities purchased under agreements to resell was determined by reference to market interest rates.

The cost basis of securities purchased under agreements to resell, securities sold under agreements to repurchase, and other investments held in the SOMA approximate fair value.

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

	2013		2012	
Distribution of MBS holdings by coupon rate	Amortized cost	Fair value	Amortized cost	Fair value
Total SOMA:				
2.0%	$ 14,191	$ 13,529	$ 845	$ 846
2.5%	123,832	118,458	37,562	37,766
3.0%	521,809	484,275	160,613	161,757
3.5%	349,689	338,357	179,587	184,752
4.0%	230,256	231,113	137,758	145,955
4.5%	185,825	195,481	262,485	282,182
5.0%	83,290	87,968	125,107	132,213
5.5%	21,496	22,718	39,970	41,819
6.0%	3,051	3,225	5,642	5,888
6.5%	421	448	752	812
Total	$ 1,533,860	$ 1,495,572	$ 950,321	$ 993,990

Because SOMA securities are recorded at amortized cost, the change in the cumulative unrealized gains (losses) is not reported in the Combined Statements of Income and Comprehensive Income. The following table presents the realized gains and the change in the cumulative unrealized gains (losses), presented as "Fair value changes unrealized losses," of the domestic securities holdings during the years ended December 31, 2013 and 2012 (in millions):

	2013		2012	
	Total portfolio holdings realized gains[1]	Fair value changes unrealized losses	Total portfolio holdings realized gains[1]	Fair value changes unrealized losses
Treasury securities	$ -	$ (183,225)	$ 13,255	$ (1,142)
GSE debt securities	-	(2,411)	-	(885)
Federal agency and GSE MBS	51	(81,957)	241	(3,568)
Total	$ 51	$ (267,593)	$ 13,496	$ (5,595)

[1] Total portfolio holdings realized gains are reported in "Non-interest income (loss): System Open Market Account" in the Combined Statements of Income and Comprehensive Income.

The amount of change in unrealized gains position, net, related to foreign currency denominated assets was a decrease of $90 million and an increase of $3 million for the years ended December 31, 2013 and 2012, respectively.

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. INVESTMENTS HELD BY CONSOLIDATED VARIABLE INTEREST ENTITIES

a. *Summary Information for Consolidated Variable Interest Entities*

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

	2013	2012
ML	$ 1,732	$ 1,811
ML II	63	61
ML III	22	22
TALF LLC	109	856
Total	$ 1,926	$ 2,750

The FRBNY's approximate maximum exposure to loss at December 31, 2013 and 2012, was $1,089 million and $829 million, respectively. These estimates incorporate potential losses associated with assets recorded on the FRBNY's balance sheet, net of the fair value of subordinated interests (beneficial interest in consolidated VIEs).

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

	2013	2012
Assets:		
Short-term investments	$ 530	$ 690
Commercial mortgage loans	507	466
Swap contracts	158	408
Non-agency RMBS	8	2
Other investments[1]	2	66
Subtotal	$ 1,205	$ 1,632
Cash, cash equivalents, accrued interest receivable, and other receivables	721	1,118
Total investments held by consolidated VIEs	$ 1,926	$ 2,750
Liabilities:		
Beneficial interest in consolidated VIEs	$ 116	$ 803
Other liabilities[2]	$ 158	$ 415

[1] Investments with a fair value of $1 million as of December 31, 2012 were recategorized from "Federal agency and GSE MBS" to "Other investments" to conform to the current year presentation.
[2] The amount reported as "Consolidated variable interest entities: Other liabilities" in the Combined Statements of Condition includes $82 million and $341 million related to cash collateral received on swap contracts at December 31, 2013 and 2012, respectively. The amount also includes accrued interest and accrued other expenses.

Total realized and unrealized gains (losses) for the year ended December 31, 2013, were as follows (in millions):

	Total portfolio holdings realized gains (losses)	Fair value changes unrealized gains (losses)	Total portfolio holdings realized/unrealized gains (losses)
Commercial mortgage loans[1]	$ 28	$ 176	$ 204
Swap contracts	83	(136)	(53)
Non-agency RMBS	10	1	11
Residential mortgage loans[1]	(1)	1	-
CDOs	2	(2)	-
Other investments	9	12	21
Total	$ 131	$ 52	$ 183

[1] Substantially all unrealized gains (losses) on the commercial mortgage loans are attributable to changes in instrument-specific credit risk.

Total realized and unrealized gains (losses) for the year ended December 31, 2012, were as follows (in millions):

	Total portfolio holdings realized gains (losses)	Fair value changes unrealized gains (losses)	Total portfolio holdings realized/unrealized gains (losses)
Short-term investments	$ -	$ 2	$ 2
Commercial mortgage loans[1]	(101)	394	293
Swap contracts	75	(165)	(90)
Non-agency RMBS	(334)	2,038	1,704
Residential mortgage loans[1]	(326)	322	(4)
CDOs	1,110	4,439	5,549
Other investments[2]	11	(14)	(3)
Total	$ 435	$ 7,016	$ 7,451

[1] Substantially all unrealized gains (losses) on the commercial and residential mortgage loans are attributable to changes in instrument-specific credit risk.
[2] Investments with realized gains of $12 million, unrealized losses of $13 million, and total realized/unrealized losses of $1 million as of December 31, 2012 were recategorized from "Federal agency and GSE MBS" to "Other investments" to conform to the current year presentation.

The net income (loss) attributable to ML, ML II, ML III, and TALF LLC for the year ended December 31, 2013, was as follows (in millions):

	ML	ML II	ML III	TALF LLC	Total
Interest income:					
Portfolio interest income	$ 2	$ 4	$ -	$ -	$ 6
Less: Interest expense	-	-	-	-	-
Net interest income	2	4	-	-	6
Non-interest income:					
Portfolio holdings gains, net	183	-	-	-	183
Realized losses on beneficial interest in consolidated VIEs	-	-	-	(573) [1]	(573)
Unrealized gains (losses) on beneficial interest in consolidated VIEs	-	(1)	-	574 [1]	573
Net non-interest income (loss)	183	(1)	-	1	183
Total net interest income and non-interest income	185	3	-	1	189
Less: Professional fees	6	1	-	1	8
Net income attributable to consolidated VIEs	$ 179	$ 2	$ -	$ - [2]	$ 181

[1] The TALF LLC's realized and unrealized loss on beneficial interest represents Treasury's financial interest in the net income of TALF LLC for the year ended December 31, 2013.

[2] Additional information regarding TALF-related income recorded by the FRBNY is presented in Note 4.

The net income (loss) attributable to ML, ML II, ML III, and TALF for the year ended December 31, 2012, was as follows (in millions):

	ML	ML II	ML III	TALF LLC	Total
Interest income:					
Portfolio interest income	$ 34	$ 52	$ 1,023	$ 1	$ 1,110
Less: Interest expense	45	7	97	4	153
Net interest income (loss)	(11)	45	926	(3)	957
Non-interest income:					
Portfolio holdings gains, net	553	1,392	5,506	-	7,451
Realized losses on beneficial interest in consolidated VIEs	-	(453)	(2,905)	- [1]	(3,358)
Unrealized gains (losses) on beneficial interest in consolidated VIEs	-	216	801	(4) [1]	1,013
Net non-interest income (loss)	553	1,155	3,402	(4)	5,106
Total net interest income and non-interest income (loss)	542	1,200	4,328	(7)	6,063
Less: Professional fees	13	1	11	-	25
Net income (loss) attributable to consolidated VIEs	$ 529	$ 1,199	$ 4,317	$ (7) [2]	$ 6,038

[1] The TALF LLC's realized and unrealized loss on beneficial interest represents Treasury's financial interest in the net income of TALF LLC for the year ended December 31, 2012.
[2] Additional information regarding TALF-related income recorded by the FRBNY is presented in Note 4.

Following is a summary of the consolidated VIEs' subordinated financial interest for the years ended December 31, 2013 and 2012 (in millions):

	ML subordinated loan	ML II deferred purchase price	ML III equity contribution	TALF financial interest	Total
Fair value, December 31, 2011	$ 1,385	$ 1,332	$ 6,350	$ 778	$ 9,845
Interest accrued and capitalized	45	7	97	4	153
Realized (gain) / loss	-	453	2,905	-	3,358
Unrealized (gain) / loss	-	(216)	(801)	4	(1,013)
Payments[1]	(1,430)	(1,566)	(8,544)	-	(11,540)
Fair value, December 31, 2012	$ -	$ 10	$ 7	$ 786	$ 803
Interest accrued and capitalized	$ -	$ -	$ -	$ -	$ -
Realized (gain) / loss	-	-	-	573	573
Unrealized (gain) / loss	-	1	-	(574)	(573)
Payments[1]	-	-	-	(687)	(687)
Fair value, at December 31, 2013	$ -	$ 11	$ 7	$ 98	$ 116

[1] For ML includes payments of $1,150 million of principal and $280 million of interest. For ML II includes payments of $1,000 million of principal, $113 million of interest, and $453 million of variable deferred purchase price. For ML III includes payments of $5,000 million of principal, $639 million of interest, and $2,905 million of excess amounts. For TALF LLC includes payments of $100 million of principal, $13 million of interest, and $574 million of contingent interest.

b. ***Maiden Lane LLC***

To facilitate the merger of The Bear Stearns Companies, Inc. (Bear Stearns) and JPMorgan Chase & Co. (JPMC), the FRBNY extended credit to ML in June 2008. ML is a Delaware LLC formed by the FRBNY to acquire certain assets of Bear Stearns and to manage those assets. The assets acquired by ML were valued at $29.9 billion as of March 14, 2008, the date that the FRBNYcommitted to the transaction, and largely consisted of federal agency and GSE MBS, non-agency residential mortgage-back securities (RMBS), commercial and residential mortgage loans, and derivatives and associated hedges.

The FRBNY extended a senior loan of approximately $28.8 billion and JPMC extended a subordinated loan of $1.15 billion to finance the acquisition of the assets. On June 14, 2012, the remaining outstanding balance of the senior loan from the FRBNY to ML was repaid in full, with interest. On November 15, 2012, the remaining outstanding balance of the subordinated loan from JPMC was repaid in full, with interest. The FRBNY will continue to sell the remaining assets from the ML portfolio as market conditions warrant and if the sales represent good value for the public. In accordance with the ML agreements, proceeds from future asset sales will be distributed to the FRBNY as contingent interest after all derivative instruments in ML have been terminated and paid or sold from the portfolio.

The following is a description of the significant holdings at December 31, 2013, and the associated risk for each holding:

i. *Debt Securities*

ML has investments in short-term instruments with maturities of greater than three months and less than one year when acquired. As of December 31, 2013, ML's short-term instruments consisted of approximately $530 million in U.S. Treasury bills.

ii. *Commercial Mortgage Loans*

Commercial mortgage loans are subject to a high degree of credit risk because of exposure to financial loss resulting from failure by a counterparty to meet its contractual obligations. Default rates are subject to a wide variety of factors, including, but not limited to, property performance, property management, supply and demand, construction trends, consumer behavior, regional economic conditions, interest rates, and other factors.

The performance profile for the commercial mortgage loans at December 31, 2013, was as follows (in millions):

	Unpaid principal balance	Fair value	Fair value as a percentage of unpaid principal balance
Commercial mortgage loans:			
Performing loans	$ 28	$ 28	99.6%
Non-performing / non-accrual loans [1]	512	479	93.5%
Total	$ 540	$ 507	93.8%

[1] Non-performing/non-accrual loans include loans with payments past due greater than 90 days.

Commercial mortgage loans held by ML are composed of different levels of subordination with respect to the underlying properties, and relative to each other. Senior mortgage loans are secured property loans evidenced by a first mortgage that is senior to any subordinate or mezzanine financing. Subordinate mortgage interests, sometimes known as B Notes, are loans evidenced by a junior note or a junior participation in a mortgage loan. Mezzanine loans are loans made to the direct or indirect owner of the property-owning entity. Mezzanine loans are not secured by a mortgage on the property but rather by a pledge of the mezzanine borrower's direct or indirect ownership interest in the property-owning entity. As of December 31, 2013, ML had unpaid principal balances of approximately $12 million in senior mortgage loans and $528 million in mezzanine loans.

As of December 31, 2013, the property types of commercial mortgage loans were concentrated in the office sector with one sponsor representing all of the total unpaid principal balance

iii. Derivative Instruments

Derivative contracts are instruments, such as swap contracts, that derive their value from underlying assets, indexes, reference rates, or a combination of these factors. The ML portfolio is composed of derivative financial instruments included in a total return swap (TRS) agreement with JPMC. ML and JPMC entered into the TRS with reference obligations representing credit default swaps (CDS) primarily on commercial mortgage-backed securities (CMBS) and RMBS, with various market participants, including JPMC.

On an ongoing basis, ML pledges collateral for credit or liquidity related shortfalls based on 20 percent of the notional amount of sold CDS protection and 10 percent of the present value of future premiums on purchased CDS protection. Failure to post this collateral constitutes a TRS event of default. Separately, ML and JPMC engage in bilateral posting of collateral to cover the net mark-to-market (MTM) variations in the swap portfolio. ML only nets the collateral received from JPMC from the bilateral MTM posting for the reference obligations for which JPMC is the counterparty.

The values of ML's cash equivalents, purchased by the re-hypothecation of cash collateral associated with the TRS, were $149 million and $477 million, for the years ended December 31, 2013 and 2012, respectively. In addition, ML has pledged $124 million and $231 million of US Treasury notes to JPMC as of December 31, 2013 and 2012, respectively.

The following risks are associated with the derivative instruments held by ML as part of the TRS agreement with JPMC:

Market Risk

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

Credit Risk

Credit risk is the risk of financial loss resulting from failure by a counterparty to meet its contractual obligations to ML. This can be caused by factors directly related to the counterparty, such as business or management. Taking collateral is the most common way to mitigate credit risk. ML takes financial collateral in the form of cash and marketable securities to cover JPMC counterparty risk as part of the TRS agreement with JPMC. ML remains exposed to credit risk for counterparties, other than JPMC, related to the swaps that underlie the TRS.

ML has entered into an International Swaps and Derivatives Association, Inc. master netting agreement with JPMC in connection with the TRS. This agreement provides ML with the right to liquidate securities held as collateral and to offset receivables and payables with JPMC in the event of default. This agreement also establishes the method for determining the net amount of receivables and payables that ML is entitled to receive from or owes to each counterparty to the swaps that underlie the TRS based upon the relevant fair value of the CDS.

For the derivative balances reported in the Combined Statements of Condition, ML offsets its asset and liability positions held with the same counterparty. In addition, ML offsets the cash collateral held with JPMC against any net liabilities of JPMC with ML under the TRS. As of December 31, 2013 and 2012, there were no amounts subject to an enforceable master netting agreement that were not offset in the Combined Statements of Condition.

The following table summarizes the fair value and notional amounts of derivative instruments by contract type on a gross basis as of December 31, 2013 and 2012, which is reported as a component of "Investments held by consolidated variable interest entities" in the Combined Statements of Condition (in millions, except contract data):

	2013			2012		
	Gross derivative assets	Gross derivative liabilities	Notional amounts[3]	Gross derivative assets	Gross derivative liabilities	Notional amounts[3]
Credit derivatives:						
CDS[1,2]	$ 345	$ (193)	$ 899	$ 816	$ (343)	$ 1,755
Amounts offset in the Combined Statements of Condition						
Counterparty netting	(120)	120		(272)	272	
Cash collateral	(67)	-		(136)	-	
Net amounts in the Combined Statements of Condition	$ 158	$ (73)		$ 408	$ (71)	

[1]CDS fair values as of December 31, 2013 for assets and liabilities include interest receivables of $15 million and payables of $2 million. CDS fair values as of December 31, 2012 for assets and liabilities includes interest receivables of $15 million and payables of $9 million.

[2]There were 269 and 470 CDS contracts outstanding as of December 31, 2013 and 2012, respectively.

[3]Represents the sum of gross long and gross short notional derivative contracts. The change in notional amounts is representative of the volume of activity for the year ended December 31, 2013.

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

	Maximum potential payout / notional							
	2013						2012	
	Years to maturity					Fair value		Fair value
Credit ratings of the reference obligation	1 year or less	After 1 year through 3 years	After 3 years through 5 years	After 5 years	Total	Asset / (liability)	Total	Asset / (liability)
Investment grade (AAA to BBB-)	$ -	$ -	$ -	$ 13	$ 13	$ (3)	$ 52	$ (5)
Non-investment grade (BB+ or lower)	-	-	-	293	293	(188)	438	(329)
Total credit protection sold	$ -	$ -	$ -	$ 306	$ 306	$ (191)	$ 490	$ (334)

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

	Maximum potential recovery / notional							
	2013						2012	
	Years to maturity					Fair value		Fair value
Credit ratings of the reference obligation	1 year or less	After 1 year through 3 years	After 3 years through 5 years	After 5 years	Total	Asset / (liability)	Total	Asset
Investment grade (AAA to BBB-)	$ -	$ -	$ 5	$ 51	$ 56	$ 2	$ 150	$ 27
Non-investment grade (BB+ or lower)	-	-	9	528	537	327	1,115	774
Total credit protection bought	$ -	$ -	$ 14	$ 579	$ 593	$ 329	$ 1,265	$ 801

Currency Risk

Currency risk is the risk of financial loss resulting from exposure to changes in exchange rates between two currencies. Under the terms of the TRS, JPMC may post cash collateral in the form of either U.S. dollar or Euro denominated currencies to cover the net MTM variation in the swap portfolio. Starting in December 2012, JPMC began posting collateral in Euro currency. This risk is mitigated by daily variation margin updates that capture the movement in the value of the swap portfolio in addition to any movement in exchange rates on the swap collateral. Swap collateral received that is denominated in a foreign currency is translated into U.S. dollar amounts using the prevailing exchange rate as of the date of the combined financial statements. There is no gain or loss associated with this foreign denominated collateral as the asset and liability positions associated with it are offsetting.

c. *Maiden Lane II LLC*

The FRBNY extended credit to ML II, a Delaware LLC formed to purchase non-agency RMBS from the reinvestment pool of the securities lending portfolios of several regulated U.S. insurance subsidiaries of American International Group, Inc. (AIG). ML II borrowed $19.5 billion from the FRBNY and used the proceeds to purchase non-agency RMBS that had an approximate fair value of $20.8 billion as of October 31, 2008, from AIG's domestic insurance subsidiaries. The FRBNY is the sole and managing member and the controlling party of ML II and will remain as the controlling party as long as the FRBNY retains an economic interest in ML II. As part of the agreement, the AIG subsidiaries also received from ML II a fixed deferred purchase price of up to $1.0 billion, plus interest on any such fixed deferred purchase price outstanding.

On February 28, 2012, the FRBNY announced the sale of the remaining securities in the ML II portfolio. On March 1, 2012, the loan from the FRBNY to ML II was repaid in full with interest, in accordance with the terms of the facility. On March 15, 2012, the remaining portion of the fixed deferred purchase price plus interest owed to the AIG subsidiaries was repaid in full. Concurrently, distributions were made to the Bank and the AIG subsidiaries in the form of contingent interest and variable deferred purchase price for the amounts of $2.3 billion and $0.5 billion, respectively.

On March 19, 2012, ML II was dissolved and the FRBNY began the wind up process in accordance with and as required by Delaware law and the agreements governing ML II. Winding up requires ML II to pay or make reasonable provision to pay all claims and obligations. Any remaining proceeds will be divided between the Bank, which is entitled to receive five-sixths, and the AIG subsidiaries, which are entitled to receive one-sixth. While its affairs are being wound up, the ML II is retaining certain assets to meet trailing expenses and other obligations as required by law. Dissolution costs are not expected to be material.

d. ***Maiden Lane III LLC***

The FRBNY extended credit to ML III, a Delaware LLC formed to purchase ABS CDOs from certain third-party counterparties of AIG Financial Products Corp. ML III borrowed approximately $24.3 billion from the FRBNY, and AIG provided an equity contribution of $5.0 billion to ML III. The proceeds were used to purchase ABS CDOs with a fair value of $29.6 billion. On April 3, 2012, the FRBNY revised ML III's investment objective to allow for asset sales and began conducting such sales shortly thereafter. On June 14, 2012, the FRBNY announced that its loan to ML III had been repaid in full, with interest. On July 16, 2012, the FRBY announced that net proceeds from additional sales of securities in ML III enabled the full repayment of AIG's equity contribution plus accrued interest and provided residual profits to the FRBNY and AIG. During 2012, distributions were made to the Bank and AIG in the form of contingent interest and excess amounts in the amounts of $5.9 billion and $2.9 billion, respectively. On August 23, 2012, the FRBNY announced that all remaining securities in ML III were sold.

On September 10, 2012, ML III was dissolved and the FRBNY began the wind up process in accordance with and as required by Delaware law and the agreements governing ML III. Winding up requires ML III to pay or make reasonable provision to pay all claims and obligations. Any remaining proceeds will be divided between the FRBNY, which is entitled to receive two-thirds, and AIG (or its assignee), which is entitled to receive one-third, in accordance with the agreement. While its affairs are being wound up, ML III is retaining certain assets to meet trailing expenses and other obligations as required by law. Dissolution costs are not expected to be material.

e. ***TALF LLC***

Cash receipts resulting from the put option fees paid to TALF LLC are invested in the following types of U.S. dollar-denominated short-term investments and cash equivalents eligible for purchase by the LLC: (1) U.S. Treasury securities, (2) federal agency securities that are senior, negotiable debt obligations of Fannie Mae, Freddie Mac, Federal Home Loan Banks, and Federal Farm Credit Banks, which have a fixed rate of interest, (3) repurchase agreements that are collateralized by Treasury and federal agency securities and fixed-rate agency mortgage-backed securities, and (4) money market mutual funds registered with the Securities and Exchange Commission and regulated under Rule 2a-7 of the Investment Company Act that invest exclusively in U.S. Treasury and federal agency securities. Cash may also be invested in a demand interest-bearing account held at The Bank of New York Mellon. Proceeds from the Treasury's loan were also invested in these short-term investments and cash equivalents until the outstanding principal on the loan was repaid in full as described below.

On January 15, 2013, the Treasury and FRBNY eliminated the Treasury's and FRBNY's funding commitments to TALF LLC. These commitments were no longer deemed necessary because the cash equivalents and short-term investments held by TALF LLC exceeded the amount of TALF loans then outstanding. In addition, the agreement related to distribution of proceeds was amended to limit funding of the cash collateral account to an amount equal to the outstanding principal plus accrued interest of all TALF loans as of the payment determination date; all accumulated funding in excess of that amount would then be distributed according to the distribution priorities described in the agreements governing TALF LLC.

Pursuant to this agreement on February 6, 2013, TALF LLC repaid in full the outstanding principal and accrued interest on the Treasury loan. During the year ended December 31, 2013, additional distributions were made to the Treasury and FRBNY as contingent interest in the amounts of $573 million and $64 million, respectively.

f. ***Fair Value Measurement***

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

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

i. Determination of Fair Value

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

Market quotations may not represent fair value in circumstances in which the investment manager believes that facts and circumstances applicable to an issuer, a seller, a purchaser, or the market for a particular security result in the current market quotations reflecting an inaccurate measure of fair value. In such cases or when market quotations are unavailable, the investment manager determines fair value by applying proprietary valuation models that use collateral performance scenarios and pricing metrics derived from the reported performance of the universe of investments with similar characteristics as well as the observable market.

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

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

ii. Valuation Methodologies for Level 3 Assets and Liabilities

In certain cases in which there is limited activity around inputs to the valuation, investments are classified within Level 3 of the valuation hierarchy. These valuations also incorporate pricing metrics derived from the reported performance of the universe of similar investments and from observations and estimates of market data. Because external price information is not available, market-based models are used to value these securities. Key inputs to the model may include market spreads or yield estimates for comparable instruments, performance data (i.e. prepayment rates, default rates, and loss severity), valuation estimates for underlying property collateral, projected cash flows, and other relevant contractual features. Because there is lack of observable pricing, some securities and investment loans that are carried at fair value are classified within Level 3.

For the CDS agreements, all of which are categorized as Level 3 assets and liabilities, there are various valuation methodologies. In each case, the fair value of the instrument underlying the swap is a significant input used to derive the fair value of the swap. When there are broker or dealer prices available for the underlying instruments, the fair value of the swap is derived based on those prices. When the instrument underlying the swap is a market index (i.e. CMBS index), the closing market index price, which can also be expressed as a credit spread, is used to determine the fair value of the swap. In the remaining cases, the fair value of the underlying instrument is principally based on inputs and assumptions not observable in the market (i.e. discount rates, prepayment rates, default rates, and recovery rates).

ML Inputs for Level 3 Assets and Liabilities

The following table presents the valuation techniques and ranges of significant unobservable inputs generally used to determine the fair values of ML's Level 3 assets and liabilities as of December 31, 2013 (in millions, except for input values):

Investment	Fair value	Principal valuation technique	Unobservable inputs	Range of input values			Weighted average[3]
Commercial mortgage loans	$ 507	Discounted cash flows	Discount rate	4%	-	13%	12%
			Property capitalization rate		7%		7%
			Net operating income growth rate	3%	-	5%	4%
CDS[1]	152	Discounted cash flows	Credit spreads[2]	2,259 bps	-	8,870 bps	6,299 bps
			Discount rate	5%	-	25%	15%
			Constant prepayment rate	0%	-	17%	3%
			Constant default rate	0%	-	30%	6%
			Loss severity	40%	-	95%	54%

[1] Swap assets and liabilities are presented net for the purposes of this table.
[2] Implied spread on closing market prices for index positions.
[3] Weighted averages are calculated based on the fair value of the respective instruments.

The following table presents the valuation techniques and ranges of significant unobservable inputs generally used to determine the fair values of ML's Level 3 assets and liabilities as of December 31, 2012 (in millions, except for input values):

Investment	Fair value	Principal valuation technique	Unobservable inputs	Range of input values	Weighted average[3]
Commercial mortgage loans	$ 466	Discounted cash flows	Discount rate	6% - 20%	14%
			Property capitalization rate	6% - 10%	7%
			Net operating income growth rate	3% - 7%	3%
CDS[1]	$ 473	Discounted cash flows	Credit spreads[2]	100 bps - 6,451 bps	4,995 bps
			Discount rate	0% - 47%	15%
			Constant prepayment rate	0% - 20%	1%
			Constant default rate	0% - 34%	7%
			Loss severity	40% - 80%	49%

[1] Swap assets and liabilities are presented net for the purposes of this table.
[2] Implied spread on closing market prices for index positions.
[3] Weighted averages are calculated based on the fair value of the respective instruments.

Sensitivity of ML Level 3 Fair Value Measurements to Changes in Unobservable Inputs

The following provides a general description of the impact of a change in an unobservable input on the fair value measurement and the interrelationship of unobservable inputs.

I. Mortgage loans

In general, an increase in isolation in either the discount rate or the property capitalization rate, which is the ratio between the net operating income produced by an asset and its current fair value, would result in a decrease in the fair value measurement; while an increase in net operating income growth rate, in isolation would result in an increase in the fair value measurement. For each of the relationships described above, the inverse would also generally apply.

II. Derivatives

For CDS with reference obligations on CMBS, an increase in credit spreads would generally result in a higher fair value measurement for protection buyers and a lower fair value measurement for protection sellers. The inverse would also generally apply to this relationship given a decrease in credit spreads.

For CDS with reference obligations on RMBS or other ABS assets, changes in the discount rate, constant prepayment rate, constant default rate, and loss severity would have an uncertain effect on the overall fair value measurement. This is because, in general, changes in these inputs could potentially affect other inputs used in determining the fair value measurement. For example, a change in the assumptions used for the constant default rate will generally be accompanied by a corresponding change in the assumption used for the loss severity and an inverse change in the assumption used for constant prepayment rates. Additionally, changes in the fair value measurement based on variations in the inputs used generally cannot be extrapolated because the relationship between each input is not perfectly correlated.

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

	2013				
	Level 1[1]	Level 2[1]	Level 3	Netting[2]	Total fair value
Assets:					
Cash equivalents[3]	$ 569	$ -	$ -	$ -	$ 569
Short-term investments	530	-	-	-	530
Commercial mortgage loans	-	-	507	-	507
Swap contracts	-	-	345	(187)	158
Non-agency RMBS	-	2	6	-	8
Other investments	-	-	2	-	2
Total assets	$ 1,099	$ 2	$ 860	$ (187)	$ 1,774
Liabilities:					
Beneficial interest in consolidated VIEs	$ -	$ 116	$ -	$ -	$ 116
Swap contracts	-	-	193	(120)	73
Total liabilities	$ -	$ 116	$ 193	$ (120)	$ 189

[1] There were no transfers between Level 1 and Level 2 during the year ended December 31, 2013.
[2] Derivative receivables and payables and the related cash collateral received and paid are shown net when a master netting agreement exists.
[3] Cash equivalents consist primarily of money market funds.

	2012				
	Level 1[1]	Level 2[1]	Level 3	Netting[2]	Total fair value
Assets:					
Cash equivalents[3]	$ 634	$ -	$ -	$ -	$ 634
Short-term investments	454	236	-	-	690
Commercial mortage loans	-	-	466	-	466
Swap contracts	-	-	816	(408)	408
Non-agency RMBS	-	2	-	-	2
Other investments[4]	-	11	55	-	66
Total assets	$ 1,088	$ 249	$ 1,337	$ (408)	$ 2,266
Liabilities:					
Beneficial interest in consolidated VIEs	$ -	$ 803	$ -	$ -	$ 803
Swap contracts	-	-	343	(272)	71
Total liabilities	$ -	$ 803	$ 343	$ (272)	$ 874

[1] There were no significant transfers between Level 1 and Level 2 during the year ended December 31, 2012.
[2] Derivative receivables and payables and the related cash collateral received and paid are shown netted when a master netting agreement exists.
[3] Cash equivalents consist primarily of money market funds and repurchase agreements.
[4] Investments with a fair value of $1 million that were classified as a Level 2 instrument as of December 31, 2012 were recategorized from "Federal agency and GSE MBS" to "Other investments" to conform to the current year presentation.

The table below presents a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) as of December 31, 2013 (in millions). Unrealized gains and losses related to those assets still held at December 31, 2013 are reported as a component of "Investments held by consolidated variable interest entities, net" in the Combined Statements of Condition.

	2013						
	Fair value December 31, 2012	Purchases, sales, issuances and settlements, net	Net realized/unrealized gains (losses)	Gross transfers in[1,2]	Gross transfers out[1,2]	Fair value December 31, 2013	Change in unrealized gains (losses) related to financial instruments held at December 31, 2013
Assets:							
Commercial mortgage loans	$ 466	$ (163)	$ 204	$ -	$ -	$ 507	$ 183
Non-agency RMBS	-	4	-	2	-	6	-
CDOs	-	-	-	-	-	-	(2)
Other investments	55	(73)	18	2	-	2	(2)
Total assets	$ 521	$ (232)	$ 222	$ 4	$ -	$ 515	$ 179
Net swap contracts[3]	$ 473	$ (268)	$ (53)	$ -	$ -	$ 152	$ (53)

[1] The amount of transfers is based on the fair values of the transferred assets at the beginning of the reporting period.
[2] Non-agency RMBS and other investments, with December 31, 2012 fair values of $2 and $2, respectively, were transferred from Level 2 to Level 3 because they are valued at December 31, 2013 based on non-observable inputs (Level 3). These investments were valued in the prior year based on quoted prices for identical or similar assets in non-active markets or model-based techniques for which all significant inputs were observable (Level 2).
[3] Level 3 derivative assets and liabilities are presented net for purposes of this table.

The following table presents the gross components of purchases, sales, issuances, and settlements, net, shown for the year ended December 31, 2013 (in millions):

	2013				
	Purchases	Sales	Issuances	Settlements[2]	Purchases, sales, issuances, and settlements, net
Assets:					
Commercial mortgage loans	$ -	$ (88)	$ -	$ (75)	$ (163)
Non-agency RMBS	4	-	-	-	4
CDOs	3	(5)	-	2	-
Other investments	-	(74)	-	1	(73)
Total assets	$ 7	$ (167)	$ -	$ (72)	$ (232)
Net swap contracts[1]	$ -	$ (153)	$ -	$ (115)	$ (268)

[1] Level 3 swap assets and liabilities are presented net for the purpose of this table.
[2] Includes paydowns

The table below presents a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) as of December 31, 2012 (in millions). Unrealized gains and losses related to those assets still held at December 31, 2012 are reported as a component of "Investments held by consolidated variable interest entities, net" in the Combined Statements of Condition.

	2012						
	Fair value December 31, 2011	Purchases, sales, and settlements, net	Net realized/unrealized gains (losses)	Gross transfers in[1,2]	Gross transfers out[1,2]	Fair value December 31, 2012	Change in unrealized gains (losses) related to financial instruments held at December 31, 2012
Assets:							
Commercial mortgage loans	$ 1,397	$ (1,187)	$ 256	$ -	$ -	$ 466	$ 135
Non-agency RMBS	5,410	(6,347)	937	-	-	-	-
Residential mortgage loans	378	(374)	(4)	-	-	-	(1)
CDOs	17,687	(23,196)	5,509	-	-	-	(2)
Other investments	108	(65)	2	10	-	55	-
Total assets	$ 24,980	$ (31,169)	$ 6,700	$ 10	$ -	$ 521	$ 132
Net swap contracts[3]	$ 839	$ (276)	$ (90)	$ -	$ -	$ 473	$ (93)
Liabilities:							
Beneficial interest in consolidated VIEs	$ 9,845	$ (1,385)	$ -	$ -	$ (8,460)	$ -	$ -

[1] The amount of transfers is based on the fair values of the transferred assets at the beginning of the reporting period.
[2] Beneficial interest in consolidated VIEs, with a December 31, 2011, fair value of $8,460 million, were transferred from Level 3 to Level 2 because they are valued at December 31, 2012, based on model-based techniques for which all significant inputs are observable (Level 2). These investments were valued in the prior year on non-observable model based inputs (Level 3). There were also certain other investments for which valuation inputs became less observable during the year ended December 31, 2012, which resulted in $10 million in transfers from Level 2 to Level 3. There were no other transfers between Level 2 and Level 3 during the current year.
[3] Level 3 derivative assets and liabilities are presented net for purposes of this table.

The following table presents the gross components of purchases, sales, issuances, and settlements, net, shown for the year ended December 31, 2012 (in millions):

	2012				
	Purchases	Sales	Issuances	Settlements[2]	Purchases, sales, issuances, and settlements, net
Assets:					
Commercial mortgage loans	$ -	$ (1,119)	$ -	$ (68)	$ (1,187)
Non-agency RMBS	-	(6,221)	-	(126)	(6,347)
Residential mortgage loans	-	(370)	-	(4)	(374)
CDOs	-	(22,206)	-	(990)	(23,196)
Other investments	-	(66)	-	1	(65)
Total assets	$ -	$ (29,982)	$ -	$ (1,187)	$ (31,169)
Net swap contracts[1]	$ -	$ (147)	$ -	$ (129)	$ (276)
Liabilities:					
Beneficial interest in consolidated VIEs	$ 45 [2]	-	-	$ (1,430)	$ (1,385)

[1] Level 3 swap assets and liabilities are presented net for the purpose of this table.
[2] Includes paydowns

g. *Professional Fees*

The consolidated VIEs have recorded costs for professional services provided, among others, by several nationally recognized institutions that serve as investment managers, administrators, and custodians for the VIEs' assets. The fees charged by the investment managers, custodians, administrators, auditors, attorneys, and other service providers, are recorded in "Operating Expenses: Other" in the Combined Statements of Income and Comprehensive Income.

7. Bank Premises, Equipment, and Software

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

	2013	2012
Bank premises and equipment:		
Land and land improvements	$ 395	$ 394
Buildings	2,693	2,659
Building machinery and equipment	554	520
Construction in progress	37	27
Furniture and equipment	1,006	1,024
Subtotal	4,685	4,624
Accumulated depreciation	(2,032)	(1,948)
Bank premises and equipment, net	$ 2,653	$ 2,676
Depreciation expense, for the years ended December 31	$ 202	$ 218

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

	2013	2012
Leased premises and equipment under capital leases	$ 27	$ 33
Accumulated depreciation	(18)	(20)
Leased premises and equipment under capital leases, net	$ 9	$ 13
Depreciation expense related to leased premises and equipment under capital leases, for the years ended December 31	$ 6	$ 7

The Reserve Banks lease space to outside tenants with remaining lease terms ranging from 1 to 11 years. Rental income from such leases was $35 million and $37 million for the years ended December 31, 2013 and 2012, respectively, and is reported as a component of "Non-interest income: Other" in the Combined Statements of Income and Comprehensive Income. Future minimum lease payments that the Reserve Banks will receive under noncancelable lease agreements in existence at December 31, 2013, are as follows (in millions):

2014	$ 33
2015	29
2016	23
2017	18
2018	14
Thereafter	36
Total	$ 153

The Reserve Banks had capitalized software assets, net of amortization, of $356 million and $213 million at December 31, 2013 and 2012, respectively. Amortization expense was $73 million and $64 million for the years ended December 31, 2013 and 2012, respectively. Capitalized software assets are reported as a component of "Other assets" in the Combined Statements of Condition and the related amortization is reported as a component of "Operating expenses: Other" in the Combined Statements of Income and Comprehensive Income.

As a result of the Federal Reserve Bank of Cleveland's (FRBC) restructuring plan discussed in Note 12, the FRBC sold its Pittburgh facility during the third quarter of 2013. This sale resulted in a $1.9 million loss, of which $0.2 million is reflected in "Operating expense: Occupancy" and $1.7 million is reflected in "Operating expense: Other" in the Statements of Income and Comprehensive Income.

In 2008 after relocating operations to a new facility, the Federal Reserve Bank of San Francisco (FRBSF) classified its former Seattle branch office building as held for sale, and the building was reported at fair value as a component of "Other Assets" in the Statements of Condition. In April 2012, the FRBSF completed the donation of the building to the United States General Services Administration (GSA). Under the donation agreement, the FRBSF must continue to maintain the building for up to fifteen months from the time GSA takes ownership. The FRBSF recorded an additional impairment of $3.4 million during the year ended December 31, 2012, to reflect the final disposition of this building, which was recorded as a component of "Operating expenses: Other" in the Statements of Income and Comprehensive Income.

8. COMMITMENTS AND CONTINGENCIES

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

At December 31, 2013, the Reserve Banks were obligated under noncancelable leases for premises and equipment with remaining terms ranging from 1 to approximately 9 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), net of sublease rentals, was $17 million and $16 million for the years ended December 31, 2013 and 2012, respectively.

Future minimum lease payments under noncancelable operating leases, net of sublease rentals, with remaining terms of one year or more, at December 31, 2013, are as follows (in millions):

2014	$	5
2015		5
2016		2
2017		2
2018		2
Thereafter		4
Future minimum lease payments	$	20

At December 31, 2013, the Reserve Banks had unrecorded unconditional purchase commitments and long-term obligations extending through the year 2022 with a remaining fixed commitment of $240 million. Purchases of $37 million and $28 million were made against these commitments during 2013 and 2012, respectively. These commitments are for maintenance of currency processing machines and have variable and/or fixed components. The variable portion of the commitments is for additional services above the fixed contractual service limits. The fixed payments for the next five years under these commitments are as follows (in millions):

2014	$	23
2015		27
2016		26
2017		26
2018		26

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

Other Commitments

In support of financial market stability activities, the FRBNY entered into commitments to provide financial assistance to financial institutions. The FRBNY had remaining unfunded contractual commitments related to commercial mortgage loans in ML of $40 and $55 million at December 31, 2013 and 2012, respectively.

9. RETIREMENT AND THRIFT PLANS

Retirement Plans

The Reserve Banks currently offer 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 participate in the Retirement Plan for Employees of the Federal Reserve System (System Plan). Under the Dodd-Frank Act, newly hired Bureau employees are eligible to participate in the System Plan. In addition, employees at certain compensation levels participate in the Benefit Equalization Retirement Plan (BEP) and certain Reserve Bank officers participate in the Supplemental Retirement Plan for Select Officers of the Federal Reserve 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. During the years ended December 31, 2013 and 2012, certain costs associated with the System Plan were reimbursed by the Bureau.

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

	2013	2012
Estimated actuarial present value of projected benefit obligation at January 1	$ 11,468	$ 10,198
Service cost-benefits earned during the period	407	349
Interest cost on projected benefit obligation	472	473
Actuarial (gain) loss	(1,527)	833
Contributions by plan participants	5	4
Special termination benefits	6	9
Benefits paid	(355)	(334)
Plan amendments	-	(64)
Estimated actuarial present value of projected benefit obligation at December 31	$ 10,476	$ 11,468

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

	2013	2012
Estimated plan assets at January 1 (of which \$9,440 and \$7,977 is measured at fair value as of January 1, 2013 and 2012, respectively)	$ 9,566	$ 8,048
Actual return on plan assets	683	1,066
Contributions by the employer	909	782
Contributions by plan participants	5	4
Benefits paid	(355)	(334)
Estimated plan assets at December 31 (of which \$10,687 and \$9,440 is measured at fair value as of December 31, 2013 and 2012, respectively)	$ 10,808	$ 9,566
Funded status and accrued pension benefit costs	$ 332	$ (1,902)
Amounts included in accumulated other comprehensive loss are shown below:		
Prior service cost	$ (456)	$ (559)
Net actuarial loss	(1,928)	(3,784)
Total accumulated other comprehensive loss	$ (2,384)	$ (4,343)

The FRBNY, on behalf of the System, funded $900 million and $780 million during the years ended December 31, 2013 and 2012, respectively. The Bureau is required by the Dodd-Frank Act to fund the System plan for each Bureau employee based on an established formula. During the years ended December 2013 and 2012, the Bureau funded contributions of $9 million and $2 million, respectively.

Accrued pension benefit costs are reported as a component of "Other assets" and "Accrued benefit costs" respectively, in the Combined Statements of Condition.

The accumulated benefit obligation for the System Plan, which differs from the estimated actuarial present value of projected benefit obligation because it is based on current rather than future compensation levels, was $9,308 million and $10,035 million at December 31, 2013 and 2012, respectively.

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

	2013	2012
Discount rate	4.92%	4.00%
Rate of compensation increase	4.50%	4.50%

Net periodic benefit expenses for the years ended December 31, 2013 and 2012, were actuarially determined using a January 1 measurement date. The weighted-average assumptions used in developing net periodic benefit expenses for the System Plan for the years were as follows:

	2013	2012
Discount rate	4.00%	4.50%
Expected asset return	6.50%	7.25%
Rate of compensation increase	4.50%	5.00%

Beginning in 2013, the System Plan discount rate assumption setting convention changed from rounding the rate to the nearest 25 basis points to using an unrounded rate.

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

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

	2013	2012
Service cost - benefits earned during the period	$ 407	$ 349
Interest cost on projected benefit obligation	472	473
Amortization of prior service cost	103	116
Amortization of net loss	284	292
Expected return on plan assets	(638)	(599)
Net periodic pension benefit expense	628	631
Special termination benefits	6	9
Bureau of Consumer Financial Protection contributions	(9)	(2)
Total periodic pension benefit expense	$ 625	$ 638

Estimated amounts that will be amortized from accumulated other comprehensive loss into net periodic pension benefit expense in 2014 are shown below:

Prior service cost	$	100
Net actuarial loss		87
Total	$	187

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

2014	$	406
2015		429
2016		455
2017		483
2018		512
2019-2023		2,982
Total	$	5,267

The System's Committee on Investment Performance (CIP) is responsible for establishing investment policies, selecting investment managers, and monitoring the investment managers' compliance with its policies. At December 31, 2013, the System Plan's assets were held in nine investment vehicles: three actively-managed long-duration fixed income portfolios, a passively-managed long-duration fixed income portfolio, an indexed U.S. equity fund, an indexed non-U.S. developed-markets equity fund, an indexed emerging-markets equity fund, a private equity limited partnership, and a money market fund.

The diversification of the Plan's investments is designed to limit concentration of risk and the risk of loss related to an individual asset class. The three actively-managed long-duration fixed income portfolios are separate accounts benchmarked to a custom benchmark of 55 percent Barclays Long Credit Index and 45 percent Citigroup 15+ years U.S. Treasury STRIPS Index. This custom benchmark was selected as a proxy to match the liabilities of the Plan and the guidelines for these portfolios are designed to limit portfolio deviations from the benchmark. The passively-managed long-duration fixed-income portfolio is invested in two commingled funds and is benchmarked to 55 percent Barclays Long Credit Index and 45 percent Barclays 20+ STRIPS Index. The indexed U.S. equity fund is intended to track the overall U.S. equity market across market capitalizations and is benchmarked to the Dow Jones U.S. Total Stock Market Index. The indexed non-U.S. developed-markets equity fund is intended to track the Morgan Stanley Capital International (MSCI) World ex-US Investible Markets Index (IMI), which includes stocks from 23 markets deemed by MSCI to be "developed markets." The indexed emerging-markets equity fund is intended to track the MSCI Emerging Markets IMI Index, which includes stocks from 21 markets deemed by MSCI to be "emerging markets." The three indexed equity funds include stocks from across the market capitalization spectrum (i.e., large-, mid- and small-cap stocks). The private equity limited partnership invests globally across various private equity strategies. Finally, the money market fund, which invests in short term Treasury and Agency debt and repurchase agreements backed by Treasury and Agency debt, is the repository for cash balances and adheres to a constant dollar methodology.

Permitted and prohibited investments, including the use of derivatives, are defined in either the trust agreement (for the passively-managed long-duration fixed income portfolio) or the investment guidelines (for the remaining investments). The CIP reviews the trust agreement and approves all investment guidelines as part of the selection of each investment to ensure that the trust agreement is consistent with the CIP's investment objectives for the System Plan's assets.

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

	Policy weight	Actual asset allocations 2013	2012
U.S. equities	30.0%	29.7%	34.9%
International equities	18.0%	18.3%	13.6%
Emerging markets equities	2.0%	1.9%	0.0%
Fixed income	50.0%	49.4%	50.4%
Cash and cash equivalents	0.0%	0.7%	1.1%
Total	100.0%	100.0%	100.0%

In June 2013, the Committee on Investment Performance (the "Committee") approved a change in the allocation and benchmarks for the Plan's public equity portfolio. The new benchmark is the MSCI All Country World Investible Markets Index. This benchmark change will reduce the Plan's holdings in U.S. equities, increase the Plan's holdings of developed markets international equities, and add an investment in emerging market equities when it is fully implemented in mid-2014. The Committee approved a phased six-month implementation period for these changes, commencing in September 2013 for developed market equities and November 2013 for emerging market equities. The policy weight percentages shown above reflect the target allocation as of December 2013 based on this implementation strategy.

Employer contributions to the System Plan may be determined using different assumptions than those required for financial reporting. The System Plan's anticipated funding level for 2014 is $480 million. In 2014, the Bank plans to make monthly contributions of $40 million and will reevaluate the monthly contributions upon completion of the 2014 actuarial valuation. The Bank's projected benefit obligation, funded status, and net pension expenses for the BEP and the SERP at December 31, 2013 and 2012, and for the years then ended, were not material.

Determination of Fair Value

The System Plan's publicly available investments are valued on the basis of the last available bid prices or current market quotations provided by dealers, or pricing services. To determine the value of a particular investment, pricing services may use information on transactions in such investments; quotations from dealers; pricing metrics; market transactions in comparable investments; relationships observed in the market between investments; and calculated yield measures based on valuation methodologies commonly employed in the market for such investments.

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

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

	2013			
Description	Level 1 [1]	Level 2 [1]	Level 3	Total
Short-term investments [2]	$ 14	$ 126	$ -	$ 140
Treasury and Federal agency securities	38	1,565	-	1,603
Corporate bonds	-	1,773	-	1,773
Other fixed income securities	-	362	-	362
Commingled funds	-	6,795	-	6,795
Private Equity	-	-	14	14
Total	$ 52	$ 10,621	$ 14	$ 10,687

[1] There were no transfers between Level 1 and Level 2 during the year.
[2] Short-term investments includes cash equivalents of $78 million.

	2012			
Description	Level 1 [1]	Level 2 [1]	Level 3	Total
Short-term investments	$ 23	$ 25	$ -	$ 48
Treasury and Federal agency securities	141	1,746	-	1,887
Corporate bonds	-	1,947	-	1,947
Other fixed income securities	-	352	-	352
Commingled funds	-	5,206	-	5,206
Total	$ 164	$ 9,276	$ -	$ 9,440

[1] U.S. Treasury STRIPs with a fair value of $1,737 million were transferred from Level 1 to Level 2 because they were valued based on quoted prices in non-active markets (Level 2). There were no other transfers between Level 1 and Level 2 during the year.

The System Plan enters into futures contracts, traded on regulated exchanges, to manage certain risks and to maintain appropriate market exposure in meeting the investment objectives of the System Plan. The System Plan bears the market risk that arises from any unfavorable changes in the value of the securities or indexes underlying these futures contracts. The use of futures contracts involves, to varying degrees, elements of market risk in excess of the amount recorded in the Combined Statements of Condition. The guidelines established by the CIP further reduce risk by limiting the net futures positions, for most fund managers, to 15 percent of the market value of the advisor's portfolio.

At December 31, 2013 and 2012, a portion of short-term investments was available for futures trading. There were $8 million and $7 million of Treasury securities pledged as collateral for the years ended December 31, 2013 and 2012, respectively.

Thrift Plan

Employees of the Reserve Banks participate in the defined contribution Thrift Plan for Employees of the Federal Reserve System (Thrift Plan). The Reserve Banks match 100 percent of the first six percent of employee contributions from the date of hire and provides an automatic employer contribution of one percent of eligible pay. The Reserve Banks' Thrift Plan contributions totaled $108 million and $102 million for the years ended December 31, 2013 and 2012, respectively, and are reported as a component of "Operating expenses: Salaries and benefits" in the Combined Statements of Income and Comprehensive Income.

10. Postretirement Benefits Other Than Retirement Plans and Postemployment Benefits

Postretirement Benefits Other Than Retirement Plans

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

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

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

	2013	2012
Accumulated postretirement benefit obligation at January 1	$ 1,755	$ 1,506
Service cost benefits earned during the period	75	59
Interest cost on accumulated benefit obligation	67	69
Net actuarial (gain) loss	(290)	181
Curtailment loss (gain)	-	-
Special termination benefits loss	1	1
Contributions by plan participants	24	22
Benefits paid	(93)	(87)
Medicare Part D subsidies	5	5
Plan amendments	(6)	(1)
Accumulated postretirement benefit obligation at December 31	$ 1,538	$ 1,755

At December 31, 2013 and 2012, the weighted-average discount rate assumptions used in developing the postretirement benefit obligation were 4.79 percent and 3.75 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. Beginning in 2013, the System Plan discount rate assumption setting convention changed from rounding the rate to the nearest 25 basis points to using an unrounded rate.

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

	2013	2012
Fair value of plan assets at January 1	$ -	$ -
Contributions by the employer	64	60
Contributions by plan participants	24	22
Benefits paid	(93)	(87)
Medicare Part D subsidies	5	5
Fair value of plan assets at December 31	$ -	$ -
Unfunded obligation and accrued postretirement benefit cost	$ 1,538	$ 1,755

Amounts included in accumulated other comprehensive loss are shown below:

	2013	2012
Prior service cost	$ 29	$ 36
Net actuarial loss	(201)	(538)
Total accumulated other comprehensive loss	$ (172)	$ (502)

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

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

	2013	2012
Health-care cost trend rate assumed for next year	7.00%	7.00%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.00%	5.00%
Year that the rate reaches the ultimate trend rate	2019	2018

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, 2013 (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	$ 25	$ (20)
Effect on accumulated postretirement benefit obligation	184	(157)

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

	2013		2012	
Service cost-benefits earned during the period	$	75	$	59
Interest cost on accumulated benefit obligation		67		69
Amortization of prior service credit		(11)		(10)
Amortization of net actuarial loss		46		31
Total periodic expense	$	177	$	149
Curtailment (gain)		-		-
Special termination benefits loss		1		1
Net periodic postretirement benefit expense	$	178	$	150

Estimated amounts that will be amortized from accumulated other comprehensive loss into net periodic postretirement benefit expense in 2014 are shown below:

Prior service credit	$	(10)
Net actuarial loss		9
Total	$	(1)

Net postretirement benefit costs are actuarially determined using a January 1 measurement date. At January 1, 2013 and 2012, the weighted-average discount rate assumptions used to determine net periodic postretirement benefit costs were 3.75 percent and 4.5 percent, respectively.

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

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

Federal Medicare Part D subsidy receipts were $4.0 million and $4.3 million in the years ended December 31, 2013 and 2012, respectively. Expected receipts in 2014, related to benefits paid in the years ended December 31, 2013 and 2012, are $3.5 million.

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

	Without subsidy	With subsidy
2014	$ 77	$ 72
2015	$ 81	$ 75
2016	$ 85	$ 79
2017	$ 89	$ 83
2018	$ 94	$ 87
2019 - 2023	$ 544	$ 498
Total	$ 970	$ 894

Postemployment Benefits

The Reserve Banks offer benefits to former or inactive employees. Postemployment benefit costs are actuarially determined using a January 1 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 Reserve Banks at December 31, 2013 and 2012, were $148 million and $164 million, respectively. This cost is included as a component of "Accrued benefit costs" in the Combined Statements of Condition. Net periodic postemployment benefit expense included in 2013 and 2012 operating expenses were $7 million and $25 million, respectively, and are recorded as a component of "Operating expenses: Salaries and benefits" in the Combined Statements of Income and Comprehensive Income.

11. Accumulated Other Comprehensive Income And Other Comprehensive Income

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

	2013			2012		
	Amount related to defined benefit retirement plan	Amount related to postretirement benefits other than retirement plans	Total accumulated other comprehensive loss	Amount related to defined benefit retirement plan	Amount related to postretirement benefits other than retirement plans	Total accumulated other comprehensive loss
Balance at January 1	$ (4,343)	$ (502)	$ (4,845)	$ (4,449)	$ (343)	$ (4,792)
Change in funded status of benefit plans:						
Prior service costs arising during the year	-	5	5	64	1	65
Amortization of prior service cost	103 [1]	(11) [2]	92	116 [1]	(10) [2]	106
Change in prior service costs related to benefit plans	103	(6)	97	180	(9)	171
Net actuarial gain (loss) arising during the year	1,572	290	1,862	(366)	(181)	(547)
Amortization of net actuarial loss	284 [1]	46 [2]	330	292 [1]	31 [2]	323
Change in actuarial gain (losses) related to benefit plans	1,856	336	2,192	(74)	(150)	(224)
Change in funded status of benefit plans - other comprehensive income (loss)	1,959	330	2,289	106	(159)	(53)
Balance at December 31	$ (2,384)	$ (172)	$ (2,556)	$ (4,343)	$ (502)	$ (4,845)

[1] Reclassification is reported as a component of "Operating Expenses: Net periodic pension expense" in the Combined Statements of Income and Comprehensive Income.

[2] Reclassification is reported as a component of "Operating Expenses: Salaries and benefits" in the Combined Statements of Income and Comprehensive Income.

Additional detail regarding the classification of accumulated other comprehensive loss is included in Note 9 and 10.

12. Business Restructuring Charges

The Reserve Banks had no material business restructuring charges in 2013 or 2012.

In 2011, the U.S. Treasury announced a restructuring initiative to consolidate the Treasury Retail Securities operations. As a result of this initiative, Treasury Retail Securities operations performed by the FRBC were consolidated into the Federal Reserve Bank of Minneapolis. Additional announcements in 2011 included the consolidation of paper check processing, performed by the FRBC, into the Federal Reserve Bank of Atlanta (FRBA).

In years prior to 2011, the Reserve Banks announced the acceleration of their check restructuring initiatives to align the check processing infrastructure and operations with declining check processing volumes. The new infrastructure consolidated paper and electronic check processing at the FRBA.

Restructuring costs associated with certain Bank assets, including software, buildings, leasehold improvements, furniture, and equipment, are discussed in Note 7.

13. Distribution of Comprehensive Income

In accordance with Board policy, Reserve Banks remit excess earnings, after providing for dividends and the amount necessary to equate surplus with capital paid-in, to the U.S. Treasury as earnings remittances to Treasury. The following table presents the distribution of the Reserve Banks' comprehensive income in accordance with the Board's policy for the years ended December 31 (in millions):

	2013	2012
Dividends on capital stock	$ 1,650	$ 1,637
Transfer to surplus - amount required to equate surplus with capital paid-in	147	461
Earnings remittances to Treasury	79,633	88,418
Total distribution	$ 81,430	$ 90,516

14. Subsequent Events

There were no subsequent events that require adjustments to or disclosures in the combined financial statements as of December 31, 2013. Subsequent events were evaluated through March 14, 2014, which is the date that the combined financial statements were available to be issued.