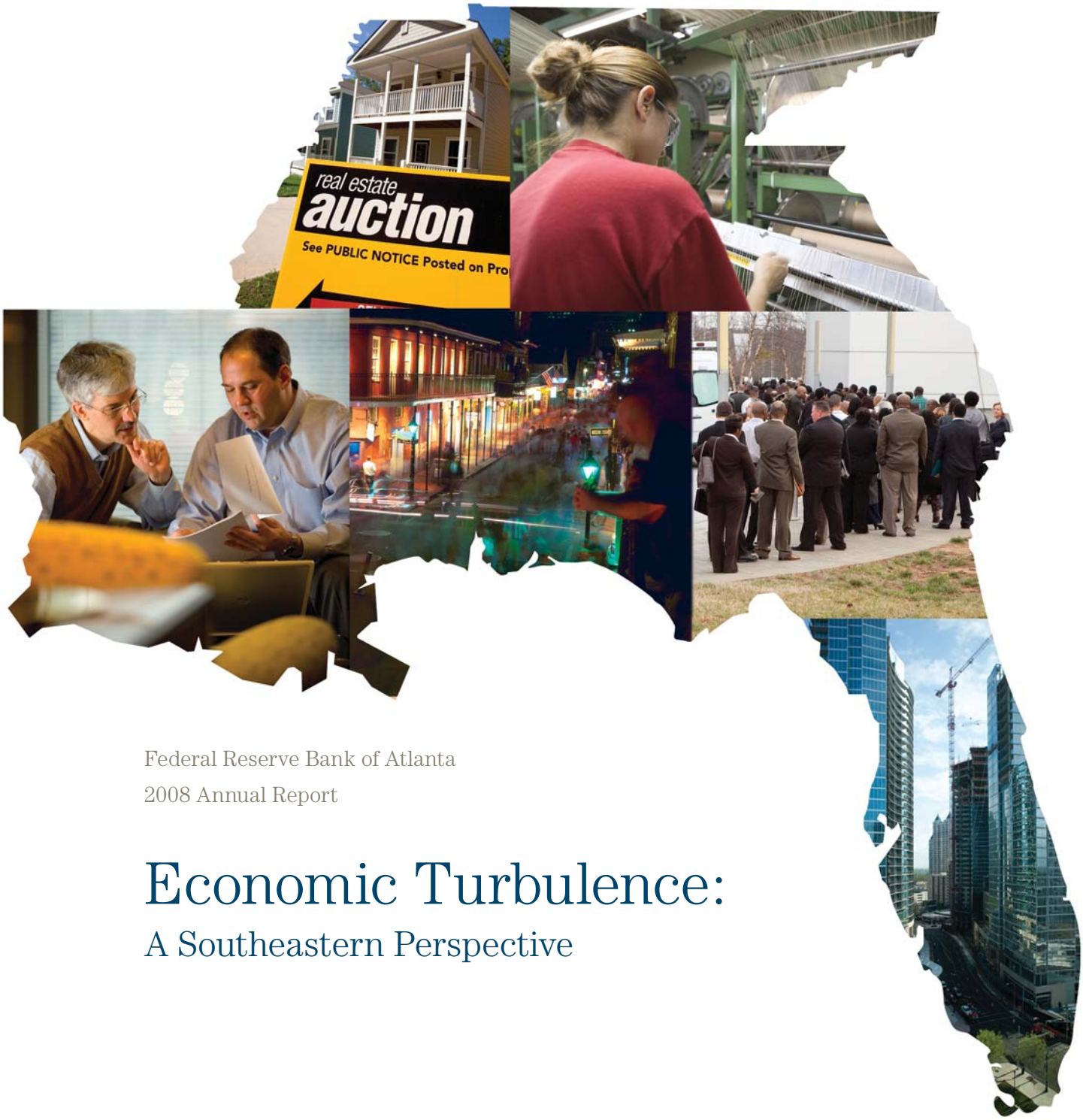

Federal Reserve Bank of Atlanta

2008 Annual Report

Economic Turbulence:

A Southeastern Perspective

The Federal Reserve Bank of Atlanta is one of twelve regional Reserve Banks in the United States that, together with the Board of Governors in Washington, D.C., make up the Federal Reserve System—the nation's central bank. Since its establishment by an act of Congress in 1913, the Federal Reserve System's primary role has been to foster a sound financial system and a healthy economy.

To advance this goal, the Atlanta Fed helps formulate monetary policy, supervises banks and bank and financial holding companies, and provides payment services to depository institutions and the federal government.

Through its six offices in Atlanta, Birmingham, Jacksonville, Miami, Nashville, and New Orleans, the Federal Reserve Bank of Atlanta serves the Sixth Federal Reserve District, which comprises Alabama, Florida, Georgia, and parts of Louisiana, Mississippi, and Tennessee.

Federal Reserve Bank of Atlanta 2008 Annual Report

Economic Turbulence: A Southeastern Perspective

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Dennis P. Lockhart, president and chief executive officer, and Patrick K. Barron, first vice president and chief operating officer

A Message from the President

The year 2008 began with financial instability. As the year drew to a close, that instability had become turmoil, and the economic recession had deepened and broadened, affecting the region, the nation, and much of the world.

This year's annual report examines this painful economic transition in 2008 from the Atlanta Fed's southeastern perspective. The financial crisis and recession were tightly interconnected. With continued bouts of financial volatility and the important secondary credit markets frozen, almost all significant economic measures took a turn for the worse. Business investment and consumer spending faltered, and the job market declined proportionately more than it had in decades. Nationally, about 3.1 million Americans lost their jobs in 2008, and the unemployment rate increased from 4.9 percent in January to 7.2 percent in December.

Price pressures also swung widely during 2008. Because global economic growth was solid early in the year, prices increased sharply during the spring and summer. Inflation concerns abated late in the year even to the point of deflation as the economy slackened.

In the Southeast the housing boom in Florida and Georgia that had driven growth for years ended before 2008. Weakness in the housing sector in 2008 spread to commercial real estate and most other sectors of an economy that had grown accustomed to an influx of new people and new construction. But old assumptions collapsed under the pressure of the 2008 downturn. As in the nation, business investment and consumer spending faltered, and the job market took a sharp turn for the worse, with the six states of the Southeast shedding 674,000 net jobs in 2008.

The Federal Reserve acted swiftly and comprehensively to address conditions nationally. The Federal Open Market

Committee (FOMC) cut the federal funds rate seven times in 2008, from 4.25 percent in early January to a range just above zero in December.

But even with the fed funds rate as low as it can go, the Fed has other options for implementing monetary policy. Since the outbreak of financial turmoil in mid-2007, the Fed has greatly expanded its role as lender of last resort while undertaking a host of other policy actions geared toward helping markets resume normal functioning. The Fed launched various programs to lend to primary dealers, investment banks, a global insurance company, and industrial and financial companies issuing commercial paper. At the final 2008 meeting, in December, the FOMC announced plans to purchase large quantities of agency debt and mortgage-backed securities to support the mortgage and housing markets.

Of course, the Fed has not acted alone in efforts to stabilize the financial sector and reverse the economic slowdown. The Fed has worked in concert with other central banks around the world. And the U.S. Treasury and the Federal Deposit Insurance Corporation have moved decisively to stabilize and repair financial institutions to encourage them to resume lending—a necessary precursor to recovery in the broader economy.

The Atlanta Fed did its part in helping to formulate effective monetary policy for these turbulent times. The six states that make up the Atlanta Fed's region have a diverse economy, with 46 million people, and the region as a whole is an excellent proxy for the broader national economy. So a firsthand perspective on the region's economy provides an advantage in achieving our mission to inform national monetary policy.

To help enhance this firsthand insight, the bank's Research Department established the Regional Economic Information Network, or REIN, in 2008 to extend our sources of intelligence about the southeastern economy. As part of REIN, our regional executives based at the five Atlanta Fed branches are recruiting new contacts and developing a broader base of information sources.

Along with the REIN network, the Atlanta Fed's head office and branch boards of directors, made up of forty-four business and community leaders, provide invaluable insights into the economic and financial dynamics of the Southeast.

Just as the Research Department expanded its efforts to meet 2008's extraordinary demands, other areas of the Atlanta Fed also worked hard to fulfill our central banking responsibilities amid changing and unprecedented circumstances. Problems in the real estate sector undermined the health of banking institutions the Atlanta Fed supervises and triggered a rise in foreclosures in the Southeast that the bank's community affairs staff actively addressed.

Likewise, the Fed System's Retail Payments Office, based at the Atlanta Fed, responded to cost pressures and a changing payments mix with continued improvements in efficiency, even as economic conditions in the country worsened.

I believe one of the lessons of 2008 is that a functioning financial sector is absolutely vital to economic growth. Banks play a pivotal role in the allocation of credit that is so important to private sector economic activity—from buying homes to investing in new equipment to meeting payroll. But during 2008 we saw the collapse or near collapse of major financial institutions. These failures severely undermined the most important factor in our economy—trust. The collapse of trust or confidence further restricted the flow of credit, which in turn added to risk aversion and magnified weaknesses in the broader economy.

With so much attention devoted to our nation's financial health, tensions have grown between those who identify with the mainstream public—Main Street—and the institutions that make up the financial sector, or Wall Street. This perception is understandable. But I believe it's a mistake for Americans to see their interests as disconnected from banks and financial markets.

The turbulence that spread from the financial sector to the broader economy was years in the making, and it won't disappear overnight. But I believe the comprehensive policy actions that began in 2008 and continued into 2009 will help to position the U.S. financial sector and economy for stability and recovery in the long term.

Dennis P. Lockhart

Tough Times: The Southeastern Economy in 2008

In 2008 the U.S. economy faced many economic challenges: tight financial markets, rising foreclosure rates, and job losses. By almost any yardstick, the problems affecting the nation's financial system took a toll on an already weak general economy. Rapidly escalating rates of home foreclosures, declines in home prices, and, ultimately, the lack of credit availability in the economy translated into sharply lower levels of economic activity.

Employment takes huge hits

For many years the southeastern economy generated hundreds of thousands of jobs, but it showed signs of fatigue in 2007 and outright decline in 2008. Its twin locomotives—Florida and Georgia—stalled and began rolling backward. Florida, the leader of the region's economic surge in recent years, suffered from overbuilt residential real estate markets and related financial turmoil. Georgia, another major growth engine in recent years, joined Florida, California, and Michigan as the states that lost the most jobs in 2008.

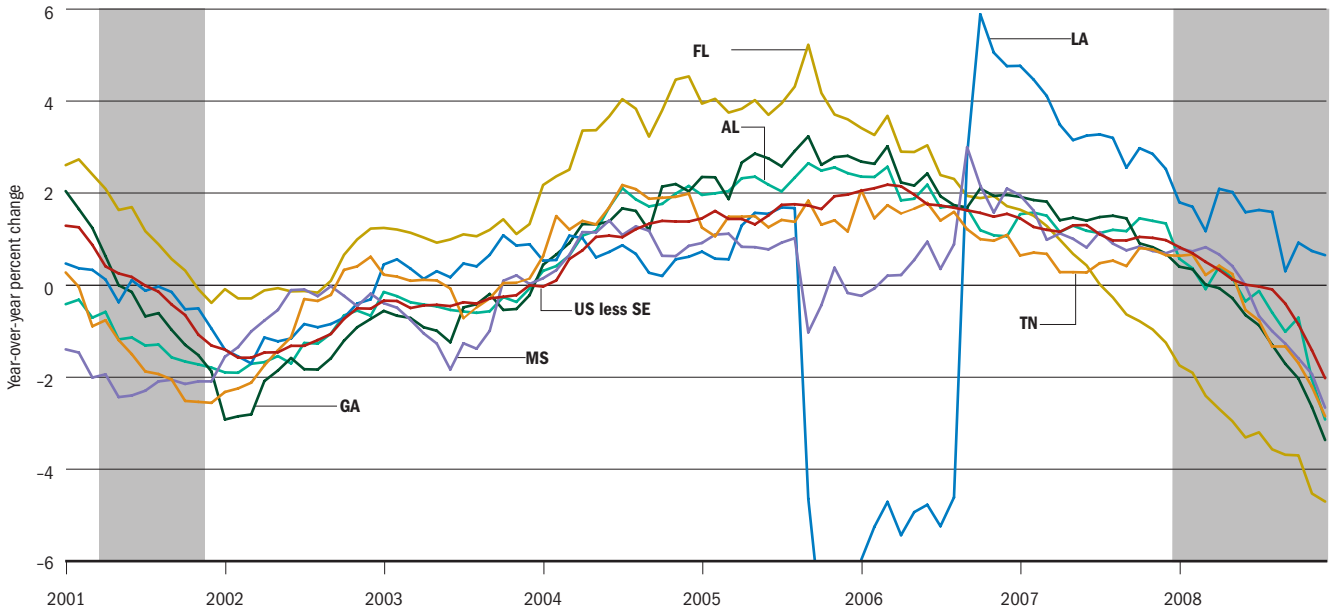
All told, the six states of the Southeast shed 674,000 jobs in 2008 (chart 1). The decline started early, and job losses accelerated in the final quarter of 2008. A quarter million net jobs were lost in the fourth quarter alone.

As the year ended, there were few positive signs. A shrinking employed workforce and rising ongoing unemployment insurance claims indicated that jobless people were having difficulty finding new work.

While payroll employment shrank in most southeastern states, Florida experienced the worst losses. Notably, employment in the Sunshine State's once robust construction industry in 2008 dipped to its lowest level since 1991. In the fourth quar-

Chart 1

Southeastern Employment Growth



Note: The gray bars indicate recessions.

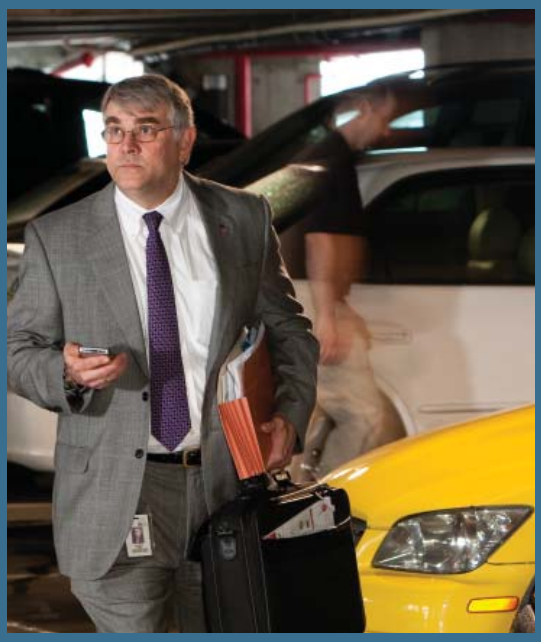
Source: U.S. Bureau of Labor Statistics and Federal Reserve Bank of Atlanta

The Financial and Economic Crisis: A Timeline of Events and Policy Actions

2007

July 11: Standard and Poor's places 612 securities backed by subprime residential mortgages on a credit watch.

Source: Abridged from "The Financial Crisis: A Timeline of Events and Policy Actions," Federal Reserve Bank of St. Louis (stlouisfed.org)



Joseph Hale

Community bank safety and soundness examiner covering institutions in Georgia and north Florida

Eight years of service

For most of the eight years he's been with the Atlanta Fed, Joseph Hale was able to leave his work behind at the end of the day.

"But that's not the case any more," Hale says. "We all want to see banks do well, and we want to be part of the solution to turning around the economy. So sometimes we take those worries home with us in the evenings."

There was plenty to worry over in 2008. Among the sixty-one community banks (those with under $10 billion in assets) that the Atlanta Fed regulates, there was a roughly fourfold increase in the number of troubled institutions, according to FDIC data.

For examiners like Hale, who are on the front lines in the Fed's efforts to safeguard the safety and soundness of the nation's financial system, troubled banks mean an intensified work schedule. In normal times, examiners thoroughly check a bank every twelve to eighteen months. When a bank's condition deteriorates, the Fed initiates some type of on-site examination activity at least every six months.

That means longer, more stressful hours for Hale and his fellow examiners. There are sometimes difficult dealings with bank executives and directors and more frequent meetings with bank boards of directors. At those meetings, examiners reveal overall soundness metrics that gauge capital adequacy, asset quality, and earnings, among other measurements.

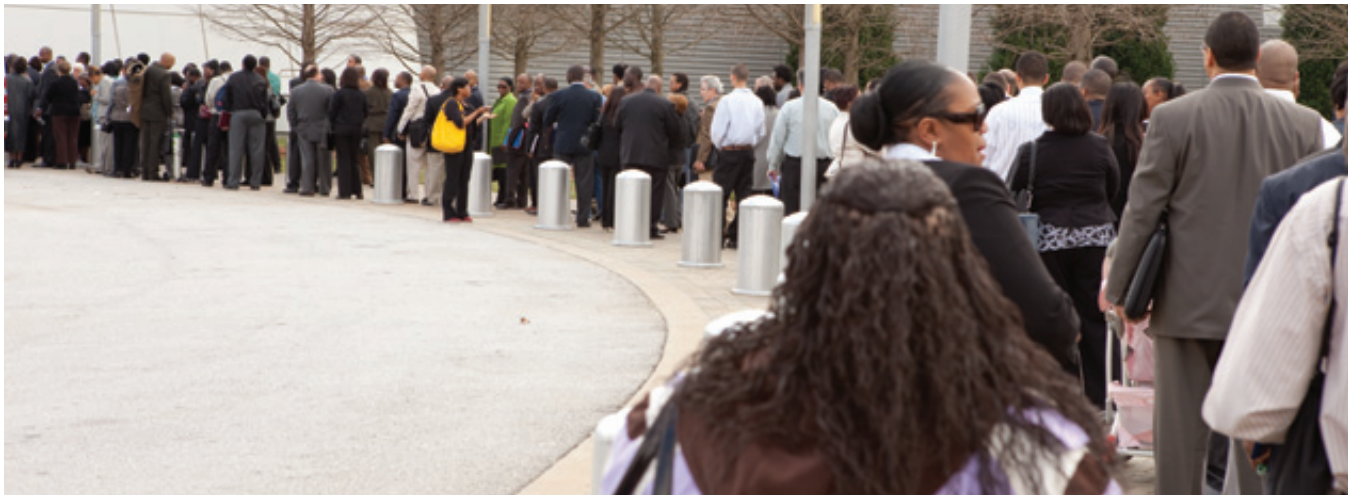
During the financial difficulties of 2008, those meetings centered on asset quality, in particular on loans ninety days or more past due, which are known as classified assets. Ideally, the examiners' findings concerning classified assets are no surprise to a bank's board.

That was usually the case in 2008. In contrast, meetings in late 2007 had often been tense as widespread problems related to real estate development lending began to surface. "There was some resistance to our recommendations then," Hale says. "Now, everybody pretty much has been affected, especially in the Sixth District."

To help affected institutions cope with deteriorating loan quality, Fed examiners will recommend various measures. To strengthen underwriting standards, for instance, Hale might recommend that a bank track its real estate loans in greater detail.

Rather than simply lumping loans together under a general "commercial real estate" category, he would advise a bank to stratify loans based on risk: loans made to a developer to buy land or to a builder to construct houses, loans to build hotels or convenience stores, or loans to develop owner-occupied commercial properties. Then, the bank might be asked to place internal limits on its lending volume in each of those more precisely defined classes of loans.

In retrospect, for community banks the lessons from one of the most severe crunches since World War II may boil down to fundamentals. "Usually," says Hale, "the problems we've seen involved excessive risk taking and trying to show better numbers than the bank down the street."



With unemployment rising in the Southeast, an estimated 3,000 job seekers stood in line at just one fair, the South Fulton Bilingual and Diversity Job Fair held in College Park, Georgia, just outside Atlanta.

ter of 2008, Florida also reported the highest number of layoffs of fifty or more jobs on record in the state. For all of 2008, Florida lost more than 375,000 jobs. The state had added 275,000 jobs as recently as 2005, before employment growth started to decline.

Florida's neighbor to the north fared little better. In Georgia, job losses in 2008 were spread among most economic sectors but were heaviest in manufacturing, construction, and business services. In December the state's unemployment rate reached 7.5 percent on a seasonally adjusted basis, the worst reading since 1983. This downturn came after Georgia had added more jobs between 2003 and 2006 than all but six other states, including Florida.

The news was better in Alabama, which maintained modest job growth for most of 2008, but even there employment started falling after the third quarter. In Louisiana, employment remained positive, but growth was much slower than during the post–Hurricane Katrina recovery. Meanwhile, Tennessee and Mississippi began losing jobs in the spring in most sectors.

Regionwide, the unemployment rate had begun climbing in the spring of 2007. By the end of 2008, the jobless rate in the Southeast as a whole, as well as in Alabama, Florida, Georgia, and Tennessee individually, was the highest since the early 1990s. Unemployment in the region was above the national average for most of the year.

Out of service

One factor that provided a cushion during past downturns was no comfort in 2008. Service-sector employment growth no longer offset losses in goods-producing industries. In fact, in most southeastern states annual growth in services employment in 2008 was no better and in some cases worse than during the 2001 recession.

The region's public sector eliminated jobs too. Governments across the Southeast, as elsewhere in the nation, pared payrolls because tax revenues declined along with consumer spending. In Georgia, for instance, by December governments were hiring at their slowest pace since the early 1980s. In November the city of Atlanta, like many municipalities across the country, announced a plan to adopt four-day work weeks, even furloughing police officers, in the face of declining tax collections.

Real estate takes a tumble

Like the region's workers, the Southeast's housing markets were hit hard, most notably in Florida and Georgia. In several areas of the region, existing home sales and inventories of homes for sale began to stabilize later in 2008. Yet even that good news was tempered by the reality that lender-owned foreclosed houses crowded the market and depressed prices (chart 2).

August 17: The Federal Reserve Board votes to reduce the primary credit rate 50 basis points to 5.75 percent, bringing the rate to only 50 basis points above the Federal Open Market Committee's (FOMC) federal funds rate target.

September 18: After holding the rate steady at 5.25 percent for fifteen months, the FOMC reduces its target for the fed funds rate by 50 basis points to 4.75 percent.

October 31: The FOMC reduces its fed funds target rate to 4.50 percent.

During the fourth quarter, for example, existing home sales in Florida climbed 12.5 percent above a weak year-earlier period. But the average price tumbled 24 percent. Industry contacts told the Atlanta Fed that houses foreclosed by financial institutions accounted for up to half those sales.

Falling prices and scarce sales also plagued Georgia, particularly the once-booming metro Atlanta market. Over the past decade, no metro area in the country issued more single-family building permits than Atlanta. But since peaking in 2005, the number of permits issued slid 91 percent through the fourth quarter of 2008.

In Georgia, the value of new residential construction contracts plunged to $6.6 billion in 2008 from $11.8 billion in 2007 and $16.3 billion in 2006, according to McGraw-Hill Construction, a compiler of industry news and data. In Florida, new contracts fell to $13 billion from $22.3 billion in 2007. The combined value of residential and nonresidential construction projects in the Sunshine State in 2008 was roughly $34 billion, or less than half the 2005 level of $71.7 billion, according to McGraw-Hill Construction estimates.

As demand dried up, many home builders closed or were forced into bankruptcy. In September 2008, the Greater Atlanta Homebuilders Association reported its membership had shrunk 22 percent in two years.

The effects of foreclosures and bank-owned houses flooding the market were not contained to Florida and Georgia. In markets across the Southeast, home prices fell, and access to financing was limited.

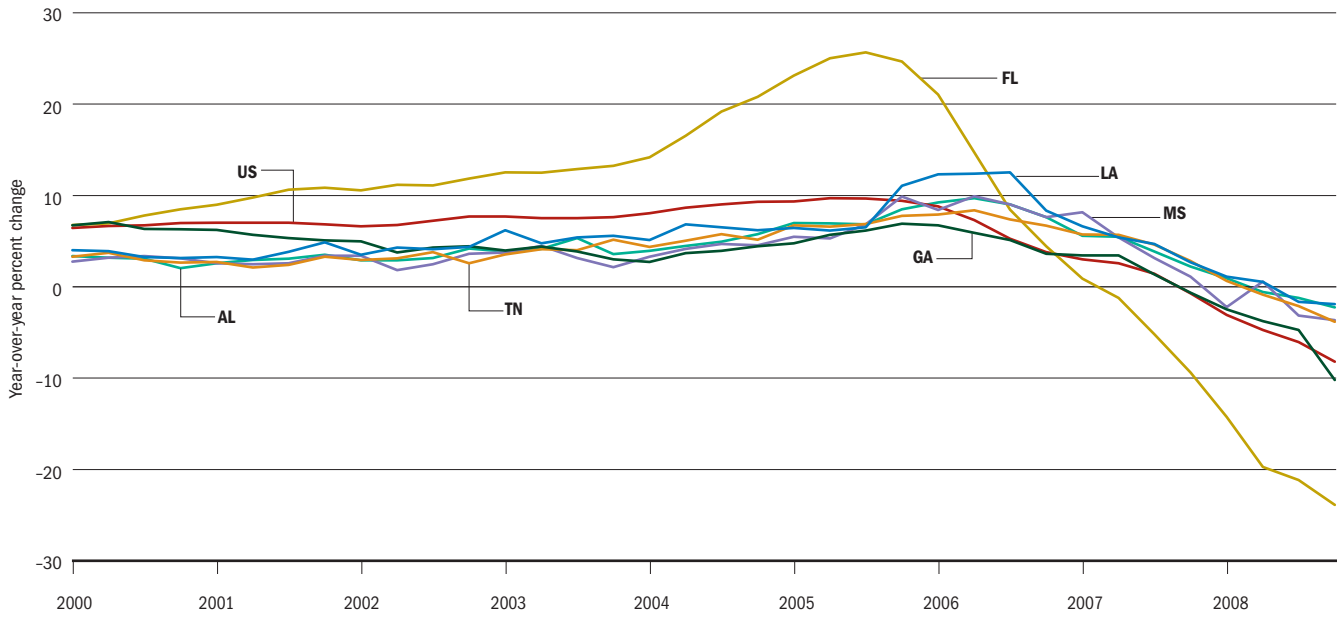
Commercial real estate saw shrinking demand

The commercial real estate industry, another pillar of the southeastern economy, was bedeviled in 2008 by the same forces that crippled the housing market and the broader economy—job losses, thriftier consumers, and frozen capital markets.

Commercial contractors reported fewer projects in their backlogs, especially in Florida. Not surprisingly, more bidders, including some idle residential builders, chased less work, forcing prices down. By the middle of the year, more construction projects were being postponed or canceled. Worried consumers spent

Chart 2

Existing Home Prices



Source: Federal Housing Finance Agency

December 12: The Fed Board announces the creation of a Term Auction Facility (TAF), providing longer-term credit to banks. The FOMC authorizes temporary reciprocal currency arrangements (swap lines) with the European Central Bank and the Swiss National Bank.

2008

January 11: Bank of America announces it will purchase Countrywide Financial in an all-stock transaction worth $4 billion.

Janet Hamer

Senior community development specialist, Jacksonville

Seven years of service

Janet Hamer has a meeting in a couple of days that she knows could be unpleasant.

A community development financial institution with an excellent track record is nonetheless having trouble maintaining its funding. The institution's mission is to pool capital from numerous sources and make loans for affordable housing and other community development projects. For more than a decade, it has performed well—earning returns, improving communities, and helping banks comply with the Community Reinvestment Act.

In 2008, however, some deals soured. Thus, banks are reluctant to continue funding the community lender. Community development lending is never straightforward, and so it may be one of the programs financial institutions look to scale back in a difficult economy. "And that's what they're doing," Hamer says.

As a community development specialist, Hamer convenes various players—commercial bankers, government officials, officials of nonprofits—to form partnerships, and she promotes financial literacy focusing on the importance of being "banked" throughout north and central Florida.

In prior years the groups with which Hamer works prospered. "It really was easier," she says. "And it was very gratifying that a lot of nonprofits I work with were buying land and doing their deals."

Then came a foreclosure crisis, financial turmoil, and recession.

So rather than introducing potential partners in community development investments, during a typical late 2008 day, Hamer trades ideas with colleagues about helping people whose homes are in foreclosure. She meets with a Jacksonville group that helps lower-income people join the economic mainstream.

During and after that meeting, the talk is of a weak job market and, on a happier note, of new grant funding. Community groups in larger cities, Hamer explains, are far better funded than those in smaller cities and rural areas, particularly in a sagging economy.

The poor economy and foreclosure crisis have not only reoriented Hamer's work toward what she calls asset preservation and away from the traditional mission of asset building, but these developments have also stalled new initiatives.

Take, for example, the Atlanta Fed's plans to encourage lenders to finance energy-efficient building. The "green lending" concept is so new it lacks some essential elements. Yet for builders, financial institutions, and the Fed, work on green lending has been delayed by more urgent financial concerns.

Still, for all the havoc the recession and foreclosure crisis have wrought, positives could emerge. Hamer believes that many subprime borrowers could have qualified for more favorable traditional mortgages had they been more informed and therefore not enticed by often misleading advertising.

"If anything ever said we need financial education in this country," she says, "this says it."

Home sales were hard to come by in parts of the Southeast, particularly in once-booming metro Atlanta and throughout Florida.

less, undercutting the need for new shopping centers, while demand for office space and access to financing also shrank.

Construction industry woes were bad news for workers. Construction employment in the Southeast in 2008 dipped more than 14 percent from the year before.

Banking buffeted by financial storm

Shock waves emanating from Wall Street and residential real estate markets rattled the financial sector in the Southeast and the nation in 2008.

Many of 2008's problems surfaced in 2007—falling home prices, rising mortgage defaults, and foreclosures that led to losses at banks and other financial institutions. During 2008, U.S. financial firms absorbed write-downs and credit losses totaling more than $650 billion, according to Bloomberg News.

Financial and economic currents in 2008 fed a vicious cycle that played out in the region and throughout the nation: Poor economic conditions and weak employment contributed to further deterioration in residential mortgage loans and reduced the quality of many other types of loans. Riskier borrowers led cautious lenders to tighten underwriting standards and demand higher interest rates, further restraining economic growth.

Financial institutions in the Southeast were not spared. At large banking companies, deteriorating real estate loan portfolios led to higher loan losses and lower earnings. Many banking firms reduced their dividends to shareholders. The situation was equally difficult for community banks, defined as those with under $10 billion in assets. Among sixty-one community banks the Atlanta Fed supervises, the number of troubled institutions, as classified by the Federal Deposit Insurance Corporation (FDIC), more than doubled during 2008.

Other financing mechanisms, such as commercial paper, also were sharply curtailed. The Federal Reserve in 2008 took numerous steps to try to address this lack of liquidity in the economy (see the sidebar on page 8).

Financial institutions in the Southeast particularly suffered in 2008. During the fourth quarter, for instance, the share of unprofitable banks in the region rose 27 percent from a year earlier, to just under 50 percent. A key measure of bank profitability, return on average assets (ROAA), tells the tale. Since its cyclical peak in the middle of 2006, the median ROAA for banks in the region had dropped by 87 basis points by the fourth quarter of 2008, a much steeper decline than for banks outside the Southeast.

An ROAA of at least 1 percent is generally considered a mark of strong profitability. By the October–December period of 2008, nearly 80 percent of southeastern banks, compared to just over half a year earlier, reported an ROAA below 1 percent.

The major reason for this decline was a deterioration in asset quality as the year progressed. By the fourth quarter,

January 22 and 30: The FOMC lowers the fed funds target rate to 3.5 percent and eight days later reduces it another 50 basis points to 3 percent.

February 13: President Bush signs the Economic Stimulus Act of 2008 into law.

March 11: The Fed announces the creation of the Term Securities Lending Facility (TSLF).

The Fed devises unprecedented responses

The Federal Reserve in 2008 took several innovative steps to address strains in the financial system. While the Fed actions in many cases went beyond traditional monetary tools, they are grounded in a coherent strategy of targeted credit policy.

A series of cuts in the federal funds rate, totaling more than 500 basis points, that began in September 2007 brought the rate to a range of 0 to 0.25 percent as of December 2008.

The Federal Reserve also enacted a variety of policies to help systemically important credit markets resume normal functioning. Starting in August 2007, these measures have been designed to address problems in three critical areas of the financial system—financial institutions, borrowers and investors in key credit markets, and longer-term securities.

Programs to support financial institutions included changes in the Federal Reserve discount window: lowering the discount rate relative to other interest rates; an auction program allowing financial institutions to access funds without some of the stigma associated with discount window lending; longer-term loans and availability of credit to a wider range of institutions; and the acceptance of less liquid collateral. In addition, the Federal Reserve initiated a series of reciprocal currency swaps with sixteen foreign central banks to improve dollar liquidity in global financial markets.

Meanwhile, the Fed targeted two key credit markets. Some of the strain in the market for short-term debt could be traced to money market funds, which are significant buyers of commercial paper—short-term promissory notes that corporations and financial institutions use to finance day-to-day operations. Significantly, money market funds link investors seeking a return with businesses looking to sell their short-term debt.

To help stabilize the commercial paper market and money market funds, the Federal Reserve created three facilities. The Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility provides funding to U.S. depository institutions and bank holding companies to finance their purchases of high-quality asset-backed commercial paper from money market mutual funds. The Commercial Paper Funding Facility provides liquidity to U.S. issuers of commercial paper. And the Money Market Investor Funding Facility supports a private-sector initiative to provide liquidity to investors in U.S. money markets.

Finally, to support longer-term securities, the Fed announced programs to purchase asset-backed instruments, including mortgage-backed securities backed by Fannie Mae, Freddie Mac, and Ginnie Mae, and student loans, small business loans, and credit card receivables. The ability to package and sell such credits in the form of securities is essential to ensure that consumers and businesses have broad access to credit. ▮

3.83 percent of all loans were noncurrent—more than ninety days past due and not accruing interest. That number was more than double the percentage a year earlier and well above the peak during the 2001 recession.

As the financial crisis deepened, some banks closed and reopened under different banners. Seven banks in the Southeast failed and were shut down by regulators in 2008, equal to the number in the previous eight years combined.

Meanwhile, companies had trouble securing financing from sources other than banks. Firms turning to the corporate bond market found it costlier to issue debt to investors, who were skittish about the economic outlook. Consequently, many companies apparently deferred issuing new bonds. In August 2008, for instance, investment grade bond issuance totaled just $26.5 billion nationally compared to average monthly issuance of about $83 billion in 2007, according to the Securities Industry and Financial Markets Association.

Consumer spending slumps

In some previous recessions, consumer spending remained strong and helped the economy turn toward recovery. But in 2008, consumer spending suffered along with the rest of the economy, in part because more people were out of work and because shoppers cut back as prices climbed for commodities like food and energy. Nationally, retail sales fell 8 percent year over year in the fourth quarter of 2008. In Florida and Tennes-

March 14: The Fed approves the financing arrangement announced by JPMorgan Chase and Bear Stearns.

March 16: The Fed establishes the Primary Dealer Credit Facility (PDCF).

March 18: The FOMC lowers the fed funds target rate to 2.25 percent.

April 30: The FOMC lowers the fed funds target rate to 2 percent.

Galina Alexeenko

Senior economic policy analyst

Four years of service

As a senior economic analyst at the Atlanta Fed, Galina Alexeenko found her normal work routine scrambled in 2008.

Before financial crisis and recession gripped the globe, Alexeenko was a specialist. She tracked global economics—mainly trade—and its impact on the United States and the Southeast. Her duties were reasonably clear-cut and constant: She dissected and decoded streams of data and anecdotal information in search of long-term trends.

Every week or so, she joined a team of analysts and economists to brief the Atlanta Fed president as part of the preparations for his participation in Federal Open Market Committee meetings. In those briefings, Alexeenko reported on trade flows, currency fluctuations, and other vital signs from the international economy.

All that changed in 2008. When financial markets went haywire in October, the once-a-week briefings became daily affairs. Atlanta Fed President Dennis Lockhart was hungry for insight and information as conditions shifted, literally minute by minute. For Alexeenko, work grew in volume and breadth. No longer did she concentrate solely on global economics. Events hurtled forward so fast that the demands of the moment superseded long-term projects.

For example, Alexeenko and her colleagues were called upon to prepare reports on specific topics that became urgent. It might be commodity prices one week, global trade finance the next. At the behest of Lockhart, she and other analysts and economists explored whether and how the financial crisis and recession might affect the saving habits of Americans in coming years.

A former analyst of the U.S. economy, Alexeenko also became reacquainted with domestic economic indicators such as new home sales and durable goods orders. Always important, financial markets took center stage at all times. After concerns about European banks' exposure to Eastern European economies buffeted financial markets, Alexeenko and a team of analysts were charged with studying the impact on the American economy of problems in emerging markets.

"What this crisis clearly illustrates is how interdependent everything is," said Alexeenko, a native of Ukraine.

In addition to markets and economies, the Fed watches its peers. As the gears of the global economy balked, Alexeenko and her colleagues paid close attention to the policy actions of other central banks. Recession and financial turmoil have, for Alexeenko, underscored her view that the actions of the Federal Reserve are hugely influential in the course of the U.S. economy and thus in the lives of Americans at all socioeconomic levels.

"There has always been pressure to perform, but the stakes have been raised," Alexeenko said of the economic condition. "You want to make sure Dennis is well informed and his decisions are based on the best analysis possible."

Southeastern states account for one-third of U.S. oil production, so when energy prices drop globally, the region feels the pinch. Pictured is the Mars platform (a joint venture of Shell Oil and BP), currently the largest producing oil platform in the Gulf of Mexico.

see, state sales tax revenue, a useful proxy for spending, was down in each quarter of 2008 compared to 2007 (chart 3). In Georgia, sales tax revenue rose slightly in the fourth quarter after declining during the previous three quarters. Mississippi and Louisiana collected more sales taxes during 2008 than in 2007, yet even in those states growth was down from 2006.

As in virtually every other measure of economic activity, Florida suffered the region's biggest hits in consumer spending. Florida's sales tax revenues, which have declined steadily since a peak in 2005, slipped 4.1 percent for 2008 compared to 2007.

Auto sales were especially weak. From January through December, the number of new vehicles registered in the Southeast plummeted 21.5 percent from a year earlier compared to an 18.3 percent drop nationally.

Energy all over the map

The year 2008 was likely one of the most volatile ever in global energy markets. After scarce supply and ravenous demand especially in emerging market economies sent prices to record heights early in the year, by late in 2008 tight credit and the slowing economy sapped demand and prices.

Energy is, of course, important to the Southeast not just to fuel vehicles and heat, cool, and light homes and businesses. Three states in the region—Louisiana, Mississippi, and Alabama—combined with federal waters in the Gulf of Mexico, account for more than a third of the nation's oil production and almost half of U.S. refining capacity, according to the Energy Information Administration of the U.S. Department of Energy. The Henry Hub in Louisiana is the nation's largest natural gas trading center, while the Louisiana Offshore Oil Port is the only U.S. port that can accommodate the world's largest oil tankers.

Therefore, when global energy markets move, the Southeast feels it. And move they did in 2008. Energy costs crested in the summer as the price of light sweet crude oil topped $145 a barrel. That price sent the average U.S. price of regular gasoline to $4.11 a gallon in July, a record even in inflation-adjusted terms, and almost 40 percent higher than the summer 2007 average.

Even amid the gyrations in the energy markets, among the signature events of 2008 were two hurricanes that temporarily shut down much of the region's energy infrastructure. By some estimates, Hurricanes Gustav and Ike damaged oil production and refining as much as Katrina and Rita did in 2005 (chart 4).

The 2008 storms closed many of the region's refineries for a couple of weeks, and even without damage, closed refineries can take several weeks to restart. In the wake of Ike and Gustav, the nation's refinery utilization rate dropped to its lowest level on record, 66.7 percent, meaning domestic refineries processed record-low amounts of crude oil. Hurricane-related

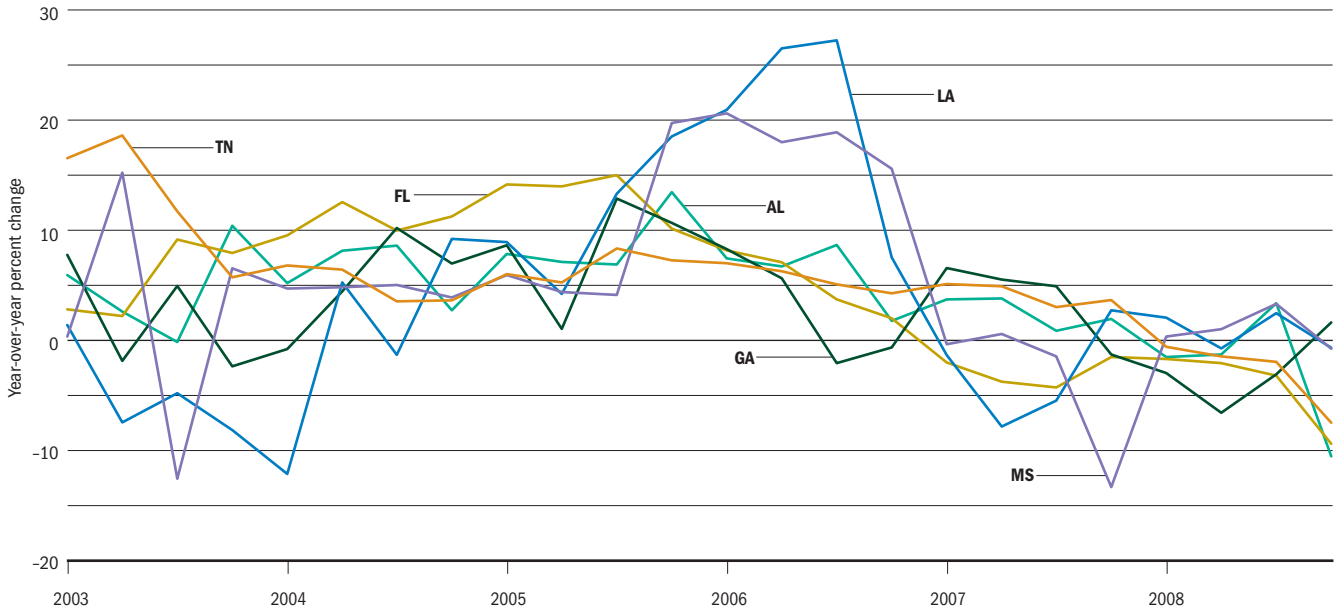
July 11: The Office of Thrift Supervision closes IndyMac Bank, F.S.B.

July 30: President Bush signs the Housing and Economic Recovery Act of 2008 into law, which, among other provisions, authorizes the Treasury to purchase GSE obligations (such as Fannie Mae and Freddie Mac obligations) and reforms the regulatory supervision of the GSEs under a new Federal Housing Finance Agency.

August 17: After its meeting, the FOMC releases a statement noting that the "downside risks to growth have increased appreciably."

Chart 3

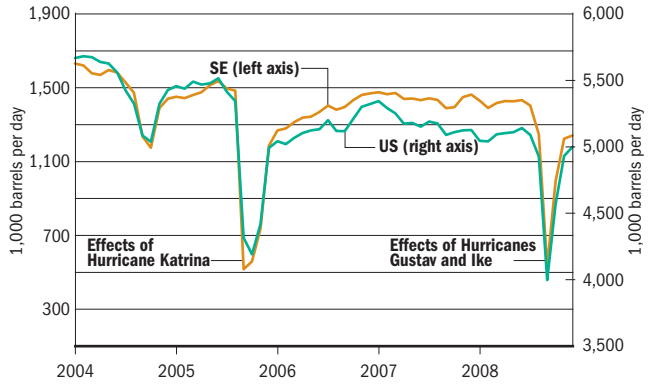
Retail Sales Tax Revenues



Source: State Departments of Revenue (for Alabama, Florida, Georgia, Louisiana, and Tennessee) and Mississippi State Tax Commission

Chart 4

Total U.S. Estimated Crude Oil Production



Note: Data represent a four-week moving average.

Source: *Oil and Gas Journal*

outages wiped out some 14.5 million barrels of crude production in 2008, equal to about three days of total U.S. output, the EIA estimated.

Tourism held up regionally . . . mostly

Tourism was one of the few bright spots in the southeastern economy through much of 2008 before slipping late in the year. International travelers flocked to the region, while Americans traveled less because of high fuel prices, rising airfares, and recession.

A weaker dollar attracted vacationers from other countries in greater numbers through most of the year. International flights added seats in advance of the peak travel season in December, while domestic carriers pared capacity at some southeastern airports.

Especially in Florida, tourism was fueled by foreign visitors. In Miami-Dade County, international tourists accounted for nearly 45 percent of the market in the first half of 2008. International passenger traffic at the Miami International Airport for the year increased 3.9 percent even though it tapered off starting in September because of hurricanes and the financial crisis. Domestic passenger volume, meanwhile, declined 1.6 percent.

September 7: The Federal Housing Finance Agency places Fannie Mae and Freddie Mac in government conservatorship.

September 15: Bank of America announces its intent to purchase Merrill Lynch & Co. for $50 billion.

September 16: The Federal Reserve Board, acting under emergency provisions of the Federal Reserve Act, authorizes the New York Fed to lend up to $85 billion to American International Group (AIG).

Jay Repine

Supervision and Regulation subject matter expert, Miami

Seventeen years of service

It's all about lights and patios.

Soaring stacks of patios have risen all over Miami in the past few years. The problem: Many of those balconies sit empty, like the gleaming new condominiums to which they are attached. Granted, it's highly unscientific, but checking for patio furniture—or for lights at night—makes it painfully clear that many of Miami's 22,000-plus condos built since 2003 sit vacant.

Huge numbers of condos are dark with bare balconies, and to make matters worse hundreds more will be completed during 2009. Thus, Miami has become the epicenter of the real estate glut in the Southeast and one of the nation's most overbuilt markets.

As a result, Repine saw his job and his colleagues' jobs transformed during 2008. "There were people here who before this year had rarely seen a problem loan," Repine said. They saw plenty during 2008.

For Repine, the economic tremors radiating from south Florida's condo boom upended the normal work day. Before the upheaval in the financial services industry, he had devoted more than half his time to anti-money-laundering work—a major focus, along with international banking analysis and monitoring, of the Miami team. While he still must carve out significant hours in the day for those critical functions, his workday is different now.

Repine's work changed in 2008 as he and other international and anti-money-laundering specialists found their regular duties had to share time with significant work examining local and regional financial institutions, gathering and analyzing information in an attempt to untangle the causes of a financial downturn that emerged quickly and worsened even faster.

To that end, during the late fall of 2008 Repine compared notes on market conditions several times a week with contacts at global financial institutions. In more normal times, he made those calls only in advance of the Federal Reserve's Federal Open Market Committee meetings, which are scheduled eight times a year.

During calls one day in early December, Repine's contacts delivered some very bad news: Loan demand had all but evaporated as corporate borrowers deferred taking on debt. Banks had little appetite to lend and expected additional businesses to face hard times after the first of the year. Investors large and small remained suspicious.

In another meeting with Atlanta Fed colleagues, the talk was of difficult discussions with financial institution managers and of condo towers with so few residents that owner association fees were skyrocketing.

A few encouraging signs emerged from Repine's discussions. As of year's end, large money market mutual funds, for instance, were gradually putting money to work again. Nevertheless, pessimism prevailed.

After one call with a gloomy banker, Repine said that before the financial turmoil began, his contact "couldn't think of a way to lose money." In 2008, it was hard to think of a way not to.

A bright spot in 2008, New Orleans tourism was generally good at events like Mardi Gras.

At the Orlando International Airport, international passenger volume for the year rose 17 percent even as domestic traffic fell 3.5 percent.

Strong early, travel took a hit late in the year. In November, the Orlando market's hotel occupancy rate plunged 15 percent from the same month in 2007, to 53 percent, the biggest one-month decline since November 2001. Although the rate rose slightly year over year in December, Orlando's hotel occupancy levels for 2008 were 3 percent lower than the year before. Room rates also fell nearly 9 percent in December from a year earlier, and revenue per room was off 3.8 percent.

In New Orleans, the all-important tourist business was generally good. Large crowds came for the city's signature events, including Mardi Gras and the Jazz and Heritage Festivals. The French Quarter Festival in April and the month-long Essence Music Festival in July set attendance records. Bugs, normally a nuisance, actually lured visitors to the Crescent City in 2008. The $25 million, 23,000-square-foot Audubon Insectarium opened in June, drawing more than 100,000 visitors in its first two months.

Traffic at New Orleans's Louis Armstrong International Airport for 2008 was up 5.5 percent from the year before. But as was the case in Florida's tourist centers of Orlando and Miami, New Orleans passenger traffic slowed in step with the economy in the fall but picked up slightly in December.

Just east of New Orleans, the Mississippi Gulf Coast's gaming industry suffered from post-hurricane closings in August and September, high gas prices, and the generally sluggish economy. Gross gaming revenues at the eleven coastal casinos declined 7.5 percent for the year, according to the Mississippi State Tax Commission.

International trade held firm

International trade has been a beacon in the economic clouds the past couple of years in the nation and the Southeast, helping to offset weaknesses elsewhere.

The value of international shipments through the region's ports increased in 2008 from 2007, and several southeastern ports are expanding. Exports grew by 10 percent or more at every port in the region in 2008, according to the U.S. Department of Commerce (chart 5). Southeast exports jumped more than 23 percent, thanks primarily to heavy demand from Canada, Mexico, Brazil, Europe, and China.

Southeastern ports also imported 15 percent more year over year in 2008 in terms of value of shipments, mainly because of higher commodities prices. While import values rose, volume actually declined at the region's ports.

Growing trade with Asia and investments here by foreign manufacturers led ports such as those in Savannah and Jacksonville to upgrade container facilities. Savannah is the

September 19: The Fed announces the creation of the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF).

September 21: The Federal Reserve Board approves applications of investment banking companies Goldman Sachs and Morgan Stanley to become bank holding companies.

September 25: The Office of Thrift Supervision closes Washington Mutual Bank, and JPMorgan Chase acquires its banking operations in a transaction facilitated by the FDIC.

REIN gets to the roots of the Southeast economy

The Atlanta Fed took a significant step in 2008 to strengthen the Bank's contribution to the nation's monetary and economic policymaking: the establishment of the Regional Economic Information Network, or REIN.

Created to enhance the Atlanta Fed's knowledge of the Southeast's economy, REIN has two components—an online repository of southeastern data and analysis, updated monthly, and the Local Economic Analysis and Research Network (LEARN).

Those elements make REIN a natural extension of the regional Federal Reserve Bank's historic mission to feed independent and diverse economic intelligence into the nation's monetary policymaking process. In many ways, the Sixth Federal Reserve District is particularly well suited to take advantage of regional information gathering: It is populous, with 46 million residents; it is geographically large; and it is economically diverse, from tourism in Florida and New Orleans to professional services in Atlanta to automotive manufacturing in Alabama. That diversity makes it reasonably representative of the national economy.

What's happening now

By extending its reach deeper into local economies throughout the Southeast, the Atlanta Fed gains a better sense of what might show up weeks or months later in official statistics. Timeliness is especially important during an economic downturn because statistical evidence of a turnaround often does not emerge until well after recovery has begun.

REIN filters information to the bank's Atlanta headquarters through a structure built geographically—with a presence at each of the Atlanta Fed's five branch offices—and around particular industries.

The Atlanta Fed's Regional Executive at each branch office convenes a regional advisory council. The councils, some convening in 2008 and some to begin work in 2009, are assembled around an important local industry, and participants provide insight from their business experience and contacts. The regional advisory councils and the offices running each are energy, New Orleans; trade and transportation, Jacksonville; tourism, Miami; agribusiness, Birmingham; small and midsize entrepreneurial business, Nashville; and health care, education, and labor, Atlanta.

nation's fastest-growing container port, according to the American Association of Port Authorities. And Jacksonville's container capacity could triple by 2011, as Japanese and Korean shippers add terminals at the port.

Ports on the Gulf of Mexico are growing too. The Port of Mobile in Alabama is expanding container capacity to accommodate shipments to and from the $4.2 billion ThyssenKrupp steel processing plant that is scheduled to open near Mobile in 2010.

Manufacturing decline continues

ThyssenKrupp can't arrive soon enough. The woeful housing market, tepid automobile sales, credit strains, and the effects of the recession spelled a difficult year for southeastern manufacturers. However, energy-related manufacturers and exporters generally fared better than others.

One measure of the decline is Kennesaw State University's monthly Southeast Purchasing Managers Index (PMI) (chart 6). A reading above 50 indicates growth in manufacturing; under

October 3: Congress passes and President Bush signs into law the Emergency Economic Stabilization Act of 2008 (EESA), which establishes the $700 billion Troubled Asset Relief Program (TARP).

October 7: The FDIC announces an increase in deposit insurance coverage to $250,000 per depositor as authorized by the EESA. The Fed announces the creation of the Commercial Paper Funding Facility (CPFF).

October 8: The FOMC lowers the target for the fed funds rate to 1.50 percent.

The Atlanta Fed's Regional Executives are key players in REIN. As the mission of the branches has evolved, the Regional Executive's duties have also transitioned from an operational role centered on running the branch to a position more concerned with gathering economic intelligence and representing the Federal Reserve Bank of Atlanta.

The five Regional Executives work closely with their branch board of directors, cultivate business contacts in their communities, deliver speeches, and generally serve as the face of the Atlanta Fed in their respective areas. In this way, the Regional Executives help the Reserve Bank serve its constituencies on a more personal level and at the same time gain insight into how businesses affect and are affected by the economy.

Under the auspices of REIN, the Regional Executives have become part of the Atlanta Fed's Research Department. To stay abreast of economic and business data and trends, the Regional Executives spend considerable time exchanging ideas and information with the Reserve Bank's analysts and economists.

REIN also brings greater structure to the Reserve Bank's monthly surveys of businesses. These include industry-focused questionnaires answered by home builders, real estate agents, retailers, and manufacturers. While the surveys are not new, REIN has helped to increase the number of participants and made it easier to assimilate the information the surveys produce on moods and expectations in the marketplace.

LEARN keeps Fed's ear to the ground on campus

Another component of the REIN initiative is LEARN, a forum for academics and researchers with detailed knowledge of local economies in the Southeast. The aim of LEARN is to create a nexus for discussing and exchanging ideas on research, methodologies, and current economic developments.

Through LEARN, the Atlanta Fed deepens its relationships with university economists and researchers and establishes a more systematic means of incorporating their research and expertise into monetary and economic policymaking.

Ultimately, REIN generates raw material for the vital work of formulating monetary policy. At the meetings of the Federal Open Market Committee, each Reserve Bank president makes a presentation about conditions in his or her region. With the advent of REIN, Atlanta Fed President Dennis Lockhart approaches those sessions armed with even more nuanced and textured grassroots intelligence. ∎

50 signals contraction. At the end of December, the regional PMI sank to 25.8. That reading slid as the year progressed: The average for 2008 was 44.4 versus 53.1 in 2007. The national average for 2008 was 45.5, so the Southeast underperformed the nation by this measure.

The Atlanta Fed's surveys of regional manufacturers painted a similar picture. Respondents reported weak production, shipments, and new orders compared to a year earlier. Most also continued to lay off workers and reduce hours.

Factory employment in the Southeast, as in the country at large, has fallen dramatically in the past few decades. In 1970 one in four workers in the region held a manufacturing job. By 2007 that share dwindled to one in ten.

By 2008 manufacturing employment for the year in the six southeastern states was down 8.1 percent from 2007, according to the U.S. Bureau of Labor Statistics. Employment in durable goods manufacturing declined 9.2 percent and dropped 6.4 percent in nondurable goods manufacturing.

October 12: The Fed announces its approval of an application by Wells Fargo & Co. to acquire Wachovia Corporation.

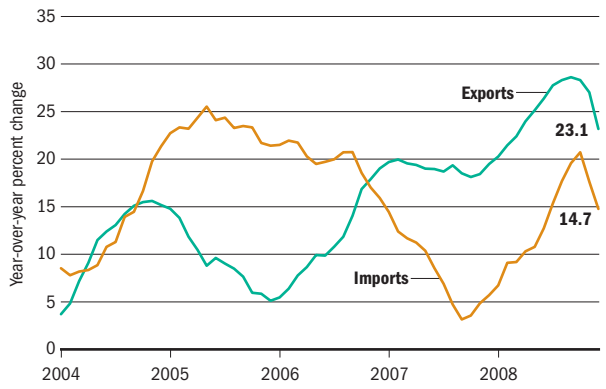
October 21: The Fed announces creation of the Money Market Investor Funding Facility (MMIFF).

October 28: The U.S. Treasury purchases a total of $125 billion in preferred stock in nine U.S. banks under the Capital Purchase Program.

October 29: The FOMC lowers the fed funds target rate to 1 percent.

Chart 5

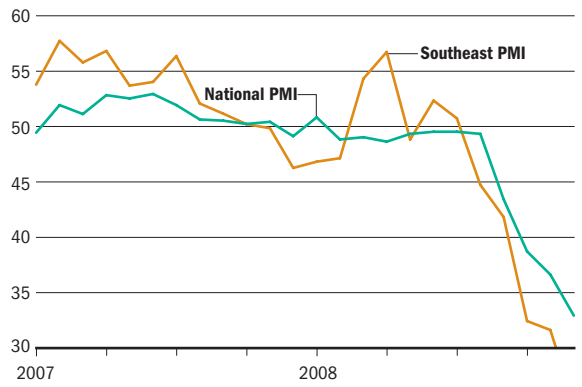
Growth of Southeastern International Port Shipments



Source: U.S. Department of Commerce

Chart 6

National and Southeast Purchasing Managers Indexes



Note: An index reading above 50 indicates expanding manufacturing activity, below 50, contracting activity.

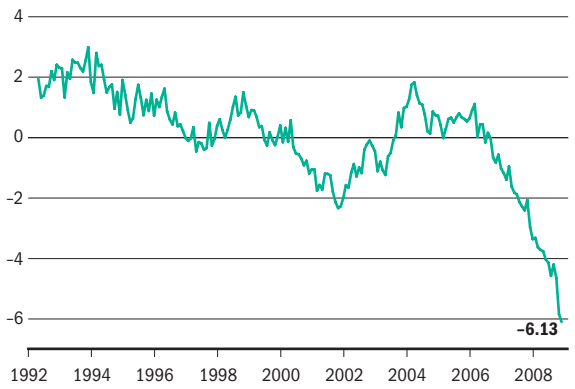
Source: Institute for Supply Management (national PMI); Kennesaw State University (Southeast PMI)

As expected, manufacturers that fed the boom in real estate and construction suffered in 2008. In December, employment at wood product manufacturers declined 17 percent in Alabama, one of the leading wood products centers in the region; 15.4 percent in Tennessee; and 9.5 percent in Mississippi.

Furniture factory payrolls in Alabama, Mississippi, and Tennessee were hit hard in 2008, with payrolls down at least 10 percent in each state.

Chart 7

The D6 Factor



Note: The D6 Factor is an index of southeastern economic trends. A negative value indicates that economic conditions are weak. The growth rate is normalized to zero.

Source: Federal Reserve Bank of Atlanta

Even the Southeast's recently ascendant automotive manufacturing industry did not escape the recession in 2008. For every auto factory job there are three in related suppliers, and these suppliers also lost jobs in 2008. In December, employment in the Southeast's transportation equipment industry was 8 percent lower than the year before; Tennessee was particularly affected.

On the flip side, employment in aerospace manufacturing continued to expand in Alabama and Florida in 2008.

Agriculture battles drought and the economy

Like most other industries, agriculture in the Southeast confronted an array of challenges in 2008. Drought, rising costs, a weak economy, and the battered housing market hindered growers of poultry, cotton, citrus, cattle and livestock, and greenhouse nursery operators.

With revenues exceeding $9 billion, poultry is the Southeast's biggest cash crop. But in 2008 domestic demand slackened as consumers spent less on groceries and on eating out, while costs rose for feed and other inputs. Exports were steady to China and Mexico, but demand from the top importer of U.S. poultry, Russia, softened for various reasons, including import restrictions.

Cotton production in the Southeast is also declining. For cotton, worldwide demand is critical because 75 percent of

November 25: The Fed announces plans to create the Term Asset-Backed Securities Lending Facility (TALF).

December 11: The Business Cycle Dating Committee of the National Bureau of Economic Research announces that a peak in U.S. economic activity occurred in December 2007 and that the U.S. economy has since been in a recession.

December 16: The FOMC votes to cut the effective fed funds rate to a target range of 0 to 0.25 percent.

Mark Craig

Director, Credit and Risk Management Department

Fourteen years of service

Since joining the Atlanta Fed in 1994, Mark Craig has never seen a year like 2008.

Craig's duties include cooperating with other financial regulatory agencies in resolving failed financial institutions in the Southeast. That duty has been rare: Only seven banks in the region failed from 2000 to 2007.

Then came 2008, when bank regulatory agencies shut down seven banks in the Southeast in a single year.

On the Friday before Thanksgiving, Craig worked long into the night after hearing from the Federal Deposit Insurance Corporation that a Georgia bank had failed. Craig's department lets the FDIC know what Fed services a failed institution received and what risk the Fed incurs, such as overdrafts on an institution's cash account with the Reserve Bank. Reserve Banks routinely allow banks to run overdrafts, usually only for a few hours, to keep the payment system functioning smoothly.

Banks also borrow from the Atlanta Fed's discount window, though that option is typically not available to severely troubled institutions.

The discount window is central to Craig's duties, never more so than in 2008. The Credit and Risk Department monitors the condition of some 2,000 southeastern depository institutions, including banks, savings and loans, and credit unions. Since these institutions are eligible to borrow through the discount window, Craig's unit tracks their creditworthiness.

Like helping to resolve the rare (until now) failed bank, managing the discount window has traditionally been an exercise in a comparatively low-volume facility. That's because banks historically viewed the discount window as a last resort to raise capital.

That view changed dramatically in late 2007 and through 2008. As financial institutions had an unusually difficult time obtaining funds through more common channels, the discount window was opened to more types of borrowers and offered more types of loans. Craig's team made discount window loans totaling $72 billion, far and away the most in a single year. By comparison, in 2007 they made loans worth $244.7 million. The Credit and Risk Department analyzed collateral for each of those loans and fielded phone calls from the borrowers.

Not only did loan volume soar, but terms also were extended from the traditional one-day loans to ninety days. "You have to do your homework because you don't want to have a loan out to a bank that appeared sound when the loan was made but then see its condition deteriorate within ninety days," Craig said.

Craig's team also administered an array of new Federal Reserve lending programs. For example, Credit and Risk staffers fielded calls from banks bidding on loans in the Term Auction Facility, through which the Federal Reserve lent about $150 billion every two weeks. Banks phoned in their bids, or the interest rate they were willing to pay. Atlanta Fed employees passed that information on to the New York Fed, which determined the winners and administered the loans.

Americans' appetite for poultry declined as producers' costs rose.

U.S. cotton production is exported. Cotton prices fell alongside global demand in 2008. Revenues for southeastern growers, along with the amount of land planted in cotton, have decreased. In 2008, cotton acreage in the region dipped to a twenty-five-year low of 9.4 million acres, 40 percent lower than in 2006. Most farmers have switched to more profitable crops such as corn and soybeans.

Little in the way of good news

In 2008 the southeastern economy struggled with many of the same problems that plagued the nation at large—financial market turmoil, housing market and credit crises, rising food and energy costs, and job losses. Indeed, when the United States officially entered recession in December 2007, according to the National Bureau of Economic Research, the Southeast's economy dipped below its worst performance during the past two recessions, as measured by the Atlanta Fed's D6 Factor (chart 7). Based on twenty-five monthly data series, the D6 Factor is a composite indicator of economic activity in the six southeastern states.

As the national and global economies worsened through 2008, so did the region's. After falling lower in December 2007 than the lows recorded during the 1991 and 2001 recessions, the D6 Factor index tumbled an additional 3.1 points through December 2008.

Economic factors that had buoyed the region's economy in previous years began to crumble. Southeastern employment in 2008 fell for the first time in five years, and by the third quarter the unemployment rate was at its highest level since the 1991 recession.

Some housing markets showed signs of stabilizing late in the year, but a fast recovery appeared unlikely. Tourism and exports, two relative bright spots in 2008, may fare less well if the strengthening of the dollar and the global economic slowdown that began late in 2008 continue. On the upside, plans for expansion in auto and aerospace manufacturing should help bolster the Southeast's economy in 2009.

Economics is often called the dismal science, and that epithet was especially deserved in 2008. In the Southeast as elsewhere, 2008 was as dismal economically as any year in recent memory. Neither the Atlanta Fed economists nor most others foresee a quick rebound from this recession. Yet the core resilience of the U.S. economy combined with the regenerative capacity of the financial system should ultimately carry us through these trying times.

2008 Milestones

Research hones its economic focus

- A team of research economists and analysts created the Regional Economic Information Network (REIN), and the roles of Atlanta Fed branch managers—retitled as regional executives—were expanded to include helping collect economic information used to formulate monetary policy.

- The bank's annual Financial Markets Conference focused on taking stock of financial market reform, such as the Sarbanes-Oxley Act of 2002 and the internationalization of exchanges. Fed Chairman Ben Bernanke gave the keynote address on liquidity provisions by the Federal Reserve.

- The bank's Americas Center hosted three conferences in 2008: "Remittances and the Macroeconomy," "New Horizons: Wealth Management and the Changing Global Landscape," and the Second Georgia International Development workshop.

- The bank introduced "macroblog" on the Atlanta Fed's Web site (frbatlanta.org) to explore monetary policy topics, macroeconomic developments, financial issues, and southeastern trends.

Supervision and Regulation resources focus on real estate and credit issues

- The Supervision and Regulation Department's Real Estate Analytic Strategy was formally adopted as a bankwide initiative to centrally coordinate real estate analysis, conduct research and projects, and host forums and events that address issues pertinent in the Sixth Federal Reserve District and serve as a resource to the Federal Reserve System.

- More than 100 representatives of financial institutions, government, and nonprofit agencies gathered at Atlanta Fed headquarters for the "Re-engineering the Real Estate Market" conference to examine what the industry might look like after the foreclosure crisis.

- The bank's Community Affairs Department began a series of online discussion papers focused on issues related to residential foreclosures and the Federal Neighborhood Stabilization Program. The department also introduced an online Foreclosure Resource Center for consumers.

- The bank hosted its third annual housing summit, attended by builders, bankers, suppliers, and brokers, to gain insight into regional housing activity.

- The Credit and Risk Management Department dealt with sharply higher demand from Sixth Federal Reserve District financial institutions for overnight and term Federal Reserve liquidity through the Fed's discount window. The number of loans made by the Atlanta Fed discount window increased 1,484 percent in 2008 compared to 2007.

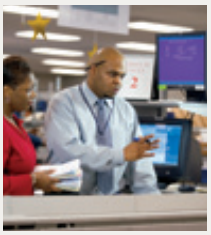
Despite checks' decline, payments remain a Fed priority

- In the payments arena, the bank launched the Retail Payments Risk Forum, which works with industry leaders, financial institutions, regulators, and law enforcement officials to understand, identify, and promote the mitigation of risks.

- The Atlanta Fed hosted the Retail Payments Legal Forum, which focused on the current state of check processing; transactional structures, risks, and liability; and new technical and operational realities and legal risks.

- Atlanta was selected to eventually become the Federal Reserve System's only electronic check processing site. After 2009 the Atlanta Fed will no longer process traditional paper checks as all Federal Reserve paper check processing is moved to the Cleveland Fed.

- According to the Fed's Retail Payment Office (RPO) based in Atlanta, the volume of paper checks processed by the Federal Reserve declined through the year. The check service customer volume of paper deposits dropped from 40.7 percent of total volume in January to 8.9 percent by December. As part of the Fed's efforts to reduce its paper check infrastructure, the RPO successfully transitioned the Memphis and Jacksonville check operations into Atlanta.



Bank programs educate and serve the public

- The Atlanta office held a two-day personal financial education event for 265 students from our partner school, Inman Middle School. The seventh and eighth graders attended a series of courses on banking and personal financial issues. Fed President Dennis Lockhart visited with the students and made a special presentation to them on the final day.

- The Atlanta Fed's economic and financial education programs successfully reached over 12,600 educators through teacher workshops, presentations, and education association conferences. Another 18,500 people—primarily middle and high school students—participated in guided tours or took advantage of self-guided tours in the monetary museums and visitors centers in Atlanta and at the branch offices.

- President Dennis Lockhart and other Atlanta Fed officials increased the frequency of their public speaking engagements to help explain the Fed's role in trying to stabilize the economy and financial system.

- To promote public awareness and debate, the bank's quarterly Public Affairs Forums invite distinguished scholars to address business, civic, and community leaders about important national issues. In 2008, the forums featured Joseph Newhouse of Harvard University, who discussed health care policy; Gordon Hanson of the University of California, San Diego (UCSD), who spoke on immigration; James Hamilton, also from UCSD, who examined the economics of oil prices; and Lawrence Kotlikoff of Boston University, who focused on entitlement spending.

- In 2008 Atlanta Fed employees continued to log many hours in service to the community. Employees participated in thirty-five projects, including Hands On Atlanta day, supporting U.S. troops with USO duty at the Atlanta airport, and facilitating a boys book club for a local middle school. One in three employees participated in a community service project in 2008, volunteering a total of 3,500 hours. The five Atlanta Fed branches also participate in a wide range of volunteer activities, such as the New Orleans Foundation for Hospital Art and the Jacksonville Urban League.

SIXTH FEDERAL RESERVE DISTRICT DIRECTORS

Federal Reserve Banks each have a board of nine directors. Directors provide economic information, have broad oversight responsibility for their bank's operations, and, with Board of Governors approval, appoint the bank's president and first vice president.

Six directors—three class A, representing the banking industry, and three class B—are elected by banks that are members of the Federal Reserve System. Three class C directors (including the chairman and deputy chairman) are appointed by the Board of Governors. Class B and C directors represent agriculture, commerce, industry, labor, and consumers in the district; they cannot be officers, directors, or employees of a bank; class C directors cannot be bank stockholders.

Fed branch office boards have five or seven directors; the majority are appointed by head-office directors and the rest by the Board of Governors.

Atlanta Board of Directors

V. Larkin Martin
Chairman
Managing Partner
Martin Farm
Courtland, Alabama

D. Scott Davis
Deputy Chairman
Chairman and
Chief Executive Officer
United Parcel Service
Atlanta, Georgia

Teri G. Fontenot
President and
Chief Executive Officer
Woman's Hospital
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L. Phillip Humann
(resigned)
Consultant
SunTrust Banks Inc.
Atlanta, Georgia

James H. McKillop III
President and
Chief Executive Officer
Independent Bankers' Bank of Florida
Lake Mary, Florida

Egbert L.J. Perry
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The Integral Group LLC
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Rudy E. Schupp
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Rayonier
Jacksonville, Florida

Carol B. Tomé
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Executive Vice President
The Home Depot
Atlanta, Georgia

James M. Wells III
Chairman and
Chief Executive Officer
SunTrust Banks Inc.
Atlanta, Georgia

Federal Advisory Council Member

Richard G. Hickson
Chairman and
Chief Executive Officer
Trustmark Corporation
Jackson, Mississippi

Left to right: Schupp, Tomé, Perry, Wells, Davis, McKillop, Martin, Thomas, Fontenot; not pictured: Humann, Hickson

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Chairman
Chairman of the Board
HOME Place Farms Inc.
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Bobby A. Bradley
Managing Partner
Lewis Properties LLC and
Anderson Investments LLC
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Samuel F. Dodson
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Vice Chairman
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Birmingham, Alabama

C. Richard Moore Jr.
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Chief Executive Officer
Peoples Southern Bank
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F. Michael Reilly
Chairman, President, and
Chief Executive Officer
Randall-Reilly Publishing Company
Tuscaloosa, Alabama

Left to right: Reilly, Head, Holcomb, Sanford, Bradley, Dodson, Moore

Jacksonville Branch Directors

Fassil Gabremariam
Chairman
President and Founder
U.S.-Africa Free Enterprise
Education Foundation
Tampa, Florida

Jack B. Healan Jr.
President
Amelia Island Plantation Company
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H. Britt Landrum Jr.
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Companies Inc.
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First Commercial Bank of Florida
Orlando, Florida

Wendell A. Sebastian
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Chief Executive Officer
GTE Federal Credit Union
Tampa, Florida

Linda H. Sherrer
President and
Chief Executive Officer
Prudential Network Realty
Jacksonville, Florida

Ellen S. Titen
President
E.T. Consultants
Winter Park, Florida

Left to right: Rowe, Titen, Gabremariam, Healan, Landrum, Sherrer; not pictured: Sebastian

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Chairman
President
Angus Investments Inc.
Port St. Lucie, Florida

Leonard L. Abess
Chairman, President, and
Chief Executive Officer
City National Bank of Florida
Miami, Florida

Walter Banks
President
Lago Mar Resort and Club
Fort Lauderdale, Florida

Dennis S. Hudson III
Chairman and
Chief Executive Officer
Seacoast Banking Corporation
of Florida
Stuart, Florida

Marvin O'Quinn
President and
Chief Executive Officer
Jackson Health System
Miami, Florida

Thomas H. Shea
Chief Executive Officer
Florida/Caribbean Region
Right Management
Fort Lauderdale, Florida

Gay Rebel Thompson
President and
Chief Executive Officer
Cement Industries Inc.
Fort Myers, Florida

Left to right: Shea, Abess, Thompson, Banks, Jones; not pictured: Hudson, O'Quinn

Nashville Branch Directors

Rich Ford
Chairman
President
Hylant Group of Nashville
Nashville, Tennessee

Daniel A. Gaudette
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North American Manufacturing
and Supply Chain Management
Nissan North America Inc.
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Vanderbilt University
Nashville, Tennessee

Paul G. Willson
Chairman and
Chief Executive Officer
Citizens National Bank
Athens, Tennessee

Left to right: Swain, London, Gaudette, Harrington, Willson; not pictured: Ford, Williams

New Orleans Branch Directors

Christel C. Slaughter
Chairman
Partner
SSA Consultants LLC
Baton Rouge, Louisiana

Robert S. Boh
President and
Chief Executive Officer
Boh Bros. Construction Company LLC
New Orleans, Louisiana

Gerard R. Host
President and
Chief Executive Officer
Trustmark National Bank
Jackson, Mississippi

R. King Milling
Vice Chairman
Whitney Holding Corporation and
Whitney National Bank
New Orleans, Louisiana

Earl L. Shipp
Group President—Basic Chemicals
The Dow Chemical Company
Dubai, United Arab Emirates

Matthew G. Stuller Sr.
Chairman and
Chief Executive Officer
Stuller Inc.
Lafayette, Louisiana

Anthony J. Topazi
President and
Chief Executive Officer
Mississippi Power
Gulfport, Mississippi

Left to right: Shipp, Milling, Host, Stuller, Slaughter, Topazi; not pictured: Boh

SMALL BUSINESS, AGRICULTURE, AND LABOR ADVISORY COUNCIL

Kevin Berken
Owner
KMB Farms
Lake Arthur, Louisiana

Bill Boone
Director
Agriculture Innovation Center
Tifton, Georgia

Steve Cole
President
Robert Bowden Inc.
Marietta, Georgia

Joyce I. Cook
Chief Executive Officer
International CyberTrans
Brentwood, Tennessee

Sandra Rhodes Duncan
Owner
Duplain W. Rhodes Funeral
Home—Family of Businesses
Gretna, Louisiana

Jimmy Haynes
(DECEASED)
President
J.H. Haynes Electric Company Inc.
Gulfport, Mississippi

Jeff Hubbard
President
Georgia Association of Educators
Tucker, Georgia

Thomas Huggins III
President
Ariel Business Group Inc.
Tampa, Florida

Jacques Klempf
Chairman/President
Foodonics International Inc.
Jacksonville, Florida

Barry McGriff
President
McGriff Industries Inc.
Cullman, Alabama

Roger Reisert
President
C2Biofuels LLC
Marietta, Georgia

Radhika Subramanian
Chief Executive Officer and Chairman
Emcien Inc.
Atlanta, Georgia

Ronald L. Tanner
Manager, Business Development
Ohio Valley and Southern States
Laborers-Employers Cooperation
and Education Trust
Chattanooga, Tennessee

Guy Tipton
President
Alabama District Council Ohio Valley
and Southern States Region
Hoover, Alabama

Gary Wishnatzki
President and Chief Executive Officer
Wishnatzki Inc. d/b/a
Wishnatzki Farms
Plant City, Florida

Left to right: Wishnatzki, Huggins, Hubbard, Cook, McGriff, Subramanian, Berken, Klempf, Tipton, Reisert, Cole, Boone, Haynes; not pictured: Duncan, Tanner

SIXTH FEDERAL RESERVE DISTRICT OFFICERS
Management Committee

Dennis P. Lockhart
President and
Chief Executive Officer

Patrick K. Barron
First Vice President and
Chief Operating Officer

David E. Altig
Senior Vice President and
Director of Research
Research Division

Christopher G. Brown
Senior Vice President and
Chief Financial Officer
Corporate Services Division

Anne M. DeBeer
Senior Vice President
Corporate Services/
Financial Services Division

William B. Estes III
Senior Vice President
Supervision and
Regulation Division

Marie C. Gooding
Senior Vice President
and Corporate Engagement Officer

Frederick R. Herr
Senior Vice President
System Retail Payments Office

Richard R. Oliver
Executive Vice President
System Retail Payments Office

Lois C. Berthaume
Adviser
Senior Vice President and
General Auditor
Auditing Department

Richard A. Jones
Adviser
Senior Vice President and
General Counsel
Legal Department

Seated, left to right: Jones, Barron, Oliver, Lockhart, Altig, Gooding; standing, left to right: Brown, Berthaume, Herr, DeBeer, Estes

Other Officers

Scott H. Dake
Senior Vice President

James M. McKee
Senior Vice President

Robert J. Musso
Senior Vice President and
Regional Executive
New Orleans

Donald E. Nelson
Senior Vice President

Melvyn K. Purcell
(RETIRED)
Senior Vice President and
Branch Manager
Nashville

William J. Tignanelli
Senior Vice President

Andre T. Anderson
Vice President

John S. Branigin
Vice President

Michael Bryan
Vice President

Suzanna J. Costello
Vice President

Thomas J. Cunningham
Vice President and
Associate Director of Research

Leah Davenport
Vice President

Juan del Busto
Vice President and
Regional Executive
Miami

Gerald P. Dwyer Jr.
Vice President

Brian D. Egan
Vice President

J. Stephen Foley
Vice President

Amy S. Goodman
Vice President
New Orleans

Cynthia C. Goodwin
Vice President

Lee C. Jones
Vice President and
Regional Executive
Nashville

Mary M. Kepler
Vice President

Robert A. Love
Vice President

Mary M. Mandel
Vice President

Bobbie H. McCrackin
Vice President and
Public Affairs Officer

Christopher L. Oakley
Vice President and
Regional Executive
Jacksonville

Cynthia L. Rasche
Vice President

John C. Robertson
Vice President

Melinda J. Rushing
Vice President

Juan C. Sanchez
Vice President

Robert M. Schenck
Vice President

Ellis W. Tallman
(RESIGNED)
Vice President

David E. Tatum
Vice President

Adrienne M. Wells
Vice President

Julius G. Weyman
Vice President and
Regional Executive
Birmingham

Christopher N. Alexander
Assistant Vice President

John H. Atkinson
(RETIRED)
Assistant Vice President

Robert Lee Bagosy
(RESIGNED)
Assistant Vice President

W. Brian Bowling
Assistant Vice President

Joan H. Buchanan
Assistant Vice President and
Corporate Secretary

Annella D. Campbell-Drake
Assistant Vice President

David J. Christerson
Assistant Vice President

Michael Chriszt
Assistant Vice President

Chapelle D. Davis
Assistant Vice President

W. Jeffrey Devine
(TRANSFERRED OUT OF DISTRICT)
Assistant Vice President

Robert A. de Zayas
Assistant Vice President
Miami

Angela H. Dirr
Assistant Vice President and
Assistant General Counsel

Gregory S. Fuller
Assistant Vice President

Paul Graham
(RETIRED)
Assistant Vice President
Jacksonville

Todd Greene
Assistant Vice President

Robert D. Hawkins
Assistant Vice President

Carolyn Ann Healy
Assistant Vice President

Janet A. Herring
Assistant Vice President

Kathryn Hinton
Assistant Vice President

Susan Hoy
Assistant Vice President and
Assistant General Counsel

Bradley M. Joiner
Assistant Vice President

Evette H. Jones
Assistant Vice President

Jacquelyn H. Lee
Assistant Vice President

Stephen A. Levy
Assistant Vice President

Margaret Darlene Martin
Assistant Vice President

Marie E. McNally
Assistant Vice President

Elizabeth McQuerry
Assistant Vice President

Annita T. Moore
Assistant Vice President
Nashville

D. Pierce Nelson
Assistant Vice President and
Public Information Officer

Doris Quiros
Assistant Vice President and
Assistant General Auditor

Susan L. Robertson
Assistant Vice President

David W. Smith
Assistant Vice President

Maria Smith
Assistant Vice President

Timothy R. Smith
Assistant Vice President and
Community Relations Officer

Clifford S. Stanford
Assistant Vice President

Allen D. Stanley
Assistant Vice President

Joel E. Warren
Assistant Vice President
Jacksonville

Charles L. Weems
Assistant Vice President

Kenneth Wilcox
Assistant Vice President

Christina M. Wilson
Assistant Vice President
Jacksonville

Stephen W. Wise
Assistant Vice President

FINANCIAL REPORTS

In 2008, the Board of Governors engaged Deloitte & Touche LLP (D&T) for the audits of the individual and combined financial statements of the Reserve Banks. Fees for D&T's services are estimated to be $10.2 million. Approximately $2.7 million of the estimated total fees were for the audits of the limited liability companies (LLCs) that are associated with recent Federal Reserve actions to address the financial crisis and are consolidated in the financial statements of the Federal Reserve Bank of New York.[1] To ensure auditor independence, the Board of Governors requires that D&T be independent in all matters relating to the audit. Specifically, D&T may not perform services for the Reserve Banks or others that would place it in a position of auditing its own work, making management decisions on behalf of Reserve Banks, or in any other way impairing its audit independence. In 2008, the Bank did not engage D&T for any nonaudit services.

1. Each LLC will reimburse the Board of Governors for the fees related to the audit of its financial statements from the entity's available net assets.

MANAGEMENT'S ASSERTION

To the Board of Directors of the Federal Reserve Bank of Atlanta:

The management of the Federal Reserve Bank of Atlanta ("FRB Atlanta") is responsible for the preparation and fair presentation of the Statement of Financial Condition, Statements of Income and Comprehensive Income, and Statement of Changes in Capital as of December 31, 2008 (the "Financial Statements"). The Financial Statements have been prepared in conformity with the accounting principles, policies, and practices established by the Board of Governors of the Federal Reserve System and as set forth in the *Financial Accounting Manual for Federal Reserve Banks* ("Manual") and, as such, include amounts, some of which are based on management judgments and estimates. To our knowledge, the Financial Statements are, in all material respects, fairly presented in conformity with the accounting principles, policies, and practices documented in the Manual and include all disclosures necessary for such fair presentation.

The management of the FRB Atlanta is responsible for establishing and maintaining effective internal control over financial reporting as it relates to the Financial Statements. Such internal control is designed to provide reasonable assurance to management and to the Board of Directors regarding the preparation of the Financial Statements in accordance with the Manual. Internal control contains self-monitoring mechanisms, including, but not limited to, divisions of responsibility and a code of conduct. Once identified, any material deficiencies in internal control are reported to management and appropriate corrective measures are implemented.

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

The management of the FRB Atlanta assessed its internal control over financial reporting reflected in the Financial Statements, based upon the criteria established in the *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, we believe that the FRB Atlanta maintained effective internal control over financial reporting as it relates to the Financial Statements.

Federal Reserve Bank of Atlanta

Dennis P. Lockhart
President and Chief Executive Officer

Patrick K. Barron
First Vice President and Chief Operating Officer

Christopher G. Brown
Senior Vice President and Chief Financial Officer

April 2, 2009

REPORT OF INDEPENDENT AUDITORS

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

We have audited the accompanying statements of condition of the Federal Reserve Bank of Atlanta ("FRB Atlanta") as of December 31, 2008 and 2007 and the related statements of income and comprehensive income and changes in capital for the years then ended, which have been prepared in conformity with accounting principles established by the Board of Governors of the Federal Reserve System. We also have audited the internal control over financial reporting of FRB Atlanta as of December 31, 2008, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. FRB Atlanta's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Assertion. Our responsibility is to express an opinion on these financial statements and an opinion on FRB Atlanta's internal control over financial reporting based on our audits.

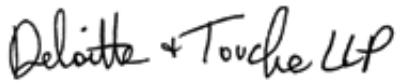
We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective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

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

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

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of FRB Atlanta as of December 31, 2008 and 2007, and the results of its operations for the years then ended, on the basis of accounting described in Note 4. Also, in our opinion, FRB Atlanta maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on the criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.



Deloitte & Touche LLP

April 2, 2009
Atlanta, Georgia

STATEMENTS OF CONDITION

(in millions)	As of December 31, 2008	As of December 31, 2007
Assets		
Gold certificates	$ 1,221	$ 1,117
Special drawing rights certificates	166	166
Coin	213	153
Items in process of collection	325	229
Loans to depository institutions	17,705	25
System Open Market Account:		
Securities purchased under agreements to resell	7,960	4,313
U.S. government, Federal agency, and government-sponsored enterprise securities, net	49,967	69,155
Investments denominated in foreign currencies	1,910	1,909
Central bank liquidity swaps	42,641	2,028
Interdistrict settlement account	20,108	3,909
Bank premises and equipment, net	256	269
Accrued interest receivable	668	592
Other assets	73	76
Total assets	**$ 143,213**	**$ 83,941**
Liabilities and Capital		
Federal Reserve notes outstanding, net	$ 105,276	$ 75,609
System Open Market Account:		
Securities sold under agreements to repurchase	8,791	4,080
Deposits:		
Depository institutions	25,593	975
Other deposits	3	3
Deferred credit items	158	143
Interest on Federal Reserve notes due to U.S. Treasury	8	140
Accrued benefit costs	130	123
Other liabilities	30	18
Total liabilities	**139,989**	**81,091**
Capital paid-in	1,612	1,425
Surplus (including accumulated other comprehensive loss of $18 and $21 at December 31, 2008 and 2007, respectively)	1,612	1,425
Total capital	**3,224**	**2,850**
Total liabilities and capital	**$ 143,213**	**$ 83,941**

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

STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(in millions)	For the year ended December 31, 2008	For the year ended December 31, 2007
Interest income		
Loans to depository institutions	$ 142	$ —
System Open Market Account:		
Securities purchased under agreements to resell	185	130
U.S. government, Federal agency, and government-sponsored enterprise securities	2,487	3,489
Investments denominated in foreign currencies	48	45
Central bank liquidity swaps	278	2
Total interest income	**3,140**	**3,666**
Interest expense		
System Open Market Account:		
Securities sold under agreements to repurchase	71	152
Depository institutions deposits	20	—
Total interest expense	**91**	**152**
Net interest income	**3,049**	**3,514**
Non-interest income		
System Open Market Account:		
U.S. government, Federal agency, and government-sponsored enterprise securities gains, net	358	—
Foreign currency gains, net	101	162
Income from services	649	754
Reimbursable services to government agencies	14	12
Other income	82	10
Total non-interest income	**1,204**	**938**
Operating expenses		
Salaries and other benefits	193	182
Occupancy expense	22	21
Equipment expense	22	20
Compensation paid for services costs incurred	471	597
Assessments by the Board of Governors	98	104
Other expenses	131	115
Total operating expenses	**937**	**1,039**
Net income prior to distribution	**3,316**	**3,413**
Change in funded status of benefit plans	**3**	**6**
Comprehensive income prior to distribution	**$ 3,319**	**$ 3,419**
Distribution of comprehensive income		
Dividends paid to member banks	$ 94	$ 78
Transferred to surplus and change in accumulated other comprehensive loss	187	149
Payments to U.S. Treasury as interest on Federal Reserve notes	3,038	3,192
Total distribution	**$ 3,319**	**$ 3,419**

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

STATEMENTS OF CHANGES IN CAPITAL

(in millions, except share data) — For the years ended December 31, 2008, and December 31, 2007

		Surplus			
	Capital Paid-In	Net Income Retained	Accumulated Other Comprehensive Loss	Total Surplus	Total Capital
Balance at January 1, 2007 (25.5 million shares)	$ 1,276	$ 1,303	$ (27)	$ 1,276	$ 2,552
Net change in capital stock issued (3 million shares)	149	—	—	—	149
Transferred to surplus and change in accumulated other comprehensive loss	—	143	6	149	149
Balance at December 31, 2007 (28.5 million shares)	$ 1,425	$ 1,446	$ (21)	$ 1,425	$ 2,850
Net change in capital stock issued (3.7 million shares)	187	—	—	—	187
Transferred to surplus and change in accumulated other comprehensive loss	—	184	3	187	187
Balance at December 31, 2008 (32.2 million shares)	$ 1,612	$ 1,630	$ (18)	$ 1,612	$ 3,224

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

NOTES TO FINANCIAL STATEMENTS

1. STRUCTURE

The Federal Reserve Bank of Atlanta ("Bank") is part of the Federal Reserve System ("System") and is one of the twelve Reserve Banks ("Reserve Banks") created by Congress under the Federal Reserve Act of 1913 ("Federal Reserve Act"), which established the central bank of the United States. The Reserve Banks are chartered by the federal government and possess a unique set of governmental, corporate, and central bank characteristics. The Bank serves the Sixth Federal Reserve District, which includes Georgia, Florida, Alabama, and portions of Louisiana, Tennessee, and Mississippi.

In accordance with the Federal Reserve Act, supervision and control of the Bank are 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 in the System. 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.

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. Functions include participation in formulating and conducting monetary policy; participation in the payments system, including large-dollar transfers of funds, automated clearinghouse ("ACH") operations, and check collection; distribution of coin and currency; performance of fiscal agency functions for the U.S. Treasury, certain federal agencies, and other entities; serving as the federal government's bank; provision of short-term loans to depository institutions; provision of loans to individuals, partnerships, and corporations in unusual and exigent circumstances; service to the consumer and the community by providing educational materials and information regarding consumer laws; and supervision of bank holding companies, state member banks, and U.S. offices of foreign banking organizations. Certain services are provided to foreign and international monetary authorities, primarily by the FRBNY.

The FOMC, in the conduct of monetary policy, establishes policy regarding domestic open market operations, oversees these operations, and annually issues authorizations and directives to the FRBNY to execute transactions. The FRBNY is authorized and directed by the FOMC to conduct operations in domestic markets, including the direct purchase and sale of securities of the U.S. government, Federal agencies, and government-sponsored enterprises ("GSEs"), the purchase of these securities under agreements to resell, the sale of these securities under agreements to repurchase, and the lending of these securities. The FRBNY executes these transactions at the direction of the FOMC and holds the resulting securities and agreements in the portfolio known as the System Open Market Account ("SOMA").

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

Although the Reserve Banks are separate legal entities, they collaborate in the delivery of certain services to achieve greater efficiency and effectiveness. This collaboration takes the form of centralized operations and product or function offices that have responsibility for the delivery of certain services on behalf of the Reserve Banks. Various operational and management models are used and are supported by service agreements between the Reserve Banks providing the service and the other 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 reimburse the other Reserve Banks for services provided to them.

Major services provided by the Bank on behalf of the System and for which the costs were not reimbursed by the other Reserve Banks include the Retail Payments Office, retail check related projects, and accounting related projects.

3. RECENT FINANCIAL STABILITY ACTIVITIES

The Federal Reserve has implemented a number of programs designed to support the liquidity of financial institutions and to foster improved conditions in financial markets. These new programs, which are set forth below, have resulted in significant changes to the Bank's financial statements.

Expanded Open Market Operations and Support for Mortgage Related Securities

The Single-Tranche Open Market Operation Program, created on March 7, 2008, allows primary dealers to initiate a series of term repurchase transactions that are expected to accumulate up to $100 billion in total. Under the provisions of the program, these transactions are conducted as 28-day term

repurchase agreements for which primary dealers pledge U.S. Treasury and agency securities and agency Mortgage-Backed Securities ("MBS") as collateral. The FRBNY can elect to increase the size of the term repurchase program if conditions warrant. The repurchase transactions are reported as "System Open Market Account: Securities purchased under agreements to resell" in the Statements of Condition.

The GSE and Agency Securities and MBS Purchase Program was announced on November 25, 2008. The primary goal of the program is to provide support to the mortgage and housing markets and to foster improved conditions in financial markets. Under this program, the FRBNY will purchase the direct obligations of housing-related GSEs and MBS backed by the Federal National Mortgage Association ("Fannie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac"), and the Government National Mortgage Association ("Ginnie Mae"). Purchases of the direct obligations of housing-related GSEs began in November 2008 and purchases of GSE and agency MBS began in January 2009. There were no purchases of GSE and agency MBS during the period ended December 31, 2008. The program was initially authorized to purchase up to $100 billion in GSE direct obligations and up to $500 billion in GSE and agency MBS. In March 2009, the FOMC authorized FRBNY to purchase up to an additional $750 billion of GSE and agency MBS and up to an additional $100 billion of GSE direct obligations.

The FRBNY holds the resulting securities and agreements in the SOMA portfolio and the activities of both programs are allocated to the other Reserve Banks.

Central Bank Liquidity Swaps

The FOMC authorized the FRBNY to establish temporary reciprocal currency swap arrangements (central bank liquidity swaps) with the European Central Bank and the Swiss National Bank on December 12, 2007 to help provide liquidity in U.S. dollars to overseas markets. Subsequently, the FOMC authorized reciprocal currency swap arrangements with additional foreign central banks. Such arrangements are now authorized with the following central banks: the Reserve Bank of Australia, the Banco Central do Brasil, the Bank of Canada, Danmarks Nationalbank, the Bank of England, the European Central Bank, the Bank of Japan, the Bank of Korea, the Banco de Mexico, the Reserve Bank of New Zealand, Norges Bank, the Monetary Authority of Singapore, Sveriges Riksbank, and the Swiss National Bank. The activity related to the program is allocated to the other Reserve Banks. The maximum amount of borrowing permissible under the swap arrangements varies by central bank. The central bank liquidity swap arrangements are authorized through October 30, 2009.

Lending to Depository Institutions

The temporary Term Auction Facility ("TAF") program was created on December 12, 2007. The goal of the TAF is to help promote the efficient dissemination of liquidity, which is achieved by the Reserve Banks injecting term funds through a broader range of counterparties and against a broader range of collateral than open market operations. Under the TAF program, Reserve Banks auction term funds to depository institutions against a wide variety of collateral. All depository institutions that are judged to be in generally sound financial condition by their Reserve Bank and that are eligible to borrow under the primary credit program are eligible to participate in TAF auctions. All advances must be fully collateralized. The loans are reported as "Loans to depository institutions" in the Statements of Condition.

Lending to Primary Dealers

The Term Securities Lending Facility ("TSLF") was created on March 11, 2008, to promote the liquidity in the financing markets for U.S. Treasuries and other collateral. Under the TSLF, the FRBNY will lend up to an aggregate amount of $200 billion of U.S. Treasury securities to primary dealers secured for a term of 28 days. Securities loans are collateralized by a pledge of other securities, including federal agency debt, federal agency residential mortgage-backed securities, and non-agency AAA/Aaa-rated private-label residential mortgage-backed securities, and are awarded to primary dealers through a competitive single-price auction. The TSLF is authorized through October 30, 2009. The fees related to these securities lending transactions are reported as a component of "Non-interest income: Other income" in the Statements of Income and Comprehensive Income.

The Term Securities Lending Facility Options Program ("TOP"), created on July 30, 2008, offers primary dealers the option to draw upon short-term, fixed-rate TSLF loans in exchange for eligible collateral. The options are awarded through a competitive auction. The program is intended to enhance the effectiveness of the TSLF by ensuring additional securities liquidity during periods of heightened collateral market pressures, such as around quarter-end dates. TOP auction dates are determined by the FRBNY, and the program authorization ends concurrently with the TSLF.

Other Lending Facilities

The Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility ("AMLF"), created on September 19, 2008, is a lending facility that provides funding to U.S. depository institutions and bank holding companies to finance the purchase of high-quality asset-backed commercial paper ("ABCP") from money market mutual funds under certain conditions. The program is intended to assist money market mutual funds that hold such paper to meet the demands for investor redemptions and to foster liquidity in the ABCP market and money markets more generally. The Federal Reserve Bank of Boston ("FRBB") administers the AMLF and is authorized to extend these loans to eligible borrowers on behalf of the other Reserve Banks. All loans extended under the AMLF are recorded as assets by the FRBB and, if the borrowing institution settles to a depository account in the Sixth Reserve District, the funds are credited to the institution's depository account and settled between the Banks through the interdistrict settlement account. The credit risk related to the AMLF is assumed by the FRBB. The FRBB is authorized to finance the purchase of commercial paper through October 30, 2009.

4. SIGNIFICANT ACCOUNTING POLICIES

Accounting principles for entities with the unique powers and responsibilities of a nation's central bank have not been formulated by accounting standard-setting bodies. The Board of Governors has developed specialized accounting principles and practices that it considers to be appropriate for the nature and

function of a central bank. These accounting principles and practices are documented in the *Financial Accounting Manual for Federal Reserve Banks* ("Financial Accounting Manual" or "FAM"), which is issued by the Board of Governors. All of the Reserve Banks are required to adopt and apply accounting policies and practices that are consistent with the FAM, and the financial statements have been prepared in accordance with the FAM.

Differences exist between the accounting principles and practices in the FAM and generally accepted accounting principles in the United States ("GAAP"), primarily due to the unique nature of the Bank's powers and responsibilities as part of the nation's central bank. The primary difference is the presentation of all SOMA securities holdings at amortized cost rather than using the fair value presentation required by GAAP. U.S. government, Federal agency, and GSE securities, and investments denominated in foreign currencies comprising the SOMA are recorded at cost, on a settlement-date basis, and are adjusted for amortization of premiums or accretion of discounts on a straight-line basis. Amortized cost more appropriately reflects the Bank's securities holdings given the System's unique responsibility to conduct monetary policy. Although the application of current market prices to the securities holdings may result in values substantially above or below their carrying values, these unrealized changes in value would have no direct effect on the quantity of reserves available to the banking system or on the prospects for future Bank earnings or capital. Both the domestic and foreign components of the SOMA portfolio may involve transactions that result in gains or losses when holdings are sold prior to maturity. Decisions regarding securities and foreign currency transactions, including their purchase and sale, are motivated by monetary policy objectives rather than profit. Accordingly, fair values, earnings, and any gains or losses resulting from the sale of such securities and currencies are incidental to the open market operations and do not motivate decisions related to policy or open market activities.

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

Preparing the financial statements in conformity with the FAM requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Certain amounts relating to the prior year have been reclassified to conform to the current-year presentation. Unique accounts and significant accounting policies are explained below.

a. Gold and Special Drawing Rights Certificates

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

Payment for the gold certificates by the Reserve Banks is made by crediting equivalent amounts in dollars into the account established for the U.S. Treasury. The gold certificates held by the Reserve Banks are required to be backed by the gold of the U.S. Treasury. The U.S. Treasury may reacquire the gold certificates at any time and the Reserve Banks must deliver them to the U.S. Treasury. At such time, the U.S. 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 a fine troy ounce. The Board of Governors allocates the gold certificates among the Reserve Banks once a year based on the average Federal Reserve notes outstanding in each Reserve Bank.

SDR certificates are issued by the International Monetary Fund (the "Fund") to its members in proportion to each member's quota in the Fund at the time of issuance. SDR certificates serve as a supplement to international monetary reserves and may be transferred from one national monetary authority to another. Under the law providing for U.S. participation in the SDR system, the Secretary of the U.S. Treasury is authorized to issue SDR certificates somewhat like gold certificates to the Reserve Banks. When SDR certificates are issued to the Reserve Banks, equivalent amounts in dollars are credited to the account established for the U.S. Treasury, and the Reserve Banks' SDR certificate accounts are increased. The Reserve Banks are required to purchase SDR certificates, at the direction of the U.S. Treasury, for the purpose of financing SDR acquisitions or for financing exchange stabilization operations. At the time SDR transactions occur, the Board of Governors allocates SDR certificate transactions among the Reserve Banks based upon each Reserve Bank's Federal Reserve notes outstanding at the end of the preceding year. There were no SDR transactions in 2008 or 2007.

b. Loans to Depository Institutions

Loans are reported at their outstanding principal balances net of commitment fees. Interest income is recognized on an accrual basis. Loan commitment fees are generally deferred and amortized on a straight-line basis over the commitment period, which is not materially different from the interest method.

Outstanding loans are evaluated to determine whether an allowance for loan losses is required. The Bank has developed procedures for assessing the adequacy of the allowance for loan losses that reflect the assessment of credit risk considering all available information. This assessment includes monitoring information obtained from banking supervisors, borrowers, and other sources to assess the credit condition of the borrowers.

Loans are considered to be impaired when it is probable that the Bank will not receive principal and interest due in accordance with the contractual terms of the loan agreement. The amount of the impairment is the difference between the recorded amount of the loan and the amount expected to be collected, after consideration of the fair value of the collateral. Recognition of interest income is discontinued for any loans that are considered to be impaired. Cash payments made by borrowers on impaired loans are applied to principal until the balance is reduced to zero; subsequent payments are recorded as recoveries of amounts previously charged off and then to interest income.

c. Securities Purchased under Agreements to Resell, Securities Sold under Agreements to Repurchase, and Securities Lending

The FRBNY may engage in tri-party purchases of securities under agreements to resell ("tri-party agreements"). Tri-party agreements are conducted with two commercial custodial banks that manage the clearing and settlement of collateral. Collateral is held in excess of the contract amount. Acceptable collateral under tri-party agreements primarily includes U.S. government securities; pass-through mortgage securities of Fannie Mae, Freddie Mac, and Ginnie Mae; STRIP securities of the U.S. government; and "stripped" securities of other government agencies. The tri-party agreements are accounted for as financing transactions and the associated interest income is accrued over the life of the agreement.

Securities sold under agreements to repurchase are accounted for as financing transactions, and the associated interest expense is recognized over the life of the transaction. These transactions are reported at their contractual amounts in the Statements of Condition and the related accrued interest payable is reported as a component of "Other liabilities."

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

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

d. U.S. Government, Federal Agency, and Government-Sponsored Enterprise Securities; Investments Denominated in Foreign Currencies; and Warehousing Agreements

Interest income on U.S. government, Federal agency, and GSE securities and investments denominated in foreign currencies comprising the SOMA is accrued on a straight-line basis. Gains and losses resulting from sales of securities are determined by specific issue based on average cost. Foreign-currency-denominated assets are revalued daily at current foreign currency market exchange rates in order to report these assets in U.S. dollars. Realized and unrealized gains and losses on investments denominated in foreign currencies are reported as "Foreign currency gains, net" in the Statements of Income and Comprehensive Income.

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

Warehousing is an arrangement under which the FOMC agrees to exchange, at the request of the U.S. Treasury, U.S. dollars for foreign currencies held by the U.S. Treasury or ESF over a limited period of time. The purpose of the warehousing facility is to supplement the U.S. dollar resources of the U.S. Treasury and ESF for financing purchases of foreign currencies and related international operations.

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

e. Central Bank Liquidity Swaps

At the initiation of each central bank liquidity swap transaction, the foreign central bank transfers a specified amount of its currency to 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. The foreign currency amounts that the FRBNY acquires are reported as "Central bank liquidity swaps" on the Statements of Condition. Because the swap transaction will be unwound at the same exchange rate that was used in the initial transaction, the recorded value of the foreign currency amounts is not affected by changes in the market exchange rate.

The foreign central bank pays interest to the FRBNY based on the foreign currency amounts held by the FRBNY. The FRBNY recognizes interest income during the term of the swap agreement and reports the interest income as a component of "Interest income: Central bank liquidity swaps" in the Statements of Income and Comprehensive Income.

Activity related to these swap transactions, including the related interest income, is allocated to each Reserve Bank based on the ratio of each Reserve Bank's capital and surplus to aggregate capital and surplus at the preceding December 31. Similar to other investments denominated in foreign currencies, the foreign currency holdings associated with these central bank liquidity swaps are revalued at current foreign currency market exchange rates. Because the swap arrangement will be unwound at the same exchange rate that was used in the initial transaction, the obligation to return the foreign currency is also revalued at current foreign currency market exchange rates and is recorded in a currency exchange valuation account by the FRBNY. This revaluation method eliminates the effects of the changes in the market exchange rate. As of December 31, 2008, the FRBNY began allocating this

currency exchange valuation account to the Bank and, as a result, the reported amount of central bank liquidity swaps reflects the Bank's allocated portion at the contract exchange rate.

f. Interdistrict Settlement Account

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

g. Bank Premises, Equipment, and Software

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

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

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

h. Federal Reserve Notes

Federal Reserve notes are the circulating currency of the United States. These notes are issued through the various Federal Reserve agents (the chairman of the board of directors of each Reserve Bank and their designees) to the Reserve Banks upon deposit with such agents of specified classes of collateral security, typically U.S. government securities. These notes are identified as issued to a specific Reserve Bank. The Federal Reserve Act provides that the collateral security tendered by the Reserve Bank to the Federal Reserve agent must be at least equal to the sum of the notes applied for by such Reserve Bank.

Assets eligible to be pledged as collateral security include all of the Bank's assets. The collateral value is equal to the book value of the collateral tendered with the exception of securities, for which the collateral value is equal to the par value of the securities tendered. The par value of securities pledged for securities sold under agreements to repurchase is deducted.

The Board of Governors may, at any time, call upon a Reserve Bank for additional security to adequately collateralize the outstanding Federal Reserve notes. To satisfy the obligation to provide sufficient collateral for outstanding Federal Reserve notes, the Reserve Banks have entered into an agreement that provides for certain assets of the Reserve Banks to be jointly pledged as collateral for the Federal Reserve notes issued to all Reserve Banks. In the event that this collateral is insufficient, the Federal Reserve Act provides that Federal Reserve notes become a first and paramount lien on all the assets of the Reserve Banks. Finally, Federal Reserve notes are obligations of the United States government. At December 31, 2008 and 2007, all Federal Reserve notes issued to the Reserve Banks were fully collateralized.

"Federal Reserve notes outstanding, net" in the Statements of Condition represents the Bank's Federal Reserve notes outstanding, reduced by the Bank's currency holdings of $24,156 million and $36,017 million at December 31, 2008 and 2007, respectively.

i. Items in Process of Collection and Deferred Credit Items

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

j. Capital Paid-in

The Federal Reserve Act requires that each member bank subscribe to the capital stock of the Reserve Bank in an amount equal to 6 percent of the capital and surplus of the member bank. These shares are nonvoting with a par value of $100 and may not be transferred or hypothecated. As a member bank's capital and surplus changes, its holdings of Reserve Bank stock must be adjusted. Currently, only one-half of the subscription is paid-in and the remainder is subject to call. A member bank is liable for Reserve Bank liabilities up to twice the par value of stock subscribed by it.

By law, each Reserve Bank is required to pay each member bank an annual dividend of 6 percent on the paid-in capital stock. This cumulative dividend is paid semiannually. To reflect the Federal Reserve Act requirement that annual dividends be deducted from net earnings, dividends are presented as a distribution of comprehensive income in the Statements of Income and Comprehensive Income.

k. Surplus

The Board of Governors requires the Reserve Banks to maintain a surplus equal to the amount of capital paid-in as of December 31 of each year. This amount is intended to provide additional capital and reduce the possibility that the Reserve Banks will be required to call on member banks for additional capital.

Accumulated other comprehensive income is reported as a component of surplus in the Statements of Condition and the Statements of Changes in Capital. The balance of accumulated other comprehensive income is comprised of expenses, gains, and losses related to other postretirement benefit plans that, under accounting standards, are included in other comprehensive income, but excluded from net income. Additional information regarding the classifications of accumulated other comprehensive income is provided in Notes 12 and 13.

l. Interest on Federal Reserve Notes

The Board of Governors requires the Reserve Banks to transfer excess earnings to the U.S. Treasury as interest on Federal Reserve notes after providing for the costs of operations, payment of dividends, and reservation of an amount necessary to equate surplus with capital paid-in. This amount is reported as "Payments to U.S. Treasury as interest on Federal Reserve notes" in the Statements of Income and Comprehensive Income and is reported as a liability, or as an asset if overpaid during the year, in the Statements of Condition. Weekly payments to the U.S. Treasury may vary significantly.

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

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

m. Interest on Depository Institution Deposits

Beginning October 9, 2008, the Reserve Banks began paying interest to depository institutions on qualifying balances held at the Banks. Authorization for payment of interest on these balances was granted by Title II of the Financial Services Regulatory Relief Act of 2006, which had an effective date of 2011. Section 128 of the Emergency Economic Stabilization Act of 2008, enacted on October 3, 2008, made that authority immediately effective. The interest rates paid on required reserve balances and excess balances are based on an FOMC-established target range for the effective federal funds rate.

n. Income and Costs Related to U.S. Treasury Services

The Bank is required by the Federal Reserve Act to serve as fiscal agent and depository of the United States. By statute, the Department of the Treasury has appropriations to pay for these services. During the years ended December 31, 2008 and 2007, the Bank was reimbursed for all services provided to the Department of the Treasury as its fiscal agent.

o. Compensation Received for Services Provided and Compensation Paid for Services Costs Incurred

The Bank has overall responsibility for managing the Reserve Banks' provision of check and ACH services to depository institutions and, as a result, recognizes total System revenue for these services on its Statements of Income and Comprehensive Income. The FRBNY manages the Reserve Banks' provision of Fedwire funds and securities transfer services, and recognizes total System revenue for these services on its Statements of Income and Comprehensive Income. Similarly, the Federal Reserve Bank of Chicago ("FRBC") has overall responsibility for managing the Reserve Banks' provision of electronic access services to depository institutions, and, as a result, recognizes total System revenue for these services on its Statements of Income and Comprehensive Income. The Bank, FRBNY, and FRBC compensate the other Reserve Banks for the costs incurred to provide these services. Compensation received by the Bank for providing Fedwire funds and securities transfer and electronic access services is reported as "Other income" in the Statements of Income and Comprehensive Income. Compensation paid by the Bank for check and ACH services is reported as "Compensation paid for services costs incurred" in the Statements of Income and Comprehensive Income.

p. Assessments by the Board of Governors

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

q. Taxes

The Reserve Banks are exempt from federal, state, and local taxes, except for taxes on real property and, in some states, sales taxes on construction-related materials. The Bank's real property taxes were $3 million for each of the years ended December 31, 2008 and 2007, and are reported as a component of "Occupancy expense."

r. Restructuring Charges

The Reserve Banks recognize restructuring charges for exit or disposal costs incurred as part of the closure of business activities in a particular location, the relocation of business activities from one location to another, or a fundamental reorganization that affects the nature of operations. Restructuring charges may include costs associated with employee separations, contract terminations, and asset impairments. Expenses are recognized in

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

Note 14 describes the Bank's restructuring initiatives and provides information about the costs and liabilities associated with employee separations and contract terminations. The costs associated with the impairment of certain of the Bank's assets are discussed in Note 9. 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.

s. Recently Issued Accounting Standards

In September 2006, FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), which established a single authoritative definition of fair value and a framework for measuring fair value, and expands the required disclosures for assets and liabilities measured at fair value. SFAS 157 was effective for fiscal years beginning after November 15, 2007, with early adoption permitted. The Bank adopted SFAS 157 effective January 1, 2008. The provisions of this standard have no material effect on the Bank's financial statements.

In February 2007, FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115" ("SFAS 159"), which provides companies with an irrevocable option to elect fair value as the measurement for selected financial assets, financial liabilities, unrecognized firm commitments, and written loan commitments that are not subject to fair value under other accounting standards. There is a one-time election available to apply this standard to existing financial instruments as of January 1, 2008; otherwise, the fair value option will be available for financial instruments on their initial transaction date. SFAS 159 reduces the accounting complexity for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently, and it eliminates the operational complexities of applying hedge accounting. The Bank adopted SFAS 159 effective January 1, 2008. The provisions of this standard have no material effect on the Bank's financial statements.

In February 2008, FASB issued FASB Staff Position ("FSP") FAS 140-3, "Accounting for Transfers of Financial Assets and Repurchase Financing Transactions." FSP FAS 140-3 requires that an initial transfer of a financial asset and a repurchase financing that was entered into contemporaneously with, or in contemplation of, the initial transfer be evaluated together as a linked transaction under SFAS 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," unless certain criteria are met. FSP FAS 140-3 is effective for the Bank's financial statements for the year beginning on January 1, 2009 and earlier adoption is not permitted. The provisions of this standard will not have a material effect on the Bank's financial statements.

5. LOANS

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

	2008	2007
Primary, secondary, and seasonal credit	$ 483	$ —
TAF	17,222	25
Total loans to depository institutions	$ 17,705	$ 25

Loans to Depository Institutions

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

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

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

Loans to depository institutions are monitored on a daily basis to ensure that borrowers continue to meet eligibility requirements for these programs. The financial condition of borrowers is monitored by the Bank and, if a borrower no longer qualifies for these programs, the Bank will generally request full repayment of the outstanding loan or 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 maturity distribution of loans outstanding at December 31, 2008, was as follows (in millions):

	Primary, secondary, and seasonal credit	TAF
Within 15 days	$ 226	$ —
16 days to 90 days	257	17,222
Total loans	$ 483	$ 17,222

Allowance for Loan Losses

At December 31, 2008 and 2007, no loans were considered to be impaired and the Bank determined that no allowance for loan losses was required.

6. U.S. GOVERNMENT, FEDERAL AGENCY, AND GOVERNMENT-SPONSORED ENTERPRISE SECURITIES; SECURITIES PURCHASED UNDER AGREEMENTS TO RESELL; SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE; AND SECURITIES LENDING

The FRBNY, on behalf of the Reserve Banks, holds securities bought outright in the SOMA. The Bank's allocated share of SOMA balances was approximately 9.950 percent and 9.275 percent at December 31, 2008 and 2007, respectively.

The Bank's allocated share of U.S. government, Federal agency, and GSE securities, net held in the SOMA at December 31 was as follows (in millions):

	2008	2007
U.S. government securities:		
Bills	$ 1,833	$ 21,132
Notes	33,310	37,264
Bonds	12,210	10,294
Federal agency and GSE securities	1,961	—
Total par value	49,314	68,690
Unamortized premiums	801	740
Unaccreted discounts	(148)	(275)
Total allocated to the Bank	$ 49,967	$ 69,155

At December 31, 2008 and 2007, the fair value of the U.S. government, Federal agency, and GSE securities allocated to the Bank, excluding accrued interest, was $56,359 million and $72,078 million, respectively, as determined by reference to quoted prices for identical securities.

The total of the U.S. government, Federal agency, and GSE securities, net, held in the SOMA was $502,189 million and $745,629 million at December 31, 2008 and 2007, respectively. At December 31, 2008 and 2007, the fair value of the U.S. government, Federal agency, and GSE securities held in the SOMA, excluding accrued interest, was $566,427 million and $777,141 million, respectively, as determined by reference to quoted prices for identical securities.

Although the fair value of security holdings can be substantially greater than or less than the recorded value at any point in time, these unrealized gains or losses have no effect on the ability of the Reserve Banks, as central bank, to meet their financial obligations and responsibilities and do not represent a risk to the Reserve Banks, their shareholders, or the public. The fair value is presented solely for informational purposes.

Financial information related to securities purchased under agreements to resell and securities sold under agreements to repurchase for the years ended December 31, 2008 and 2007, was as follows (in millions):

	Securities purchased under agreements to resell		Securities sold under agreements to repurchase	
	2008	2007	2008	2007
Allocated to the Bank:				
Contract amount outstanding, end of year	$ 7,960	$ 4,313	$ 8,791	$ 4,080
Weighted average amount outstanding, during the year	9,655	3,253	6,513	3,232
Maximum month-end balance outstanding, during the year	11,840	4,777	9,806	4,080
Securities pledged, end of year	—	—	7,850	4,085
System total:				
Contract amount outstanding, end of year	$ 80,000	$ 46,500	$ 88,352	$ 43,985
Weighted average amount outstanding, during the year	97,037	35,073	65,461	34,846
Maximum month-end balance outstanding, during the year	119,000	51,500	98,559	43,985
Securities pledged, end of year	—	—	78,896	44,048

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

The maturity distribution of U.S. government, Federal agency, and GSE securities bought outright, securities purchased under agreements to resell, and securities sold under agreements to repurchase that were allocated to the Bank at December 31, 2008, was as follows (in millions):

	U.S. government securities (par value)	Federal agency and GSE securities (par value)	Subtotal: U.S. government, Federal agency, and GSE securities (par value)	Securities purchased under agreements to resell (contract amount)	Securities sold under agreements to repurchase (contract amount)
Within 15 days	$ 1,904	$ 45	$ 1,949	$ 3,980	$ 8,791
16 days to 90 days	2,086	327	2,413	3,980	—
91 days to 1 year	6,301	97	6,398	—	—
Over 1 year to 5 years	17,246	1,130	18,376	—	—
Over 5 years to 10 years	9,684	362	10,046	—	—
Over 10 years	10,132	—	10,132	—	—
Total allocated to the Bank	$ 47,353	$ 1,961	$ 49,314	$ 7,960	$ 8,791

At December 31, 2008 and 2007, U.S. government securities with par values of $180,765 million and $16,649 million, respectively, were loaned from the SOMA, of which $17,986 million and $1,544 million, respectively, were allocated to the Bank.

7. INVESTMENTS DENOMINATED IN FOREIGN CURRENCIES

The FRBNY, on behalf of the Reserve Banks, holds foreign currency deposits with foreign central banks and with the Bank for International Settlements and invests in foreign government debt instruments. These investments are guaranteed as to principal and interest by the issuing foreign governments.

The Bank's allocated share of investments denominated in foreign currencies was approximately 7.701 percent and 8.328 percent at December 31, 2008 and 2007, respectively.

The Bank's allocated share of investments denominated in foreign currencies, including accrued interest, valued at foreign currency market exchange rates at December 31, was as follows (in millions):

	2008	2007
Euro:		
Foreign currency deposits	$ 428	$ 598
Securities purchased under agreements to resell	314	212
Government debt instruments	355	389
Japanese yen:		
Foreign currency deposits	268	234
Government debt instruments	545	476
Total allocated to the Bank	$ 1,910	$ 1,909

At December 31, 2008 and 2007, the fair value of investments denominated in foreign currencies, including accrued interest, allocated to the Bank was $1,927 million and $1,907 million, respectively. The fair value of government debt instruments was determined by reference to quoted prices for identical securities. The cost basis of foreign currency deposits and securities purchased under agreements to resell, adjusted for accrued interest, approximates fair value. Similar to the U.S. government, Federal agency, and GSE securities discussed in Note 6, unrealized gains or losses have no effect on the ability of a Reserve Bank, as central bank, to meet its financial obligations and responsibilities.

Total System investments denominated in foreign currencies were $24,804 million and $22,914 million at December 31, 2008 and 2007, respectively. At December 31, 2008 and 2007, the fair value of the total System investments denominated in foreign currencies, including accrued interest, was $25,021 million and $22,892 million, respectively.

The maturity distribution of investments denominated in foreign currencies that were allocated to the Bank at December 31, 2008, was as follows (in millions):

	Euro	Japanese Yen	Total
Within 15 days	$ 585	$ 268	$ 853
16 days to 90 days	90	49	139
91 days to 1 year	135	153	288
Over 1 year to 5 years	287	343	630
Total allocated to the Bank	$ 1,097	$ 813	$ 1,910

At December 31, 2008 and 2007, the authorized warehousing facility was $5 billion, with no balance outstanding.

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

8. CENTRAL BANK LIQUIDITY SWAPS

Central bank liquidity swap arrangements are contractual agreements between two parties, the FRBNY and an authorized foreign central bank, whereby the parties agree to exchange their currencies up to a prearranged maximum amount and for an agreed-upon period of time. At the end of that period of time, the currencies are returned at the original contractual exchange rate and the foreign central bank pays interest to the Federal Reserve at an agreed-upon rate. These arrangements give the authorized foreign central bank temporary access to U.S. dollars. Drawings under the swap arrangements are initiated by the foreign central bank and must be agreed to by the Federal Reserve.

The Bank's allocated share of central bank liquidity swaps was approximately 7.701 percent and 8.328 percent at December 31, 2008 and 2007, respectively.

At December 31, 2008 and 2007, the total System amount of foreign currency held under central bank liquidity swaps was $553,728 million and $24,353 million, respectively, of which $42,641 million and $2,028 million, respectively, was allocated to the Bank.

The maturity distribution of central bank liquidity swaps that were allocated to the Bank at December 31 was as follows (in millions):

	2008			2007
	Within 15 days	16 days to 90 days	Total	16 days to 90 days
Australian dollar	$ 770	$ 988	$ 1,758	$ —
Danish krone	—	1,155	1,155	—
Euro	11,626	10,810	22,436	1,689
Japanese yen	3,688	5,762	9,450	—
Korean won	—	797	797	—
Norwegian krone	170	464	634	—
Swedish krona	770	1,155	1,925	—
Swiss franc	1,480	459	1,939	339
U.K. pound	9	2,538	2,547	—
Total	$ 18,513	$ 24,128	$ 42,641	$ 2,028

9. BANK PREMISES, EQUIPMENT, AND SOFTWARE

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

	2008	2007
Bank premises and equipment:		
Land	$ 39	$ 39
Buildings	224	221
Building machinery and equipment	37	36
Construction in progress	1	2
Furniture and equipment	101	102
Subtotal	402	400
Accumulated depreciation	(146)	(131)
Bank premises and equipment, net	$ 256	$ 269
Depreciation expense, for the years ended December 31	$ 18	$ 17

The Bank leases space to outside tenants with remaining lease terms ranging from 1 to 10 years. Rental income from such leases was $4 million and $2 million for the years ended December 31, 2008 and 2007, respectively, and is reported as a component of "Other income." Future minimum lease payments that the Bank will receive under noncancelable lease agreements in existence at December 31, 2008, are as follows (in millions):

2009	$ 3.7
2010	3.4
2011	1.5
2012	0.7
2013	0.2
Thereafter	0.7
Total	$ 10.2

The Bank has capitalized software assets, net of amortization, of $218 thousand and $468 thousand at December 31, 2008 and 2007, respectively.

Amortization expense was $283 thousand and $1 million for the years ended December 31, 2008 and 2007, respectively. Capitalized software assets are reported as a component of "Other assets" and the related amortization is reported as a component of "Other expenses."

Assets impaired as a result of the Bank's restructuring plan, as discussed in Note 14, include equipment and software. Asset impairment losses of $2 million and $1 million for the periods ended December 31, 2008 and 2007, respectively, were determined using fair values based on quoted fair values or other valuation techniques and are reported as a component of "Other expenses."

Additionally, asset write offs of $9 million occurred due to discontinued development of a check application for the period ending December 31, 2008.

10. COMMITMENTS AND CONTINGENCIES

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

At December 31, 2008, the Bank was obligated under noncancelable leases for premises and equipment with remaining terms ranging from 1 to approximately 3 years. These leases provide for increased rental payments based upon increases in real estate taxes.

Rental expense under operating leases for certain operating facilities, warehouses, and office equipment (including taxes, insurance and maintenance when included in rent), net of sublease rentals, was $1 million for each of the years ended December 31, 2008 and 2007.

Future minimum rental payments under noncancelable operating leases with remaining terms of one year or more, at December 31, 2008 were not material.

At December 31, 2008, the Bank, acting on behalf of the Reserve Banks, had unrecorded unconditional purchase commitments extending through the year 2012 with a remaining fixed commitment of $2 million. Purchases of $1 million were made against these commitments during each of the years 2008 and 2007. These commitments represent software license and maintenance fees and have fixed components. The remaining fixed payments under these commitments are as follows (in millions):

	Fixed Commitment
2009	$ 0.7
2010	0.6
2011	0.6
2012	0.1

Under the Insurance Agreement of the Federal Reserve Banks, each of the Reserve Banks has agreed to bear, on a per incident basis, a pro rata share of losses in excess of one percent of the capital paid-in of the claiming Reserve Bank, up to 50 percent of the total capital paid-in of all Reserve Banks. Losses are borne in the ratio of a Reserve Bank's capital paid-in to the total capital paid-in of all Reserve Banks at the beginning of the calendar year in which the loss is shared. No claims were outstanding under the agreement at December 31, 2008 or 2007.

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

11. RETIREMENT AND THRIFT PLANS

Retirement Plans

The Bank currently offers three defined benefit retirement plans to its employees, based on length of service and level of compensation. Substantially all of the Bank's employees participate in the Retirement Plan for Employees of the Federal Reserve System ("System Plan"). Employees at certain compensation levels participate in the Benefit Equalization Retirement Plan ("BEP") and certain Reserve Bank officers participate in the Supplemental Employee Retirement Plan ("SERP").

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

The Bank's projected benefit obligation, funded status, and net pension expenses for the BEP and the SERP at December 31, 2008 and 2007, and for the years then ended, were not material.

Thrift Plan

Employees of the Bank may also participate in the defined contribution Thrift Plan for Employees of the Federal Reserve System ("Thrift Plan"). The Bank matches employee contributions based on a specified formula. For the years ended December 31, 2008 and 2007, the Bank matched 80 percent on the first 6 percent of employee contributions for employees with less than five years of service and 100 percent on the first 6 percent of employee contributions for employees with five or more years of service. The Bank's Thrift Plan contributions totaled $6 million for each of the years ended December 31, 2008 and 2007, and are reported as a component of "Salaries and other benefits" in the Statements of Income and Comprehensive Income. Beginning in 2009, the Bank will match 100 percent of the first 6 percent of employee contributions from the date of hire and provide an automatic employer contribution of 1 percent of eligible pay.

12. POSTRETIREMENT BENEFITS OTHER THAN PENSIONS AND POSTEMPLOYMENT BENEFITS

Postretirement Benefits Other Than Pensions

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

The Bank funds 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):

	2008	2007
Accumulated postretirement benefit obligation at January 1	$ 109.3	$ 105.2
Service cost-benefits earned during the period	4.4	4.5
Interest cost on accumulated benefit obligation	7.0	6.6
Net actuarial loss (gain)	1.4	(3.1)
Curtailment gain	(2.9)	—
Contributions by plan participants	1.3	1.1
Benefits paid	(5.2)	(5.3)
Medicare Part D subsidies	0.3	0.3
Accumulated postretirement benefit obligation at December 31	$ 115.6	$ 109.3

At December 31, 2008 and 2007, the weighted-average discount rate assumptions used in developing the postretirement benefit obligation were 6.00 percent and 6.25 percent, respectively.

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

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

	2008	2007
Fair value of plan assets at January 1	$ —	$ —
Contributions by the employer	3.6	3.9
Contributions by plan participants	1.3	1.1
Benefits paid	(5.2)	(5.3)
Medicare Part D subsidies	0.3	0.3
Fair value of plan assets at December 31	$ —	$ —
Unfunded obligation and accrued postretirement benefit cost	$ 115.6	$ 109.3
Amounts included in accumulated other comprehensive loss are shown below:		
Prior service cost	$ 2.8	$ 4.0
Net actuarial loss	(21.6)	(24.8)
Deferred curtailment gain	0.5	—
Total accumulated other comprehensive loss	$ (18.3)	$ (20.8)

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

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

	2008	2007
Health care cost trend rate assumed for next year	7.50%	8.00%
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	2014	2013

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, 2008 (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	$ 1.8	$ (1.5)
Effect on accumulated postretirement benefit obligation	14.9	(12.4)

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

	2008	2007
Service cost-benefits earned during the period	$ 4.4	$ 4.5
Interest cost on accumulated benefit obligation	7.0	6.6
Amortization of prior service cost	(1.2)	(1.2)
Amortization of net actuarial loss	2.1	3.8
Total periodic expense	12.3	13.7
Curtailment loss	0.1	—
Net periodic postretirement benefit expense	$ 12.4	$ 13.7
Estimated amounts that will be amortized from accumulated other comprehensive loss into net periodic postretirement benefit expense in 2009 are shown below:		
Prior service cost	$ (1.1)	
Net actuarial loss	1.0	
Total	$ (0.1)	

Net postretirement benefit costs are actuarially determined using a January 1 measurement date. At January 1, 2008 and 2007, the weighted-average discount rate assumptions used to determine net periodic postretirement benefit costs were 6.25 percent and 5.75 percent, respectively.

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

A deferred curtailment gain was recorded in 2008 as a component of accumulated other comprehensive loss; the gain will be recognized in net income in future years when the related employees terminate employment.

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 established a prescription drug benefit under Medicare ("Medicare Part D") and a federal subsidy to sponsors of retiree health care benefit plans that provide benefits that are at least actuarially equivalent to Medicare Part D. The benefits provided under the Bank's plan to certain participants are at least actuarially equivalent to the Medicare Part D prescription

drug benefit. The estimated effects of the subsidy are reflected in actuarial loss in the accumulated postretirement benefit obligation and net periodic postretirement benefit expense.

Federal Medicare Part D subsidy receipts were $0.3 million and $0.6 million in the years ended December 31, 2008 and 2007, respectively. Expected receipts in 2009, related to benefits paid in the years ended December 31, 2008 and 2007 are $0.2 million.

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

	Without subsidy	With subsidy
2009	$ 6.0	$ 5.6
2010	6.6	6.2
2011	7.2	6.7
2012	7.6	7.0
2013	8.0	7.4
2014–2018	45.6	41.3
Total	$ 81.0	$ 74.2

Postemployment Benefits

The Bank offers benefits to former or inactive employees. Postemployment benefit costs are actuarially determined using a December 31 measurement date and include the cost of medical and dental insurance, survivor income, disability benefits, and self-insured workers' compensation expenses. The accrued postemployment benefit costs recognized by the Bank at December 31, 2008 and 2007, were $10 million and $11 million, respectively. This cost is included as a component of "Accrued benefit costs" in the Statements of Condition. Net periodic postemployment benefit expense (credit) included in 2008 and 2007 operating expenses were $128 thousand and ($577) thousand, respectively, and are recorded as a component of "Salaries and other benefits" in the Statements of Income and Comprehensive Income.

13. ACCUMULATED OTHER COMPREHENSIVE INCOME AND OTHER COMPREHENSIVE INCOME

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

	Amount related to postretirement benefits other than pensions
Balance at January 1, 2007	$ (27)
Change in funded status of benefit plans:	
Net actuarial gain arising during the year	3
Amortization of prior service cost	(1)
Amortization of net actuarial loss	4
Change in funded status of benefit plans— other comprehensive income	6
Balance at December 31, 2007	$ (21)
Change in funded status of benefit plans:	
Net actuarial gain arising during the year	$ 1
Deferred curtailment gain	1
Amortization of prior service cost	(1)
Amortization of net actuarial loss	2
Change in funded status of benefit plans— other comprehensive income	3
Balance at December 31, 2008	$ (18)

Additional detail regarding the classification of accumulated other comprehensive loss is included in Note 12.

14. BUSINESS RESTRUCTURING CHARGES

2008 Restructuring Plans

In 2008, the Reserve Banks announced the acceleration of their check restructuring initiatives to align the check processing infrastructure and operations with declining check processing volumes. The new infrastructure will involve consolidation of operations into two regional Reserve Bank processing sites in Cleveland and Atlanta. Additional announcements in 2008 included restructuring plans associated with the closure of the Retail Product Office's Check Contingency Center in Birmingham and the consolidation of Check Adjustments to FRB Cleveland.

2007 Restructuring Plans

In 2007, the Reserve Banks announced a restructuring initiative to align the check processing infrastructure and operations with declining check processing volumes.

2006 and Prior Restructuring Costs

The Bank incurred various restructuring charges prior to 2007 related to the restructuring of check processing and cash processing.

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

	2006 and prior restructuring plans	2007 restructuring plans	2008 restructuring plans	Total
Information related to restructuring plans as of December 31, 2008:				
Total expected costs related to restructuring activity	$ 5.0	$ 2.9	$ 7.4	$ 15.3
Expected completion date	2007	2008	2008	
Reconciliation of liability balances:				
Balance at January 1, 2007	$ 5.0	$ —	$ —	$ 5.0
Employee separation costs	—	2.6	—	2.6
Adjustments	(2.6)	—	—	(2.6)
Payments	(2.3)	—	—	(2.3)
Balance at December 31, 2007	$ 0.1	$ 2.6	$ —	$ 2.7
Employee separation costs	—	—	7.4	7.4
Adjustments	—	0.3	—	0.3
Payments	(0.1)	(2.7)	—	(2.8)
Balance at December 31, 2008	$ —	$ 0.2	$ 7.4	$ 7.6

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

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

Restructuring costs associated with the impairment of certain Bank assets, including software and equipment, are discussed in Note 9. Costs associated with enhanced pension benefits for all Reserve Banks are recorded on the books of the FRBNY as discussed in Note 11.

15. SUBSEQUENT EVENTS

In February 2009, the System announced the extension through October 30, 2009, of liquidity programs that were previously scheduled to expire on April 30, 2009. The extension pertains to the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility and the Term Securities Lending Facility. In addition, the temporary reciprocal currency arrangements (swap lines) between the Federal Reserve and other central banks were extended to October 30, 2009.

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