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Councils

(From left) Mr. Hakkio, Mr. Dubbert, Ms. George, Mr. Barkema, Mr. Hoenig, Mr. Bacon, Mr. Rasdall, Mr. Scott, Mr. Gambs, Ms. Pacheco, Ms. Hearn

Management Committee

Thomas M. Hoenig
President and Chief Executive Officer

Richard K. Rasdall, Jr.
First Vice President and Chief Operating Officer

Alan D. Barkema
Senior Vice President

Kelly J. Dubbert
Senior Vice President

Carl M. Gambs
Senior Vice President

Esther L. George
Senior Vice President

Craig S. Hakkio
Senior Vice President and Director of Research

Roberta E. Hearn
Senior Vice President

Barbara S. Pacheco
Senior Vice President

Kent M. Scott
Senior Vice President

Charles L. Bacon, Jr.
Senior Vice President,
General Counsel and Secretary
Advisor to Management Committee

Boards of Directors

(From left) Mr. Schifferdecker, Mr. Dillingham, Mr. Moore, Mr. Smalley, Mr. Funk, Mr. Fricke, Ms. Cordova, Mr. Nunnink, Mr. Bard

Kansas City

Robert A. Funk, Chairman and Federal Reserve Agent
Chairman of the Board and Chief Executive Officer
Express Personnel Services International
Oklahoma City, Oklahoma (Class C)

Richard H. Bard, Deputy Chairman
Chairman and Chief Executive Officer
International Surface Preparation Corporation
Golden, Colorado (Class C)

Lu Cordova
Chief Executive Officer, Corlund Industries
Chairman, CTEK Angels
Boulder, Colorado (Class C)

Dan L. Dillingham
Chief Executive Officer, Dillingham Insurance
Enid, Oklahoma (Class B, Group 2)

Robert C. Fricke
President and Chief Executive Officer
Farmers & Merchants National Bank
Ashland, Nebraska (Class A, Group 3)

Frank Moore
President, Spearhead Ranch Company
Douglas, Wyoming (Class B, Group 3)

Kevin K. Nunnink
Chairman, Integra Realty Resources
Westwood, Kansas (Class B, Group 1)

Mark W. Schifferdecker
President and Chief Executive Officer
Girard National Bank
Girard, Kansas (Class A, Group 2)

Rick L. Smalley
Chief Executive Officer
Dickinson Financial Corporation
Kansas City, Missouri (Class A, Group 1)

Federal Advisory Council Representative
Byron G. Thompson (not pictured)
Chairman, Country Club Bank
Kansas City, Missouri

NOTE: For an explanation of class and group designations, turn to Page 28.

(From top left, standing) Mr. Helzer, Mr. Stanford, Mr. Pearson. (From bottom left, seated) Ms. Avila, Ms. Berkeley, Mr. Williams, Ms. Schloss

Denver Branch

Appointed by the Board of Governors of the Federal Reserve System

Thomas Williams, Chairman of the Branch Board
President and Chief Executive Officer
Williams Group LLC
Golden, Colorado

Kathleen Avila
Managing Member
Avila Retail Development and Management
Albuquerque, New Mexico

Kristy A. Schloss
President and Chief Executive Officer
Schloss Engineered Equipment, Inc.
Aurora, Colorado

Appointed by the Board of Directors, Federal Reserve Bank of Kansas City

Virginia K. Berkeley
President
Colorado Business Bank, N.A.
Denver, Colorado

James A. Helzer
President and Chief Executive Officer
Unicover Corporation
Cheyenne, Wyoming

John D. Pearson
Real Estate Broker/Owner
Pearson Real Estate Company, Inc.
Buffalo, Wyoming

Michael R. Stanford
President and Chief Executive Officer
First State Bancorporation
Albuquerque, New Mexico

Boards of Directors

(From left) Mr. Ramos, Mr. Ratcliffe, Mr. Nichols, Mr. Minner, Ms. Almon, Mr. Gilbert, Mr. Packnett

Oklahoma City Branch

Appointed by the Board of Governors of the Federal Reserve System

Tyree O. Minner, Chairman of the Branch Board
Plant Manager
General Motors, Oklahoma City Assembly Plant
Oklahoma City, Oklahoma

J. Larry Nichols
Chairman and Chief Executive Officer
Devon Energy Corporation
Oklahoma City, Oklahoma

Michael J. Packnett
President and Chief Executive Officer
Mercy Health Center
Oklahoma City, Oklahoma

Appointed by the Board of Directors, Federal Reserve Bank of Kansas City

Terry M. Almon
President and Chief Executive Officer
Arkansas Valley State Bank
Broken Arrow, Oklahoma

Robert R. Gilbert III
President, Chief Operating Officer and Director
The F&M Bank & Trust Company
Tulsa, Oklahoma

Fred M. Ramos
President
Greater Tulsa Hispanic Chamber of Commerce
Tulsa, Oklahoma

Richard K. Ratcliffe
Chairman
Ratcliffe's Inc.
Weatherford, Oklahoma

(From left) Mr. Moore, Mr. Hermes, Ms. Owen, Mr. Nelson, Mr. Timmerman, Ms. Milligan, Mr. Lopez

Omaha Branch

Appointed by the Board of Governors of the Federal Reserve System

Charles R. Hermes
President
Dutton-Lainson Company
Hastings, Nebraska

Terry L. Moore
President
Omaha Federation of Labor
Omaha, Nebraska

James A. Timmerman, Chairman of Branch Board
Chief Financial Officer
Timmerman & Sons Feeding Co.
Springfield, Nebraska

Appointed by the Board of Directors, Federal Reserve Bank of Kansas City

Rodrigo Lopez
President and Chief Executive Officer
AmeriSphere Multifamily Finance, L.L.C.
Omaha, Nebraska

Cynthia Hardin Milligan
Dean, College of Business Administration
University of Nebraska-Lincoln
Lincoln, Nebraska

Michael J. Nelson
Chairman
FirsTier Bank
Kimball, Nebraska

Judith A. Owen
Retired President and Chief Executive Officer
Wells Fargo Bank, N.A.
Omaha, Nebraska

Advisory Councils

(From left) Mr. King, Mr. Shaw, Mr. Stout, Ms. Johnson, Mr. Liston, Mr. Roetheli, Mr. Heilbrun, Mr. Tamba

Jeff Heilbrun
Vice President/Project Development
Destination Club Partners
Jackson, Wyoming

Deborah Johnson
Chief Executive Officer
Rick Johnson and Company, Inc.
Albuquerque, New Mexico

Ralph King
Owner/Operator
King's Management Company, Inc.
Kansas City, Kansas

Dennis Liston
Financial Secretary
International Brotherhood of Electrical Workers
Kansas City, Missouri

Russell M. Perry (not pictured)
President
Perry Publishing and Broadcasting Company
Oklahoma City, Oklahoma

Tom B. Price (not pictured)
President
UFCW District Union Local Two, AFL-CIO
Kansas City, Missouri

Anthony F. Prinster (not pictured)
Hoskin, Farina, Aldrich & Kampf
Grand Junction, Colorado

Joe Roetheli
General Manager
S&M NuTec, LLC
North Kansas City, Missouri

Michael Shaw
President and Owner
Mike Shaw Chevrolet, Buick, Saab
Denver, Colorado

John Stout
Chief Executive Officer
Plaza Belmont Management Group, LLC
Shawnee Mission, Kansas

Shin-ichi Tamba
President
Kawasaki Motors Manufacturing Corp., U.S.A.
Lincoln, Nebraska

Community Development Advisory Council

(From left) Senior Vice President Alan Barkema, Mr. Johnson, Mr. Clark, Ms. Tinney, Mr. Kenny, Mr. Loy, Assistant Vice President Paul Coquillette

Dan V. Clark
Clark Consulting Group
Arvada, Colorado

Patricia B. Fennell (not pictured)
Executive Director
Latino Community Development Agency
Oklahoma City, Oklahoma

Carol A. Grimaldi (not pictured)
Executive Director
Brush Creek Community Partners
Kansas City, Missouri

Edward F. Honesty, Jr. (not pictured)
President and Chief Operating Officer
Best Harvest Bakeries
Kansas City, Kansas

Thomas G. Johnson
Director
Community Policy Analysis Center
University of Missouri
Columbia, Missouri

Tim Kenny
Executive Director
Nebraska Investment Finance Authority
Lincoln, Nebraska

A. Thomas Loy
Chairman and President
MetaFund
Oklahoma City, Oklahoma

Linda Tinney
Vice President, Community Development,
and CRA Officer
U.S. Bank
Denver, Colorado

Robin Wells (not pictured)
Senior Vice President
Country Club Bank
Kansas City, Missouri

Customer Advisory Council on Financial Services

Kansas City

Tim Connealy
Executive Vice President and Chief Operating Officer
Bank Midwest
Kansas City, Missouri

Lloyd Davidson
President
First Bank Kansas
Salina, Kansas

William Esry
President and Chief Executive Officer
Blue Ridge Bank and Trust Company
Kansas City, Missouri

Steve Hipp
Executive Vice President
Intrust Bank, N.A.
Wichita, Kansas

L.D. McDonald
President and Chief Executive Officer
Midwest Independent Bank
Jefferson City, Missouri

Bruce Schriefer
President and Chief Executive Officer
Bankers' Bank of Kansas
Wichita, Kansas

Denver

Adam P. Coyle
President
Integrated Payment Systems
Englewood, Colorado

Mark Frank
Senior Operations Executive
CoBiz Bank, N.A.
Denver, Colorado

Roger R. Reiling
President
Bankers' Bank of the West
Denver, Colorado

James A. Reuter
President
FirstBankData Corporation
Lakewood, Colorado

Barbara M.A. Walker
Executive Manager
Independent Bankers of Colorado
Denver, Colorado

Oklahoma City

Don Abernathy
President and Chief Executive Officer
The Bankers Bank
Oklahoma City, Oklahoma

Scott Copeland
Executive Vice President
BancFirst
Oklahoma City, Oklahoma

Kerby E. Crowell
Executive Vice President
Stillwater National Bank and Trust Co.
Stillwater, Oklahoma

C.H. Wyatt, Jr.
Vice Chair and President
Interbank
Elk City, Oklahoma

Omaha

Craig E. Champion
Senior Vice President
TierOne Bank
Lincoln, Nebraska

Alan L. Fosler
Senior Vice President and Cashier
Union Bank and Trust Company
Lincoln, Nebraska

Timothy D. Hart
Chief Financial Officer, Secretary and Treasurer
First National Bank of Omaha
Omaha, Nebraska

Gerald E. Wortman
President and Chief Executive Officer
Sherman County Bank
Loup City, Nebraska

Credit Union Customer Advisory Council

Oklahoma City Branch

Kevin Bilbrey
President
Halliburton Employees Federal Credit Union
Duncan, Oklahoma

Janice Caster
Managing Officer
El Reno RIL Credit Union
El Reno, Oklahoma

William (Bill) Counts
President and Chief Executive Officer
Communication Federal Credit Union
Oklahoma City, Oklahoma

Terri Davis
Vice President
66 Federal Credit Union
Bartlesville, Oklahoma

Tom Eaton
Managing Officer
St. Francis Employees Federal Credit Union
Tulsa, Oklahoma

Denise Floyd
President and Chief Executive Officer
Fort Sill Federal Credit Union
Fort Sill, Oklahoma

Mark W. Kelly
President and Chief Executive Officer
Oklahoma Employees Credit Union
Oklahoma City, Oklahoma

Mike Kloiber
President and Chief Executive Officer
Tinker Federal Credit Union
Oklahoma City, Oklahoma

Lynette Leonard
President
Allegiance Credit Union
Oklahoma City, Oklahoma

Steve Rasmussen
President and Chief Executive Officer
FAA Employees Credit Union
Oklahoma City, Oklahoma

Marsha Schmidt
President
Red Crown Federal Credit Union
Tulsa, Oklahoma

Tenth District Officers

Kansas City

Thomas M. Hoenig
President and Chief Executive Officer

Richard K. Rasdall, Jr.
First Vice President and Chief Operating Officer

Charles L. Bacon, Jr.
Senior Vice President, General Counsel, and Secretary

Alan D. Barkema
Senior Vice President

Kelly J. Dubbert
Senior Vice President

Carl M. Gambs
Senior Vice President

Esther L. George
Senior Vice President

Craig S. Hakkio
Senior Vice President and Director of Research

Roberta E. Hearn
Senior Vice President

Stephen E. McBride
Senior Vice President and General Auditor

Barbara S. Pacheco
Senior Vice President

Kent M. Scott
Senior Vice President

John E. Yorke
Senior Vice President

Todd E. Clark
Vice President and Economist

Denise I. Connor
Vice President

Anita F. Costanza
Vice President

Mark R. Drabenstott
Vice President and Director, Center for the Study of Rural America

Steven D. Evans
Vice President

Janel K. Frisch
Vice President and Chief Financial Officer

George A. Kahn
Vice President and Associate Director of Research

Sharon Kozicki
Vice President and Economist

Kevin L. Moore
Vice President

Dawn B. Morhaus
Vice President

Charles S. Morris
Vice President

Karen A. Pennell
Vice President

Diane M. Raley
Vice President and Public Information Officer

Randy M. Schartz
Vice President

Stacey L. Schreft
Vice President and Economist

Linda S. Schroeder
Vice President

Veronica R. Sellers
Vice President and Associate General Counsel

Gordon H. Sellon, Jr.
Vice President and Economist

Stuart E. Weiner
Vice President and Director, Payments System Research

Dick H. Woods, Jr.
Vice President

Susan E. Zubradt
Vice President

Josias A. Aleman
Assistant Vice President and Assistant General Auditor

Larry D. Bailey
Assistant Vice President

Stanley R. Beatty
Assistant Vice President

Debra L. Bronston
Assistant Vice President

Harriet I. Chern
Assistant Vice President

Michael R. Childs
Assistant Vice President

Paul S.J. Coquillette
Assistant Vice President and Community Affairs Officer

Kelley D. Courtright
Assistant Vice President

Kristi A. Coy
Assistant Vice President

Kevin J. Craig
Assistant Vice President

Tanya L. Cvetan
Assistant Vice President

Nigel S. Davis
Assistant Vice President

James R. Deis
Assistant Vice President

Linda K. Edwards
Assistant Vice President

C. Alan Garner
Assistant Vice President

Lori D. Haley
Assistant Vice President

Ann L. Hoelting
Assistant Vice President

James H. Hunter
Assistant Vice President

William R. Keeton
Assistant Vice President and Economist

W. Todd Mackey
Assistant Vice President

D. Michael Manies
Assistant Vice President

Renu A. Mehra
Assistant Vice President

Korie Miller
Assistant Vice President

Randall L. Mueller
Assistant Vice President

Annette K. Owens
Assistant Vice President

Wayne M. Powell
Assistant Vice President and Assistant Secretary

Michael R. Steckline
Assistant Vice President

Lawrence D. Taft
Assistant Vice President

Leesa Guyton Thompson
Assistant Vice President

Wilmer R. Ullmann
Associate General Counsel and Ethics Officer

Donna J. Ward
Assistant Vice President

Kathryn A. Webster
Assistant Vice President

Stephan Weiler
Assistant Vice President and Economist

Ginger K. Wise
Assistant Vice President

Margaret L. Yarrington
Assistant Vice President

Catherine A. Zeigler
Assistant Vice President

Denver

Pamela L. Weinstein
Vice President and Branch Manager

Thomas P. Bennett
Assistant Vice President

Gary E. Darby
Assistant Vice President

Debbie L. Meyers
Assistant Vice President

Oklahoma City

Dwayne E. Boggs
Vice President and Branch Manager

Tara B. Koenigs
Assistant Vice President

Robert W. Toler
Assistant Vice President

Omaha

Kevin A. Drusch
Vice President and Branch Manager

Ronald M. Ryan
Assistant Vice President and Assistant Branch Manager

D. Rick Lay
Assistant Vice President


FINANCIAL
report
Statements
Notes

Federal Reserve Bank of Kansas City

925 Grand Boulevard
Kansas City, Missouri 64198-0001
(816) 881-2000

To the Board of Directors:

The management of the Federal Reserve Bank of Kansas City ("FRBKC") is responsible for the preparation and fair presentation of the Statement of Financial Condition, Statement of Income, and Statement of Changes in Capital as of December 31,2005 (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 the Federal Reserve Banks ("Manual"), and as such, include amounts, some of which are based on judgments and estimates of management. 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 FRBKC is responsible for maintaining an effective process of internal controls over financial reporting including the safeguarding of assets as they relate to the Financial Statements. Such internal controls are designed to provide reasonable assurance to management and to the Board of Directors regarding the preparation of reliable Financial Statements. This process of internal controls contains self-monitoring mechanisms, including, but not limited to, divisions of responsibility and a code of conduct. Once identified, any material deficiencies in the process of internal controls are reported to management, and appropriate corrective measures are implemented.

Even an effective process of internal controls, 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.

The management of the FRBKC assessed its process of internal controls over financial reporting including the safeguarding of assets 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 (COSO). Based on this assessment, we believe that the FRBKC maintained an effective process of internal controls over financial reporting including the safeguarding of assets as they relate to the Financial Statements.

Thomas M. Hoenig
President

Richard K. Rasdall, Jr.
First Vice President

Janel K. Frisch
Vice President, Chief Financial Officer

Federal Reserve Bank of Kansas City
March 2, 2006

PRICEWATERHOUSECOOPERS

Report of Independent Accountants

PricewaterhouseCoopers LLP
1055 Broadway
10th Floor
Kansas City MO 64105-1595
Telephone (816) 472 7921
Facsimile (816) 218 1890

To the Board of Directors of the
Federal Reserve Bank of Kansas City

We have examined management's assertion, included in the accompanying Management Assertion, that the Federal Reserve Bank of Kansas City ("FRB Kansas City") maintained effective internal control over financial reporting and the safeguarding of assets as they relate to the financial statements as of December 31, 2005, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. FRB Kansas City's management is responsible for maintaining effective internal control over financial reporting and safeguarding of assets as they relate to the financial statements. Our responsibility is to express an opinion on management's assertion based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included obtaining an understanding of internal control over financial reporting, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of internal control over financial reporting to future periods are subject to the risk that the internal control may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assertion that FRB Kansas City maintained effective internal control over financial reporting and over the safeguarding of assets as they relate to the financial statements as of December 31, 2005 is fairly stated, in all material respects, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

This report is intended solely for the information and use of management and the Board of Directors and Audit Committee of FRB Kansas City, and any organization with legally defined oversight responsibilities and is not intended to be and should not be used by anyone other than these specified parties.

PricewaterhouseCoopers LLP

March 8, 2006
Kansas City, Missouri

PRICEWATERHOUSECOOPERS

Report of Independent Auditors

PricewaterhouseCoopers LLP
1055 Broadway
10th Floor
Kansas City MO 64105-1595
Telephone (816) 472 7921
Facsimile (816) 218 1890

To the Board of Governors of the Federal Reserve System
and the Board of Directors of the Federal Reserve Bank of Kansas City

We have audited the accompanying statements of condition of the Federal Reserve Bank of Kansas City (the "Bank") as of December 31, 2005 and 2004, and the related statements of income and changes in capital for the years then ended, which have been prepared in conformity with the accounting principles, policies, and practices established by the Board of Governors of the Federal Reserve System. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 3, these financial statements were prepared in conformity with the accounting principles, policies, and practices established by the Board of Governors of the Federal Reserve System. These principles, policies, and practices, which were designed to meet the specialized accounting and reporting needs of the Federal Reserve System, are set forth in the *Financial Accounting Manual for Federal Reserve Banks* and constitute a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as of December 31, 2005 and 2004, and results of its operations for the years then ended, on the basis of accounting described in Note 3.

PricewaterhouseCoopers LLP

March 8, 2006
Kansas City, Missouri

Federal Reserve Bank of Kansas City

STATEMENTS OF CONDITION (in millions)

As of December 31, 2005 and 2004

	2005	2004
ASSETS		
Gold certificates	$ 318	$ 302
Special drawing rights certificates	66	66
Coin	61	48
Items in process of collection	591	653
Loans to depository institutions	11	1
U.S. government securities, net	21,219	19,067
Investments denominated in foreign currencies	246	392
Accrued interest receivable	165	134
Interdistrict settlement account	2,422	1,584
Bank premises and equipment, net	101	102
Other assets	10	15
Total assets	$ 25,210	$ 22,364
LIABILITIES AND CAPITAL		
LIABILITIES:		
Federal Reserve notes outstanding, net	$ 22,816	$ 20,038
Securities sold under agreements to repurchase	863	809
Deposits:		
Depository institutions	655	721
Other deposits	2	2
Deferred credit items	456	409
Interest on Federal Reserve notes due U.S. Treasury	21	30
Accrued benefit costs	39	41
Other liabilities	8	8
Total liabilities	24,860	22,058
CAPITAL:		
Capital paid-in	175	153
Surplus	175	153
Total capital	350	306
Total liabilities and capital	$ 25,210	$ 22,364

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

Federal Reserve Bank of Kansas City

STATEMENTS OF INCOME (in millions)

For the years ended December 31, 2005 and 2004

	2005	2004
INTEREST INCOME:		
Interest on U.S. government securities	$ 781	$ 581
Interest on investments denominated in foreign currencies	4	5
Interest on loans to depository institutions	1	-
Total interest income	786	586
Interest expense:		
Interest expense on securities sold under agreements to repurchase	23	8
Net interest income	763	578
OTHER OPERATING INCOME:		
Income from services	-	53
Compensation received for check services provided	56	-
Reimbursable services to government agencies	11	14
Foreign currency gains (losses), net	(38)	23
Other income	2	1
Total other operating income	31	91
OPERATING EXPENSES:		
Salaries and other benefits	109	104
Occupancy expense	9	9
Equipment expense	9	10
Assessments by Board of Governors	20	22
Other expenses	43	37
Total operating expenses	190	182
Net income prior to distribution	$ 604	$ 487
DISTRIBUTION OF NET INCOME:		
Dividends paid to member banks	$ 10	$ 9
Transferred to (from) surplus	22	(9)
Payments to U.S. Treasury as interest on Federal Reserve notes	572	487
Total distribution	$ 604	$ 487

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

Federal Reserve Bank of Kansas City
STATEMENTS OF CHANGES IN CAPITAL (in millions)

For the years ended December 31, 2005 and 2004

	Capital Paid-in	Surplus	Total Capital
BALANCE AT JANUARY 1, 2004 (3.2 million shares)	$ 162	$ 162	$ 324
Transferred from surplus	-	(9)	(9)
Net change in capital stock redeemed (0.1 million shares)	(9)	-	(9)
BALANCE AT DECEMBER 31, 2004 (3.1 million shares)	$ 153	$ 153	$ 306
Transferred to surplus	-	22	22
Net change in capital stock issued (0.4 million shares)	22	-	22
BALANCE AT DECEMBER 31, 2005 (3.5 million shares)	$ 175	$ 175	$ 350

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

1. STRUCTURE

The Federal Reserve Bank of Kansas City ("Bank") is part of the Federal Reserve System ("System") and 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 and its branches in Denver, Colorado, Oklahoma City, Oklahoma, and Omaha, Nebraska, serve the Tenth Federal Reserve District, which includes Colorado, Kansas, Nebraska, Oklahoma, Wyoming and portions of Missouri and New Mexico.

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, 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 of the Federal Reserve System ("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 System performs a variety of services and operations. Functions include formulating and conducting monetary policy; participating actively in the payments system including large-dollar transfers of funds, automated clearinghouse ("ACH") operations, and check processing; distributing coin and currency; performing fiscal agency functions for the U.S. Treasury and certain federal agencies; serving as the federal government's bank; providing short-term loans to depository institutions; serving the consumer and the community by providing educational materials and information regarding consumer laws; supervising bank holding companies, state member banks, and U.S. offices of foreign banking organizations; and administering other regulations of the Board of Governors. The System also provides certain services to foreign central banks, governments, and international official institutions.

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 for its execution of transactions. FRBNY is authorized to conduct operations in domestic markets, including direct purchase and sale of U.S. government securities, the purchase of securities under agreements to resell, the sale of securities under agreements to repurchase, and the lending of U.S. government securities. FRBNY executes these open market transactions and holds the resulting securities, with the exception of securities purchased under agreements to resell, 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 FRBNY to execute operations in foreign markets for major currencies 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 ("F/X") and securities contracts for nine foreign currencies and to invest such foreign currency holdings ensuring adequate liquidity is maintained. In addition, FRBNY is authorized to maintain reciprocal currency arrangements ("F/X swaps") with two central banks, and "warehouse" foreign currencies for the U.S. Treasury and Exchange Stabilization Fund ("ESF") through the Reserve Banks. In connection with its foreign currency activities, FRBNY may enter into contracts that contain varying degrees of off-balance-sheet market risk, because they represent contractual commitments involving future settlement and counter-party credit risk. The FRBNY controls credit risk by obtaining credit approvals, establishing transaction limits, and performing daily monitoring procedures.

Although Reserve Banks are separate legal entities, in the interests of greater efficiency and effectiveness, they collaborate in the delivery of certain operations and services. The collaboration takes the form of centralized competency centers, operations sites, and product or service 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 Bank providing the service and the other eleven Reserve Banks. In some cases, costs incurred by a Reserve Bank for services provided to other Reserve Banks are not shared; in other cases, Reserve Banks are billed for services provided to them by another Reserve Bank.

Major services provided on behalf of the System by the Bank, for which the costs were not redistributed to the other Reserve Banks, include: Check Automation Services, Customer Relations and Support Office/Customer Contact Center, Wholesale Operations Site, People*Soft* Support Center, and Billing Operations Site.

Beginning in 2005, the Reserve Banks adopted a new management model for providing check services to depository institutions. Under this new model, the Federal Reserve Bank of Atlanta ("FRBA") has the overall responsibility for managing the Reserve Banks' provision of check services and recognizes total System check revenue on its Statements of Income. FRBA compensates the other eleven Banks for the costs incurred to provide check services. This compensation is reported as "Compensation received for check services provided" in the Statements of Income. If the management model had been in place in 2004, the Bank would have reported $59 million as "Compensation received for check services provided" and $53 million in "Income from services" would have been reported by FRBA rather than the Bank.

3. SIGNIFICANT ACCOUNTING POLICIES

Accounting principles for entities with the unique powers and responsibilities of the nation's central bank have not been formulated by the various accounting standard-setting bodies. The Board of Governors has developed specialized accounting principles and practices that it believes are appropriate for the significantly different nature and function of a central bank as compared with the private sector. These accounting principles and practices are documented in the *Financial Accounting*

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

Differences exist between the accounting principles and practices in the Financial Accounting Manual and those generally accepted 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 security holdings at amortized cost, rather than using the fair value presentation requirements in accordance with GAAP. Amortized cost more appropriately reflects the Bank's security holdings given its unique responsibility to conduct monetary policy. While 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 affect 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 security and foreign currency transactions, including their purchase and sale, are motivated by monetary policy objectives rather than profit. Accordingly, market values, earnings, and any gains or losses resulting from the sale of such securities and currencies are incidental to the open market operations and do not motivate its activities or policy decisions.

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 Bank's unique powers and responsibilities. A Statement of Cash Flows, therefore, would not provide any additional meaningful information. Other information regarding the Bank's activities is provided in, or may be derived from, the Statements of Condition, Income, and Changes in Capital. There are no other significant differences between the policies outlined in the Financial Accounting Manual and GAAP.

The preparation of the financial statements in conformity with the Financial Accounting Manual requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, 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. 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. These 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 lowered. The value of gold for purposes of backing the gold certificates is set by law at $42 \frac{2}{9}$ a fine troy ounce. The Board of Governors allocates the gold certificates among Reserve Banks once a year based on the average Federal Reserve notes outstanding in each Reserve Bank.

Special drawing rights ("SDRs") are issued by the International Monetary Fund ("Fund") to its members in proportion to each member's quota in the Fund at the time of issuance. SDRs serve as a supplement to international monetary reserves and may be transferred from one national monetary authority to another. Under the law providing for United States 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. At such time, 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 Reserve Banks based upon Federal Reserve notes outstanding in each District at the end of the preceding year. There were no SDR transactions in 2005 or 2004.

b. Loans to Depository Institutions

All depository institutions that maintain reservable transaction accounts or nonpersonal time deposits, as defined in regulations issued by the Board of Governors, have borrowing privileges at the discretion of the Reserve Bank. Borrowers execute certain lending agreements and deposit sufficient collateral before credit is extended. Loans are evaluated for collectibility, and currently all are considered collectible and fully collateralized. If loans were ever deemed to be uncollectible, an appropriate reserve would be established. Interest is accrued using the applicable discount rate established at least every fourteen days by the Board of Directors of the Reserve Bank, subject to review by the Board of Governors.

c. U.S. Government Securities and Investments Denominated in Foreign Currencies

U.S. government securities and investments denominated in foreign currencies comprising the SOMA are recorded at cost, on a settlement-date basis, and adjusted for amortization of premiums or accretion of discounts on a straight-line basis. Interest income is accrued on a straight-line basis. Gains and losses resulting from sales of securities are determined by specific issues 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 (losses), net."

Activity related to U.S. government securities, including the related premiums, discounts, and realized and unrealized gains and losses, is allocated to each Reserve Bank on a percentage basis derived from an annual settlement of interdistrict clearings that occurs in April of each year. The settlement equalizes Reserve Bank gold certificate holdings to Federal Reserve notes outstanding in each District. Activity related to investments in foreign-currency-denominated assets 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.

d. U.S. Government Securities Sold Under Agreements to Repurchase and Securities Lending

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 carried in the Statements of Condition at their contractual amounts and the related accrued interest is reported as a component of "Other liabilities."

U.S. government securities held in the SOMA are lent to U.S. government securities dealers and to banks participating in U.S. government securities clearing arrangements in order to facilitate the effective functioning of the domestic securities market. Securities-lending transactions are fully collateralized by other U.S. government securities and the collateral taken is in excess of the market value of the securities loaned. The FRBNY charges the dealer or bank a fee for borrowing securities and the fees are reported as a component of "Other Income" in the Statements of Income.

Activity related to U.S. government securities sold under agreements to repurchase and securities lending is allocated to each Reserve Bank on a percentage basis derived from the annual settlement of interdistrict clearings. Securities purchased under agreements to resell are allocated to FRBNY and not to the other Banks.

e. Foreign Currency Swaps and Warehousing

F/X swap arrangements are contractual agreements between two parties to exchange specified currencies, at a specified price, on a specified date. The parties agree to exchange their currencies up to a pre-arranged maximum amount and for an agreed-upon period of time (up to twelve months), at an agreed-upon interest rate. These arrangements give the FOMC temporary access to the foreign currencies it may need to intervene to support the dollar and give the counterparty temporary access to dollars it may need to support its own currency. Drawings under the F/X swap arrangements can be initiated by either FRBNY or the counterparty (the drawer) and must be agreed to by the drawee. The F/X swaps are structured so that the party initiating the transaction bears the exchange rate risk upon maturity. FRBNY will generally invest the foreign currency received under an F/X swap in interest-bearing instruments.

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.

Foreign currency swaps and warehousing agreements are revalued daily at current market exchange rates. Activity related to these agreements, with the exception of the unrealized gains and losses resulting from the daily revaluation, 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. Unrealized gains and losses resulting from the daily revaluation are allocated to FRBNY and not to the other Reserve Banks.

f. 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 estimated useful lives of assets ranging from two to fifty years. Major alterations, renovations, and improvements are capitalized at cost as additions to the asset accounts and are amortized over the remaining useful life of the asset. Maintenance, repairs, and minor replacements are charged to operating expense in the year incurred. Capitalized assets including software, building, leasehold improvements, furniture, and equipment are impaired when it is determined that the net realizable value is significantly less than book value and is not recoverable.

Costs incurred for software, either developed internally or acquired for internal use, during the application development stage are capitalized based on the cost of direct services and materials associated with designing, coding, installing, or testing 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.

g. Interdistrict Settlement Account

At the close of business each day, each Reserve Bank assembles the payments due to or from other Reserve Banks as a result of the day's transactions that involve depository institution accounts held by other Districts. Such transactions may include funds settlement, check clearing, and ACH operations. The cumulative net amount due to or from the other Reserve Banks is reflected in the "Interdistrict settlement account" in the Statements of Condition.

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) to the Reserve Banks upon deposit with such agents of certain 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 equal to the sum of the notes applied for by such Reserve Bank.

Assets eligible to be pledged as collateral security include all Bank assets. The collateral value is equal to the book value of the collateral tendered, with the exception of securities, whose 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 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 of 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, as obligations of the United States, Federal Reserve notes are backed by the full faith and credit of the United States government.

The "Federal Reserve notes outstanding, net" account represents the Bank's Federal Reserve notes outstanding, reduced by the currency issued to the Bank but not in circulation, of $5,016 million, and $4,497 million at December 31, 2005 and 2004, respectively.

i. Items in Process of Collection and Deferred Credit Items

The balance in the "Items in process of collection" line in the Statements of Condition primarily represents amounts attributable to checks that have been deposited for collection by the payee depository institution and, as of the balance sheet date, have not yet been collected from the payor depository institution. 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 fluctuate and vary significantly from day to day.

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. By law, each 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. A member bank is liable for Reserve Bank liabilities up to twice the par value of stock subscribed by it.

k. Surplus

The Board of Governors requires Reserve Banks to maintain a surplus equal to the amount of capital paid-in as of December 31. This amount is intended to provide additional capital and reduce the possibility that the Reserve Banks would be required to call on member banks for additional capital. Pursuant to Section 16 of the Federal Reserve Act, Reserve Banks are required by the Board of Governors to transfer to the U.S. Treasury as interest on Federal Reserve notes excess earnings, after providing for the costs of operations, payment of dividends, and reservation of an amount necessary to equate surplus with capital paid-in.

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. Weekly payments to the U.S. Treasury may vary significantly.

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. This amount is reported as a component of "Payments to U.S. Treasury as interest on Federal Reserve notes."

l. 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 is permitted, but not required, to pay for these services.

m. 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. The Board of Governors also assesses each Reserve Bank for the expenses incurred for the U.S. Treasury to issue 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 previous year.

n. Taxes

The Reserve Banks are exempt from federal, state, and local taxes, except for taxes on real property. The Bank's real property taxes were $1 million for each of the years ended December 31, 2005 and 2004, and are reported as a component of "Occupancy expense."

o. Restructuring Charges

In 2003, the System began the restructuring of several operations, primarily check, cash, and U.S. Treasury services. The restructuring included streamlining the management and support structures, reducing staff, decreasing the number of processing locations, and increasing processing capacity in the remaining locations. These restructuring activities continued in 2004 and 2005.

Footnote 10 describes the restructuring and provides information about the Bank's costs and liabilities associated with employee separations and contract terminations. The costs associated with the write-down of certain Bank assets are discussed in footnote 6. Costs and liabilities associated with enhanced pension benefits in connection with the restructuring activities for all Reserve Banks are recorded on the books of the FRBNY and those associated with enhanced postretirement benefits are discussed in footnote 9.

4. U.S. GOVERNMENT SECURITIES, 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 2.828 percent and 2.628 percent at December 31, 2005 and 2004, respectively.

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

	2005	2004
Par value:		
U.S. government:		
Bills	$ 7,673	$ 6,910
Notes	10,751	9,482
Bonds	2,626	2,471
Total par value	21,050	18,863
Unamortized premiums	249	247
Unaccreted discounts	(80)	(43)
Total allocated to Bank	$ 21,219	$ 19,067

The total of the U.S. government securities, net held in the SOMA was $750,202 million and $725,584 million at December 31, 2005 and 2004, respectively.

At December 31, 2005 and 2004, the total contract amount of securities sold under agreements to repurchase was $30,505 million and $30,783 million, respectively, of which $863 million and $809 million, were allocated to the Bank. The total par value of the SOMA securities pledged for securities sold under agreements to repurchase at December 31, 2005 and 2004 was $30,559 million and $30,808 million, respectively, of which $864 million and $810 million was allocated to the Bank.

The maturity distribution of U.S. government securities bought outright and securities sold under agreements to repurchase, that were allocated to the Bank at December 31, 2005, was as follows (in millions):

Maturities of Securities Held	U.S. Government Securities (Par value)	Securities Sold Under Agreements to Repurchase (Contract amount)
Within 15 days	$ 1,160	$ 863
16 days to 90 days	4,872	-
91 days to 1 year	5,269	-
Over 1 year to 5 years	5,961	-
Over 5 years to 10 years	1,604	-
Over 10 years	2,184	-
Total	$ 21,050	$ 863

At December 31, 2005 and 2004, U.S. government securities with par values of $3,776 million and $6,609 million, respectively, were loaned from the SOMA, of which $107 million and $174 million, respectively, were allocated to the Bank.

5. INVESTMENTS DENOMINATED IN FOREIGN CURRENCIES

The FRBNY, on behalf of the Reserve Banks, holds foreign currency deposits with foreign central banks and the Bank for International Settlements and invests in foreign government debt instruments. Foreign government debt instruments held include both securities bought outright and securities purchased under agreements to resell. These investments are guaranteed as to principal and interest by the foreign governments.

The Bank's allocated share of investments denominated in foreign currencies was approximately 1.300 percent and 1.835 percent at December 31, 2005 and 2004, respectively.

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

	2005	2004
European Union Euro:		
Foreign currency deposits	$ 71	$ 112
Securities purchased under agreements to resell	25	39
Government debt instruments	46	72
Japanese Yen:		
Foreign currency deposits	34	28
Government debt instruments	70	141
Total	$ 246	$ 392

Total System investments denominated in foreign currencies were $18,928 million and $21,368 million at December 31, 2005 and 2004, respectively.

The maturity distribution of investments denominated in foreign currencies which were allocated to the Bank at December 31, 2005, was as follows (in millions):

Maturities of Investments Denominated in Foreign Currencies	European Euro	Japanese Yen	Total
Within 15 days	$ 44	$ 34	$ 78
16 days to 90 days	34	9	43
91 days to 1 year	27	13	40
Over 1 year to 5 years	37	48	85
Over 5 years to 10 years	–	–	–
Over 10 years	–	–	–
Total	$ 142	$ 104	$ 246

At December 31, 2005 and 2004, there were no open foreign exchange contracts.

At December 31, 2005 and 2004, the warehousing facility was $5,000 million, with no balance outstanding.

6. BANK PREMISES, EQUIPMENT, AND SOFTWARE

A summary of bank premises and equipment at December 31 is as follows (in millions):

	Useful Life Range (in years)	2005	2004
Bank premises and equipment:			
Land	N/A	$ 40	$ 41
Buildings	1 to 30	29	53
Building machinery and equipment	1 to 16	10	19
Construction in progress	N/A	27	9
Furniture and equipment	1 to 10	56	65
Subtotal		$ 162	$ 187
Accumulated depreciation		(61)	(85)
Bank premises and equipment, net		$ 101	$ 102
Depreciation expense, for the years ended		$ 7	$ 8

The Bank is constructing a new building to replace the head office in Kansas City. Approximately $29 million of costs associated with the acquisition of land and site preparation for the new building are included in Land, and approximately $27 million of costs associated with the construction of the new building are included in Construction in progress.

In July 2005, the Bank completed the sale and leaseback of its head office in Kansas City. The Bank will lease the space from the purchaser until the new building is completed in 2008.

The Bank leases space to outside tenants with lease terms ranging from one to three years. Rental income from such leases was not material for the years ended December 31, 2005 and 2004. Future minimum lease payments under noncancelable agreements in existence at December 31, 2005 were not material.

The Bank has capitalized software assets, net of amortization, of $2 million and $3 million at December 31, 2005 and 2004, respectively. Amortization expense was $1 million for each of the years ended December 31, 2005 and 2004. Capitalized software assets are reported as a component of "Other assets" and related amortization is reported as a component of "Other expenses."

Assets impaired as a result of the Bank's restructuring plan, as discussed in footnote 10, include software, building, leasehold improvements, furniture, and equipment. Asset impairment losses of $5 million and $1 million for the periods ended December 31, 2005 and 2004, respectively, were determined using fair values based on quoted market values or other valuation techniques and are reported as a component of "Other expenses."

7. COMMITMENTS AND CONTINGENCIES

At December 31, 2005, the Bank was obligated under noncancelable leases for premises and equipment with terms ranging from one to approximately three years. These leases provide for increased rental payments based upon increases in real estate taxes, operating costs, or selected price indices.

Rental expense under operating leases for certain operating facilities, warehouses, and data processing and office equipment (including taxes, insurance and maintenance when included in rent), net of sublease rentals, was $3 million and $2 million for the years ended December 31, 2005 and 2004, respectively. Certain of the Bank's leases have options to renew.

Future minimum rental payments under noncancelable operating leases, net of sublease rentals, with terms of one year or more, at December 31, 2005, were (in thousands):

2006	$ 2,396
2007	2,346
2008	962
2009	–
2010	–
Thereafter	–
	$ 5,704

At December 31, 2005, there were no other material commitments and long-term obligations in excess of one year.

Under the Insurance Agreement of the Federal Reserve Banks, each Reserve Bank 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 that a Reserve Bank's capital paid-in bears 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 such agreement at December 31, 2005 or 2004.

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.

8. RETIREMENT AND THRIFT PLANS

Retirement Plans

The Bank currently offers three defined benefit retirement plans to its employees, based on length of service and level of compensation. Substantially all of the 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 Bank officers participate in the Supplemental Employee Retirement Plan ("SERP").

The System Plan is a multi-employer plan with contributions fully funded by participating employers. Participating employers are the Federal Reserve Banks, the Board of Governors of the Federal Reserve System, and the Office of Employee Benefits of the Federal Reserve System. No separate accounting is maintained of assets contributed by the participating employers. The FRBNY acts as a sponsor of the System Plan and the costs associated with the Plan are not redistributed to other participating employers. The Bank's benefit obligation and net pension costs for the BEP and the SERP at December 31, 2005 and 2004, and for the years then ended, are 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's Thrift Plan contributions totaled $4 million for each of the years ended December 31, 2005 and 2004, and are reported as a component of "Salaries and other benefits." The Bank matches employee contributions based on a specified formula. For the years ended December 31, 2005 and 2004, 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.

9. 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 beginning and ending balances of the benefit obligation (in millions):

	2005	2004
Accumulated postretirement benefit obligation at January 1	$ 24.9	$ 28.7
Service cost-benefits earned during the period	0.9	0.7
Interest cost of accumulated benefit obligation	1.9	1.6
Actuarial loss	13.6	1.7
Curtailment gain	–	(0.1)
Contributions by plan participants	0.8	0.9
Benefits paid	(3.3)	(3.0)
Plan amendments	–	(5.6)
Accumulated postretirement benefit obligation at December 31	$ 38.8	$ 24.9

At December 31, 2005 and 2004, the weighted-average discount rate assumptions used in developing the postretirement benefit obligation were 5.50 percent and 5.75 percent, respectively.

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

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):

	2005	2004
Fair value of plan assets at January 1	$ –	$ –
Actual return on plan assets	–	–
Contributions by the employer	2.5	2.1
Contributions by plan participants	0.8	0.9
Benefits paid	(3.3)	(3.0)
Fair value of plan assets at December 31	$ –	$ –
Unfunded postretirement benefit obligation	$ 38.8	$ 24.9
Unrecognized net curtailment gain	–	1.0
Unrecognized prior service cost	7.6	9.1
Unrecognized net actuarial loss	(13.8)	(0.9)
Accrued postretirement benefit costs	$ 32.6	$ 34.1

Accrued postretirement benefit costs are reported as a component of "Accrued benefit costs."

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

	2005	2004
Health care cost trend rate assumed for next year	9.00%	9.00%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.00%	4.75%
Year that the rate reaches the ultimate trend rate	2011	2011

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, 2005 (in thousands):

	One Percentage Point Increase	One Percentage Point Decrease
Effect on aggregate of service and interest cost components of net periodic postretirement benefit costs	$ (10)	$ (12)
Effect on accumulated postretirement benefit obligation	$ (271)	$ 54

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

	2005	2004
Service cost-benefits earned during the period	$ 0.9	$ 0.7
Interest cost of accumulated benefit obligation	1.9	1.6
Amortization of prior service cost	(1.5)	(2.0)
Recognized net actuarial loss	0.7	–
Total periodic expense	$ 2.0	$ 0.3
Curtailment gain	(1.0)	(9.0)
Net periodic postretirement benefit costs (credit)	$ 1.0	$ (8.7)

Net postretirement benefit costs are actuarially determined using a January 1 measurement date. At January 1, 2005 and 2004, the weighted-average discount rate assumptions used to determine net periodic postretirement benefit costs were 5.75 percent and 6.25 percent, respectively.

Net periodic postretirement benefit costs are reported as a component of "Salaries and other benefits."

A plan amendment that modified the credited service period eligibility requirements created curtailment gains. The curtailment gain associated with restructuring programs announced in 2003 was recognized when employees left the Bank in 2004. The curtailment gain associated with restructuring programs announced in 2004 that are described in footnote 10 will be offset by unrecognized actuarial losses and prior service gains. As a result, an unrecognized net curtailment gain was recorded in 2005 when the affected employees terminated 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 by 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, retroactive to January 1, 2004, are reflected in actuarial loss in the accumulated postretirement benefit obligation and net periodic postretirement benefit costs.

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

	Without Subsidy	With Subsidy
2006	$ 2.7	$ 2.4
2007	2.8	2.5
2008	2.9	2.5
2009	3.0	2.6
2010	3.1	2.7
2011-2015	17.1	14.6
Total	$ 31.6	$ 27.3

Postemployment Benefits

The Bank offers benefits to former or inactive employees. Postemployment benefit costs are actuarially determined using a December 31, 2005 measurement date and include the cost of medical and dental insurance, survivor income, and disability benefits. The accrued postemployment benefit costs recognized by the Bank were $6 million for each of the years ended December 31, 2005 and 2004. This cost is included as a component of "Accrued benefit costs." Net periodic postemployment benefit costs included in 2005 and 2004 operating expenses were $1 million for both years and are recorded as a component of "Salaries and other benefits."

10. BUSINESS RESTRUCTURING CHARGES

In 2003, the Bank announced plans for restructuring to streamline operations and reduce costs, including consolidation of check operations and staff reductions in various functions of the Bank. In 2004 and 2005, additional consolidation and restructuring initiatives were announced in the check, savings bonds, and cash operations and various other functions of the Bank. These actions resulted in the following business restructuring charges (in millions):

	Total Estimated Costs	Accrued Liability 12/31/2004	Total Charges	Total Paid	Accrued Liability 12/31/2005
Employee separation	$ 5	$ 3	$ 2	$ 2	$ 3

Employee separation costs are primarily severance costs related to staff reductions of approximately 161, including 85 and 76 staff reductions related to restructuring announced in 2005 and 2004, respectively. These costs are reported as a component of "Salaries and other benefits."

Restructuring costs associated with the write-downs of certain Bank assets, including software, buildings, leasehold improvements, furniture, and equipment are discussed in footnote 6. Costs associated with enhanced pension benefits for all Reserve Banks are recorded on the books of the FRBNY as discussed in footnote 8. Costs associated with enhanced postretirement benefits are disclosed in footnote 9.

Future costs associated with the restructuring that are not estimable and are not recognized as liabilities will be incurred in 2006.

The Bank anticipates substantially completing its announced plans by 2006.

VOLUME OF PRINCIPAL OPERATIONS (UNAUDITED)

	2005	2004
Loans and Discounts, Daily Average	$ 17,263,000	$ 15,611,000
Number of Institutions Borrowing	75	75
Commercial Checks	$ 1,165,527,000,000	$ 1,066,725,000,000
Commercial Checks Collected	1,182,161,000	1,249,263,000
Currency Receipts and Payments	$ 57,636,344,000	$ 57,217,763,000
Pieces	3,663,851,000	3,692,199,000
Coin Receipts and Payments	$ 165,361,000	$ 112,831,000
Bags	313,000	223,000
Issues and Redemption of U.S. Government Securities	$ 314,303,266,000	$ 266,797,294,000
Funds Transfer	$ 83,231,378,000,000	$87,841,830,000,000
Number of Transfers	50,847,000	48,873,000

Volume of Principal Operations numbers were not included in PricewaterhouseCoopers' audit.

Statement of Auditor Independence

The firm engaged by the Board of Governors for the audits of the individual and combined financial statements of the Reserve Banks for 2005 was PricewaterhouseCoopers LLP (PwC). Fees for these services totaled $ 4.6 million. To ensure auditor independence, the Board of Governors requires that PwC be independent in all matters relating to the audit. Specifically, PwC may not perform services for the Reserve Banks or others that would place it in a position of auditing its own work, making management decisions on behalf of the Reserve Banks, or in any other way impairing its audit independence. In 2005, the Bank did not engage PwC for any material advisory services.