

	DOLLAR AMOUNT		NUMBER OF ITEMS	
	2001	2000	2001	2000
CHECK & ELECTRONIC PAYMENTS				
Checks, NOWs, & Share Drafts Processed	1.5 Trillion	1.7 Trillion	2.3 Billion	2.3 Billion
Fine Sort & Packaged Checks Handled	16.8 Billion	21.1 Billion	29.9 Million	40.0 Million
U.S. Government Checks Processed	42.4 Billion	37.5 Billion	43.8 Million	35.9 Million
Automated Clearing House (ACH)				
Items Processed	2.6 Trillion	2.5 Trillion	920.5 Million	869.8 Million
Transfer of Funds	64.9 Trillion	57.0 Trillion	22.3 Million	20.7 Million
CASH OPERATIONS				
Currency Received and Counted	52.9 Billion	51.0 Billion	3.2 Billion	3.1 Billion
Unfit Currency Destroyed	7.3 Billion	9.5 Billion	639.8 Million	731.3 Million
Coin Bags Received and Processed	1.6 Billion	1.3 Billion	2.8 Million	3.5 Million
SECURITIES SERVICES FOR DEPOSITORY INSTITUTIONS				
<i>Safekeeping Balance December 31:</i>				
Definitive Securities	135.9 Billion	124.5 Billion	5.4 Thousand	6.4 Thousand
Book Entry Securities	284.6 Billion	277.9 Billion	—	—
Purchase & Sale	1.3 Billion	1.6 Billion	2.5 Thousand	5.2 Thousand
Book Entry Government Securities	4.1 Trillion	3.8 Trillion	837.8 Thousand	709.0 Thousand
LOANS TO DEPOSITORY INSTITUTIONS				
Total Loans Made During Year	15.6 Billion	7.9 Billion	0.7 Thousand	2.1 Thousand
SERVICES TO U.S. TREASURY AND GOVERNMENT AGENCIES				
Food Stamps Redeemed	364.2 Million	640.2 Million	76.4 Million	127.4 Million
Sell Direct Transactions Processed	683.0 Million	655.8 Million	15.0 Thousand	16.4 Thousand

FEDERAL RESERVE BANK OF CHICAGO

MANAGEMENT ASSERTION

FEBRUARY 2002

TO THE BOARD OF DIRECTORS OF THE FEDERAL RESERVE BANK OF CHICAGO

The management of the Federal Reserve Bank of Chicago (FRBC) 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, 2001 (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, and as such, include amounts, some of which are based on judgments and estimates of management.

The management of the FRBC 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.

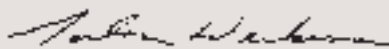
Even an effective process of internal controls, no matter how well designed, has inherent limitations, including the possibility of human error, and therefore can provide only reasonable assurance with respect to the preparation of reliable Financial Statements.

The management of the FRBC 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, the management of the FRBC believes that the FRBC maintained an effective process of internal controls over financial reporting including the safeguarding of assets as they relate to the Financial Statements.

FEDERAL RESERVE BANK OF CHICAGO



MICHAEL MOSKOW
PRESIDENT
AND CHIEF EXECUTIVE OFFICER



GORDON WERKEMA
FIRST VICE PRESIDENT
AND CHIEF OPERATING OFFICER


PricewaterhouseCoopers LLP

One North Wacker
Chicago, IL 60606
Telephone (312) 298-2000

REPORT OF INDEPENDENT ACCOUNTANTS
TO THE BOARD OF DIRECTORS OF THE FEDERAL RESERVE BANK OF CHICAGO

We have examined management's assertion that the Federal Reserve Bank of Chicago ("FRBC") maintained effective internal control over financial reporting and the safeguarding of assets as they relate to the Financial Statements as of December 31, 2001, included in the accompanying Management's Assertion. The assertion is the responsibility of FRBC's management. Our responsibility is to express an opinion on the assertions based on our examination.

Our examination was made in accordance with standards established by the American Institute of Certified Public Accountants, and accordingly, included obtaining an understanding of the internal control over financial reporting, testing, and evaluating the design and operating effectiveness of the internal control, and 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 the 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 the FRBC maintained effective internal control over financial reporting and over the safeguarding of assets as they relate to the Financial Statements as of December 31, 2001, is fairly stated, in all material respects, based upon criteria described in "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission.

MARCH 4, 2002

**PricewaterhouseCoopers LLP**

One North Wacker
 Chicago, IL 60606
 Telephone (312) 298-2000

REPORT OF INDEPENDENT ACCOUNTANTS

**TO THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM AND
 THE BOARD OF DIRECTORS OF THE FEDERAL RESERVE BANK OF CHICAGO**

We have audited the accompanying statements of condition of The Federal Reserve Bank of Chicago (the "Bank") as of December 31, 2001 and 2000, and the related statements of income and changes in capital for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on the 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 discussed in Note 3, the 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, 2001 and 2000, and results of its operations for the years then ended, on the basis of accounting described in Note 3.

MARCH 4, 2002
 CHICAGO, ILLINOIS

STATEMENTS OF CONDITION (in Millions)

<i>As of December 31,</i>	2001	2000
ASSETS		
Gold Certificates	\$ 1,028	\$ 1,064
Special Drawing Rights Certificates	212	212
Coin	117	114
Items in Process of Collection	526	1,119
Loans to Depository Institutions	15	25
U.S. Government and Federal Agency Securities, Net	63,617	62,020
Investments Denominated in Foreign Currencies	1,333	1,409
Accrued Interest Receivable	646	722
Interdistrict Settlement Account	6,071	—
Bank Premises and Equipment, Net	136	135
Other Assets	48	37
Total Assets	\$ 73,749	\$ 66,857
LIABILITIES AND CAPITAL		
<i>Liabilities:</i>		
Federal Reserve Notes Outstanding, Net	\$ 68,119	\$ 61,206
Deposits		
Depository Institutions	3,498	2,796
Other Deposits	4	4
Deferred Credit Items	386	575
Interest on Federal Reserve Notes Due U.S. Treasury	43	132
Interdistrict Settlement Account	—	770
Accrued Benefit Cost	88	85
Other Liabilities	25	25
Total Liabilities	\$ 72,163	\$ 65,593
<i>Capital:</i>		
Capital Paid-In	793	632
Surplus	793	632
Total Capital	\$ 1,586	\$ 1,264
Total Liabilities and Capital	\$ 73,749	\$ 66,857

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

STATEMENTS OF INCOME (in Millions)

For the years ended December 31,

	2001	2000
INTEREST INCOME		
Interest on U.S. Government and Federal Agency Securities	\$ 3,403	\$ 3,545
Interest on Investments Denominated in Foreign Currencies	30	24
Interest on Loans to Depository Institutions	2	6
Total Interest Income	\$ 3,435	3,575
OTHER OPERATING INCOME (LOSS)		
Income From Services	\$ 110	\$ 98
Reimbursable Services to Government Agencies	11	20
Foreign Currency Losses, Net	(131)	(127)
U.S. Government Securities Gains (Losses), Net	36	(9)
Other Income	13	9
Total Other Operating Income (Loss)	\$ 39	\$ (9)
OPERATING EXPENSES		
Salaries and Other Benefits	\$ 157	\$ 141
Occupancy Expense	20	19
Equipment Expense	21	19
Cost of Unreimbursed Treasury Services	—	1
Assessments by Board of Governors	65	66
Other Expenses	80	101
Total Operating Expenses	\$ 343	\$ 347
Net Income Prior to Distribution	\$ 3,131	\$ 3,219
DISTRIBUTION OF NET INCOME		
Dividends Paid to Member Banks	\$ 43	\$ 36
Transferred to Surplus	162	391
Payments to U.S. Treasury as Interest on Federal Reserve Notes	2,926	2,792
Total Distribution	\$ 3,131	\$ 3,219

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

STATEMENTS OF CHANGES IN CAPITAL (in Millions)			
<i>For the years ended December 31, 2001 and December 31, 2000</i>	CAPITAL PAID-IN	SURPLUS	TOTAL CAPITAL
Balance at January 1, 2000 (11.6 Million Shares)	\$ 578	\$ 578	\$ 1,156
Net Income Transferred to Surplus	–	391	391
Surplus Transfer to the U.S. Treasury	–	(337)	(337)
Net Change in Capital Stock Issued (1.0 Million Shares)	54	–	54
Balance at December 31, 2000 (12.6 Million Shares)	\$ 632	\$ 632	\$ 1,264
Net Income Transferred to Surplus	–	161	161
Net Change in Capital Stock Issued (3.2 Million Shares)	161	–	161
Balance at December 31, 2001 (15.9 Million Shares)	\$ 793	\$ 793	\$ 1,586

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

1. ORGANIZATION

The Federal Reserve Bank of Chicago (“Bank”) is part of the Federal Reserve System (“System”) created by Congress under the Federal Reserve Act of 1913 (“Federal Reserve Act”) which established the central bank of the United States. The System consists of the Board of Governors of the Federal Reserve System (“Board of Governors”) and twelve Federal Reserve Banks (“Reserve Banks”). The Reserve Banks are chartered by the federal government and possess a unique set of governmental, corporate, and central bank characteristics. Other major elements of the System are the Federal Open Market Committee (“FOMC”) and the Federal Advisory Council. 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.

Structure

The Bank and its branch in Detroit, Michigan, serve the Seventh Federal Reserve District, which includes Iowa and portions of Michigan, Illinois, Wisconsin and Indiana. In accordance with the Federal Reserve Act, supervision and control of the Bank is exercised by a Board of Directors. Banks that are members of the System include all national banks and any state chartered bank that applies and is approved for membership in the System.

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. Of the six elected by member banks, three represent the public and three represent member banks. 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.

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 mechanism, including large-dollar transfers of funds, automated clearinghouse (“ACH”) operations and check processing; distributing of 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, and state member banks; and administering other regulations of the

Board of Governors. The Board of Governors’ operating costs are funded through assessments on the Reserve Banks.

The FOMC establishes policy regarding open market operations, oversees these operations, and issues authorizations and directives to the FRBNY for its execution of transactions. Authorized transaction types include direct purchase and sale of securities, matched sale-purchase transactions, the purchase of securities under agreements to resell, and the lending of U.S. government securities. The FRBNY is also authorized by the FOMC to hold balances of and to execute spot and forward foreign exchange and securities contracts in nine foreign currencies, maintain reciprocal currency arrangements (“F/X swaps”) with various central banks, and “warehouse” foreign currencies for the U.S. Treasury and Exchange Stabilization Fund (“ESF”) through the Reserve Banks.

3. SIGNIFICANT ACCOUNTING POLICIES

Accounting principles for entities with the unique powers and responsibilities of the nation’s central bank have not been formulated by the Financial Accounting Standards Board. 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 to 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.

The financial statements have been prepared in accordance with the Financial Accounting Manual. Differences exist between the accounting principles and practices of the System and accounting principles generally accepted in the United States of America (“GAAP”). The primary differences are the presentation of all security holdings at amortized cost, rather than at the fair value presentation requirements of GAAP, and the accounting for matched sale-purchase transactions as separate sales and purchases, rather than secured borrowings with pledged collateral, as is generally required by GAAP. In addition, the Bank has elected not to present a Statement of Cash Flows. The Statement of Cash Flows has not been included as the liquidity and cash position of the Bank are not of primary concern to the users of these financial statements. Other information regarding the Bank’s activities is provided in, or may be derived from, the Statements of Condition, Income, and Changes in Capital. Therefore, a Statement of Cash Flows would not provide any additional useful information. There are no other significant differences between the policies outlined in the Financial Accounting Manual and GAAP.

Effective January 2001, the System implemented procedures to eliminate the sharing of costs by Reserve Banks for certain services a Reserve Bank may provide on behalf of the System. Data for 2001 reflects the adoption of this policy. Major services provided for the

System by this bank, for which the costs will not be redistributed to the other Reserve Banks, include national business development and customer support.

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 and 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 Certificates

The Secretary of the Treasury is authorized to issue gold certificates to the Reserve Banks to monetize gold held by the U.S. Treasury. 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 upon Federal Reserve notes outstanding in each District.

B. Special Drawing Rights Certificates

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 SDRs, at the direction of the U.S. Treasury, for the purpose of financing SDR certificate acquisitions or for financing exchange stabilization operations. At the time SDR transactions occur, the Board of Governors allocates amounts 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 2001.

C. Loans to Depository Institutions

The Depository Institutions Deregulation and Monetary Control Act of 1980 provides that all depository institutions that maintain reservable transaction accounts or nonpersonal time deposits, as defined in Regulation D issued by the Board

of Governors, have borrowing privileges at the discretion of the Reserve Banks. 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 any loans were 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 Banks, subject to review by the Board of Governors. Reserve Banks retain the option to impose a surcharge above the basic rate in certain circumstances.

D. U.S. Government and Federal Agency Securities and Investments Denominated in Foreign Currencies

The FOMC has designated the FRBNY to execute open market transactions on its behalf and to hold the resulting securities 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 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. Such authorizations are reviewed and approved annually by the FOMC.

Matched sale-purchase transactions are accounted for as separate sale and purchase transactions. Matched sale-purchase transactions are transactions in which the FRBNY sells a security and

buys it back at the rate specified at the commencement of the transaction.

The FRBNY has sole authorization by the FOMC to lend U.S. government securities held in the SOMA to U.S. government securities dealers and to banks participating in U.S. government securities clearing arrangements on behalf of the system, in order to facilitate the effective functioning of the domestic securities market. These securities-lending transactions are fully collateralized by other U.S. government securities. FOMC policy requires FRBNY to take possession of collateral in excess of the market values of the securities loaned. The market values of the collateral and the securities loaned are monitored by FRBNY on a daily basis, with additional collateral obtained as necessary. The securities loaned continue to be accounted for in the SOMA.

Foreign exchange (“F/X”) contracts are contractual agreements between two parties to exchange specified currencies, at a specified price, on a specified date. Spot foreign contracts normally settle two days after the trade date, whereas the settlement date on forward contracts is negotiated between the contracting parties, but will extend beyond two days from the trade date. The FRBNY generally enters into spot contracts, with any forward contracts generally limited to the second leg of a swap/warehousing transaction.

The FRBNY, on behalf of the Reserve Banks, maintains renewable, short-term F/X swap arrangements with two authorized foreign central banks. 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 foreign currencies that it may need for intervention operations to support the dollar and give the partner foreign central bank temporary access to dollars it may need to support its own currency. Drawings under the F/X swap arrangements can be initiated by either the FRBNY or the partner foreign central bank, and must be agreed to by the drawee. The F/X swaps are structured so that the party initiating the transaction (the drawer) bears the exchange rate risk upon maturity. The 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 Treasury, U.S. dollars for foreign currencies held by the Treasury or ESF over a limited period of time. The purpose of the warehousing facility is to supplement the U.S. dollar resources of the Treasury and ESF for financing purchases of foreign currencies and related international operations.

In connection with its foreign currency activities, the FRBNY, on behalf of the Reserve Banks, may enter into contracts which contain varying degrees of off-balance sheet market risk, because they represent contractual commitments involving future settlement and counterparty credit risk. The FRBNY controls credit risk by obtaining credit approvals, establishing transaction limits, and performing daily monitoring procedures.

While the application of current market prices to the securities currently held in the SOMA portfolio and investments denominated in foreign currencies 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 Reserve Bank earnings or capital. Both the domestic and foreign components of the SOMA portfolio from time to time involve transactions that can result in gains or losses when holdings are sold prior to maturity. However, decisions regarding the securities and foreign currencies transactions, including their purchase and sale, are motivated by monetary policy objectives rather than profit. Accordingly, earnings and any gains or losses resulting from the sale of such currencies and securities are incidental to the open market operations and do not motivate its activities or policy decisions.

U.S. government and federal agency 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 and is reported as “Interest on U.S. government and federal agency securities” or “Interest on investments denominated in foreign currencies,” as appropriate. Income earned on securities lending transactions is reported as a component of “Other income.” Gains and losses resulting from sales of securities are determined by specific issues based on average cost. Gains and losses on the sales of U.S.

government and federal agency securities are reported as “U.S. government securities gains (losses), net.” Foreign-currency-denominated assets are revalued daily at current 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 losses, net.” Foreign currencies held through F/X swaps, when initiated by the counter-party, and warehousing arrangements are revalued daily, with the unrealized gain or loss reported by the FRBNY as a component of “Other assets” or “Other liabilities,” as appropriate.

Balances of U.S. government and federal agencies securities bought outright, securities loaned, investments denominated in foreign currency, interest income, securities lending fee income, amortization of premiums and discounts on securities bought outright, gains and losses on sales of securities, and realized and unrealized gains and losses on investments denominated in foreign currencies, excluding those held under an F/X swap arrangement, are allocated to each Reserve Bank. Securities purchased under agreements to resell and unrealized gains and losses on the revaluation of foreign currency holdings under F/X swaps and warehousing arrangements are allocated to the FRBNY and not to other Reserve Banks.

Statement of Financial Accounting Standards No. 133, as amended and interpreted, became effective on January 1, 2001. For the periods presented, the Reserve Banks had no derivative instruments required to be accounted for under the standard.

E. Bank Premises and Equipment

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 2 to 50 years. New assets, major alterations, renovations and improvements are capitalized at cost as additions to the asset accounts. Maintenance, repairs and minor replacements are charged to operations in the year incurred. Internally developed software is capitalized based on the cost of direct materials and services and those indirect costs associated with developing, implementing, or testing software.

F. Interdistrict Settlement Account

At the close of business each day, all Reserve Banks and branches assemble the payments due to or from other Reserve Banks and branches as a result of transactions involving accounts residing in other Districts that occurred during the day's operations. Such transactions may include funds settlement, check clearing and ACH operations, and allocations of shared expenses. The cumulative net amount due to or from other Reserve Banks is reported as the “Interdistrict settlement account.”

G. Federal Reserve Notes

Federal Reserve notes are the circulating currency of the United States. These notes are issued through the various Federal Reserve agents 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. In accordance with the Federal Reserve Act, gold certificates, special drawing rights certificates, U.S. government and federal agency securities, triparty agreements, loans to depository institutions, and investments denominated in foreign currencies are pledged as collateral for net Federal Reserve notes outstanding. 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 Board of Governors may, at any time, call upon a Reserve Bank for additional security to adequately collateralize the Federal Reserve notes. The Reserve Banks have entered into an agreement which provides for certain assets of the Reserve Banks to be jointly pledged as collateral for the Federal Reserve notes of all Reserve Banks in order to satisfy their obligation of providing sufficient collateral for outstanding Federal Reserve notes. 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 Federal Reserve notes reduced by currency held in the vaults of the Bank of \$6,424 million, and \$9,479 million at December 31, 2001 and 2000, respectively.

H. 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. As a member bank’s capital and surplus changes, its holdings of the Reserve Bank’s stock must be adjusted. Member banks are those state-chartered banks that apply and are approved for membership in the System and all national banks. Currently, only one-half of the subscription is paid-in and the remainder is subject to call. These shares are nonvoting with a par value of \$100. They may not be transferred or hypothecated. By law, each member bank is entitled to receive 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.

I. 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. Reserve Banks are required by the Board of Governors to transfer to the U.S. Treasury 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.

The Consolidated Appropriations Act of 2000 (Public Law 106-113, Section 302) directed the Reserve Banks to transfer

to the U.S. Treasury additional surplus funds of \$3,752 million during the Federal Government’s 2000 fiscal year. Federal Reserve Bank of Chicago transferred \$337 million to the U.S. Treasury. Reserve Banks were not permitted to replenish the surplus for these amounts during fiscal year 2000, which ended September 30, 2000; however, the surplus was replenished by December 31, 2000.

In the event of losses or a substantial increase in capital, payments to the U.S. Treasury are suspended until such losses are recovered through subsequent earnings. Weekly payments to the U.S. Treasury may vary significantly.

J. Income and Costs related to 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. The costs of providing fiscal agency and depository services to the Treasury Department that have been billed but not paid are immaterial and included in “Other expenses.”

K. Taxes

The Reserve Banks are exempt from federal, state, and local taxes, except for taxes on real property, which are reported as a component of “Occupancy expense.”

4. U.S. GOVERNMENT AND FEDERAL AGENCY SECURITIES

Securities bought outright are held in the SOMA at the FRBNY. An undivided interest in SOMA activity, with the exception of securities held under agreements to resell and the related premiums, discounts and income, is allocated to each Reserve Bank on a percentage basis derived from an annual settlement of interdistrict clearings. The settlement, performed in April of each year, equalizes Reserve Bank gold certificate holdings to Federal Reserve notes outstanding. The Bank's allocated share of SOMA balances was approximately 11.326 percent and 11.961 percent at December 31, 2001 and 2000, respectively.

The Bank's allocated share of securities held in the SOMA at December 31, that were bought outright, were as follows (in millions):

	2001	2000
PAR VALUE		
Federal Agency	\$ 1	\$ 16
<i>U.S. Government:</i>		
Bills	20,621	21,380
Notes	30,120	28,729
Bonds	11,740	11,098
Total Par Value	\$ 62,482	\$ 61,223
Unamortized Premiums	1,280	1,164
Unaccreted Discounts	(145)	(367)
Total Allocated to Bank	\$ 63,617	\$ 62,020

Total SOMA securities bought outright were \$561,701 million and \$518,501 million at December 31, 2001 and 2000, respectively.

The maturity distribution of U.S. government and federal agency securities bought outright, which were allocated to the Bank at December 31, 2001, were as follows (in millions):

<i>Maturities of Securities Held</i>	PAR VALUE		
	<i>U.S. Govt. Securities</i>	<i>Federal Agency Obligations</i>	<i>Total</i>
Within 15 Days	\$ 1,210	–	\$ 1,210
16 Days to 90 Days	14,106	–	14,106
91 Days to 1 Year	14,795	–	14,795
Over 1 Year to 5 Years	17,346	\$ 1	17,347
Over 5 Years to 10 Years	6,041	–	6,041
Over 10 Years	8,983	–	8,983
Total	\$62,481	\$ 1	\$ 62,482

At December 31, 2001, and 2000, matched sale-purchase transactions involving U.S. government securities with par values of \$23,188 million and \$21,112 million, respectively, were outstanding, of which \$2,626 million and \$2,525 million were allocated to the Bank. Matched sale-purchase transactions are generally overnight arrangements.

At December 31, 2001 and 2000, U.S. government securities with par values of \$7,345 million and \$2,086 million, respectively, were loaned from the SOMA, of which \$832 million and \$250 million 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 held under agreements to resell. These investments are guaranteed as to principal and interest by the foreign governments.

Each Reserve Bank is allocated a share of foreign-currency-denominated assets, the related interest income, and realized and unrealized foreign currency gains and losses, with the exception of unrealized gains and losses on F/X swaps and warehousing transactions. This allocation is based on the ratio of each Reserve Bank's capital and surplus to aggregate capital and surplus at the preceding December 31. The Bank's allocated share of investments denominated in foreign currencies was approximately 9.158 percent and 8.994 percent at December 31, 2001 and 2000, respectively.

The Bank's allocated share of investments denominated in foreign currencies, valued at current exchange rates at December 31, were as follows (in millions):

	2001	2000
<i>European Union Euro:</i>		
Foreign Currency Deposits	\$ 420	\$ 417
Government Debt Instruments Including Agreements to Resell	247	244
<i>Japanese Yen:</i>		
Foreign Currency Deposits	173	248
Government Debt Instruments Including Agreements to Resell	487	494
Accrued Interest	6	6
Total	\$ 1,333	\$ 1,409

Total investments denominated in foreign currencies were \$14,559 million and \$15,670 million at December 31, 2001 and 2000, respectively.

The maturity distribution of investments denominated in foreign currencies which were allocated to the Bank at December 31, 2001, were as follows (in millions):

<i>Maturities of Investments Denominated in Foreign Currencies</i>	
Within 1 Year	\$ 1,256
Over 1 Year to 5 Years	37
Over 5 Years to 10 Years	40
Over 10 Years	—
Total	\$ 1,333

At December 31, 2001 and 2000, there were no open foreign exchange contracts or outstanding F/X swaps.

At December 31, 2001 and 2000, the warehousing facility was \$5 billion, with zero outstanding.

6. BANK PREMISES AND EQUIPMENT

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

	2001	2000
<i>Bank Premises and Equipment:</i>		
Land	\$ 6	\$ 6
Buildings	131	129
Building Machinery and Equipment	17	17
Construction in Progress	3	1
Furniture and Equipment	107	101
	\$ 264	\$ 254
<i>Accumulated Depreciation</i>	(127)	(119)
Bank Premises and Equipment, Net	\$ 137	\$ 135

Depreciation expense was \$15 million for each of the years ended December 31, 2001 and 2000, respectively.

The Bank leases unused space to outside tenants. Those leases have terms ranging from 1 to 10 years. Rental income from such leases was \$3 million for each of the years ended December 31, 2001, and 2000. Future minimum lease payments under non-cancelable agreements in existence at December 31, 2001, were (in millions):

2002	\$ 2
2003	3
2004	3
2005	2
2006	2
Thereafter	3
Total	\$ 15

7. COMMITMENTS AND CONTINGENCIES

At December 31, 2001, the Bank was obligated under non-cancelable leases for premises and equipment with terms ranging from 1 to approximately 10 years. These leases provide for increased rentals 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 each of the years ended December 31, 2001 and 2000, 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, 2001, were (in millions):

	<i>Operating</i>
2002	\$ 2
2003	2
2004	1
2005	1
2006	1
Thereafter	1
Total	\$ 8

Under the Insurance Agreement of the Federal Reserve Banks dated as of March 2, 1999, each of the Reserve Banks has agreed to bear, on a per incident basis, a pro rata share of losses in excess of 1 percent of the capital paid-in of the claiming Reserve Bank, up to 50 percent of the total capital paid-in of all Reserve Banks. Losses are borne in the ratio 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, 2001 or 2000.

On September 4, 2001, the Bank sold its Westgate facility for a total of \$3 million. The gain of \$1 million is reported as a component of "Other income."

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 two 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") and the Benefit Equalization Retirement Plan ("BEP"). The System Plan is a multi-employer plan with contributions fully funded by participating employers. No separate accounting is maintained of assets contributed by the participating employers. The Bank's projected benefit obligation and net pension costs for the BEP at December 31, 2001 and 2000, 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 \$4.7 million and \$4.4 million for the years ended December 31, 2001 and 2000, respectively, and are reported as a component of "Salaries and other benefits."

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. Net postretirement benefit cost is actuarially determined using a January 1 measurement date.

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

	2001	2000
Accumulated Postretirement Benefit Obligation at January 1	\$ 70.1	\$ 67.3
Service Cost—Benefits Earned During the Period	1.5	1.4
Interest Cost of Accumulated Benefit Obligation	5.4	4.7
Actuarial (Gain) Loss	10.0	(0.1)
Contributions by Plan Participants	0.3	0.2
Benefits Paid	(4.1)	(3.4)
Plan Amendments, Acquisitions, Foreign Currency Exchange Rate Changes, Business Combinations, Divestitures, Curtailments, Settlements, Special Termination Benefits	(8.0)	—
Accumulated Postretirement Benefit Obligation at December 31	\$ 75.2	\$ 70.1

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

	2001	2000
Fair Value of Plan Assets at January 1	\$ —	\$ —
Actual Return on Plan Assets	—	—
Contributions by the Employer	3.7	3.2
Contributions by Plan Participants	0.3	0.2
Benefits Paid	(4.0)	(3.4)
Fair Value of Plan assets at December 31	\$ —	\$ —
Unfunded Postretirement Benefit Obligation	75.2	70.1
Unrecognized Prior Service Cost	18.6	13.9
Unrecognized Net Actuarial Gain	(17.1)	(9.3)
Accrued Postretirement Benefit Cost	\$ 76.7	\$ 74.7

Accrued postretirement benefit cost is reported as a component of "Accrued benefit cost."

At December 31, 2001 and 2000, the weighted average discount rate assumptions used in developing the benefit obligation were 7.0 percent and 7.5 percent, respectively.

For measurement purposes, a 10.00 percent annual rate of increase in the cost of covered health care benefits was assumed for 2002. Ultimately, the health care cost trend rate is expected to decrease gradually to 5.00 percent by 2008, and remain at that level thereafter.

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, 2001 (in millions):

	One Percentage Point Increase	One Percentage Point Decrease
Effect on Aggregate of Service and Interest Cost Components of Net Periodic Postretirement Benefit Cost	\$ 1.3	\$ (1.0)
Effect on Accumulated Postretirement Benefit Obligation	11.9	(9.5)

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

	2001	2000
Service Cost-Benefits Earned During the Period	\$ 1.5	\$ 1.4
Interest Cost of Accumulated Benefit Obligation	5.4	4.7
Amortization of Prior Service Cost	(1.3)	(1.3)
Recognized Net Actuarial Loss	0.2	-
Net Periodic Postretirement Benefit Cost	\$ 5.8	\$ 4.8

Net periodic postretirement benefit cost is reported as a component of "Salaries and other benefits."

Postemployment Benefits

The Bank offers benefits to former or inactive employees. Postemployment benefit costs are actuarially determined and include the cost of medical and dental insurance, survivor income, and disability benefits. Costs were projected using the same discount rate and health care trend rates as were used for projecting postretirement costs. The accrued postemployment benefit costs recognized by the Bank at December 31, 2001 and 2000, were \$11 million and \$10 million, respectively. This cost is included as a component of "Accrued benefit cost." Net periodic postemployment benefit costs included in 2001 and 2000 operating expenses were \$2 million for each year.

10. SUBSEQUENT EVENT

Subsequent to December 31, 2001 Federal Reserve System management determined that it would not proceed with an ongoing technology project. Accordingly, in 2002 the Bank will record an asset impairment of \$7 million for assets currently held by the Bank on behalf of the System.

ADDITIONAL INFORMATION

Testimony and Speeches Regarding 9/11:

- * “The Condition of the Financial Markets,” Alan Greenspan, Federal Reserve Board, Testimony before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, September 20, 2001. www.federalreserve.gov/boarddocs/testimony/2001/.
- * “Monetary Policy and Economic Outlook,” Alan Greenspan, Federal Reserve Board, Testimony before the Joint Economic Committee, U.S. Congress, October 17, 2001. www.federalreserve.gov/boarddocs/testimony/2001/.
- * “The September 11 Tragedy and the Response of the Financial Industry,” Alan Greenspan, Federal Reserve Board, October 23, 2001. www.federalreserve.gov/boarddocs/speeches/2001/.
- * “Assessing the Impact of September 11,” Michael Moskow, Federal Reserve Bank of Chicago, October 25, 2001. www.chicagofed.org/newsandevents/speeches/index.cfm#2001.
- * “A Supervisory Perspective on Disaster Recovery and Business Continuity,” Roger Ferguson, Federal Reserve Board, March 4, 2002. www.federalreserve.gov/boarddocs/speeches/2002/.

Additional Information on Post-9/11

FOMC Actions:

- * Federal Open Market Committee statements and minutes. www.federalreserve.gov/fomc/.

General Information on the Topics Covered in this Report:

- * Fedpoints series: “How Currency Gets into Circulation,” #1; “Repurchase and Matched Sale Transactions,” #4; “Float,” #8; “Discount Window,” #10; “Federal Funds,” #15; “Commercial Paper,” #29; “Open Market Operations,” #32; “Fedwire,” #43; “Federal Open Market Committee,” #48. www.newyorkfed.org/pihome/fedpoint/index.html.

In-depth Information on the Federal Reserve and Open Market Operations:

- * “Understanding Open Market Operations.” www.newyorkfed.org/pihome/addpub/omo.html.
- * “The Federal Reserve System: Purposes and Functions.” www.federalreserve.gov/pf/pf.htm.

OUR MISSION

The Federal Reserve Bank of Chicago is one of 12 regional Reserve Banks across the United States that, together with the Board of Governors in Washington, D.C., serve as the nation’s central bank. The role of the Federal Reserve System, since its establishment by an act of Congress passed in 1913, has been to foster a strong economy, supported by a stable financial system.

To this end, the Federal Reserve Bank of Chicago participates in the formulation and implementation of national monetary policy, supervises and regulates state-member banks, bank holding companies and foreign bank branches, and provides financial services to depository institutions and the U.S. government. Through its head office in Chicago, branch in Detroit, regional offices in Des Moines, Indianapolis and Milwaukee, and facility in Peoria, the Federal Reserve Bank of Chicago serves the Seventh Federal Reserve District, which includes major portions of Illinois, Indiana, Michigan and Wisconsin, plus all of Iowa.

OUR VISION

- * Further the public interest by fostering a sound economy and stable financial system
- * Provide products and services of unmatched value to those we serve
- * Set the standard for excellence in the Federal Reserve System
- * Work together, value diversity, communicate openly, be creative and fair
- * Live by our core values of integrity, respect, responsibility and excellence

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