AUDITED FINANCIAL STATEMENTS OF THE FEDERAL FINANCING BANK FOR THE FISCAL YEARS 1998 AND 1997

OIG-99-057 MARCH 22, 1999

THE DEPARTMENT OF THE TREASURY 1789

Office of Inspector General

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United States Department of the Treasury

DEPARTMENT OF THE TREASURY
WASHINGTON

INSPECTOR GENERAL

March 22, 1999

MEMORANDUM FOR SECRETARY RUBIN

FROM: David C. Williams
Inspector General

SUBJECT: Audited Financial Statements of the Federal Financing Bank for the Fiscal Years 1998 and 1997

I am pleased to transmit the audited Fiscal Years (FY) 1998 and 1997 financial statements of the Federal Financing Bank (FFB) as required by the Government Corporation Control Act. These financial statements are incorporated in the FFB's FY 1998 Annual Report. The FFB's financial statements were audited by the firm of Arthur Andersen LLP, an independent public accountant (IPA). The IPA issued the following reports which are included in the attachment:

- Report of Independent Public Accountants on Financial Statements;
- Report of Independent Public Accountants on Internal Controls; and
- Report of Independent Public Accountants on Compliance with Laws and Regulations.

The IPA rendered an unqualified opinion on the FFB's FY 1998 and 1997 financial statements. The IPA noted that the FFB received an appropriation from Congress in FY 1999 to eliminate its accumulated deficit as of September 30, 1998 and it is unlikely that the FFB's net interest earnings will be sufficient to fund any future operating losses.

The Report of Independent Public Accountants on Internal Controls contained no reportable conditions. In addition, the Report of Independent Public Accountants on Compliance with Laws and Regulations contained no instances of noncompliance.

The IPA also issued a management letter dated January 14, 1999 discussing various issues that were identified during the audit, but are not required to be included in the audit reports.

As in the prior year, my staff monitored the conduct of the audits and performed a quality control review of the IPA's working papers. The audits were performed in accordance with ***Government Auditing Standards,*** issued by the Comptroller General of the United States.

Should you or your staff have any questions, please contact me at **(202) 622-1090,** or a member of your staff may contact William H. Pugh, Deputy Assistant Inspector General for Audit, (Financial Management) at **(202) 927-5430.**

Attachment

Report of Independent Public Accountants on Financial Statements

To the Inspector General and the Fiscal Assistant Secretary of
the U.S. Department of the Treasury:

We have audited the accompanying statements of financial position of the Federal Financing Bank (the "Bank") as of September 30,1998 and 1997, and the related statements of operations and accumulated deficit and statements of cash flows for the years then ended. 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 generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards (1994 revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as of September 30,1998 and 1997, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

As discussed in Notes 2 and 9 to the financial statements, the Bank received an appropriation from Congress in fiscal year 1999 to eliminate its accumulated deficit as of September 30,1998. However, it is unlikely that the Bank's net interest earnings will be sufficient to fund any future operating losses.

In accordance with Government Auditing Standards, we have also issued our reports dated January 14,1999, on our consideration of the Bank's internal controls over financial reporting and on our tests of its compliance with laws and regulations.

Arthur Andersen LLP

Vienna, Virginia
January 14,1999

Report of Independent Public Accountants on Internal Controls

To the Inspector General and the Fiscal Assistant Secretary of
the U.S. Department of the Treasury:

We have audited the financial statements of the Federal Financing Bank (the "Bank") as of and for the year ended September 30, 1998, and have issued our report thereon dated January 14, 1999, which included an emphasis of matter paragraph. As discussed in Notes 2 and 9 to the financial statements, the Bank received an appropriation from Congress in fiscal year 1999 to eliminate its accumulated deficit as of September 30, 1998. However, it is unlikely that the Bank's net interest eamings will be sufficient to fund any future operating losses.

We conducted our audit in accordance with generally accepted-auditing standards and the standards applicable to financial audits contained in Government Auditing Standards (1994 revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

In planning and performing our audit, we considered the Bank's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of the Bank in a separate letter dated January 14, 1999.

This report is intended solely for the information and use of the Inspector General, the Fiscal Assistant Secretary of the U.S. Department of the Treasury, management of the Bank, the Office of Management and Budget, and Congress and is not intended to be and should not be used by anyone other than these specified parties.

Arthur Andersen LLP

Vienna, Virginia
January 14, 1999

ARTHUR ANDERSEN LLP

Report of Independent Public Accountants on Compliance With Laws and Regulations

To the Inspector General and the Fiscal Assistant Secretary of
the U.S. Department of the Treasury:

We have audited the financial statements of the Federal Financing Bank (the "Bank") as of and for the year ended September 30,1998, and have issued our report thereon dated January 14, 1999, which included an emphasis of matter paragraph. As discussed in Notes 2 and 9 to the financial statements, the Bank received an appropriation from Congress in fiscal year 1999 to eliminate its accumulated deficit as of September 30,1998. However, it is unlikely that the Bank's net interest earnings will be sufficient to fund any future operating losses.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards (1994 revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws and regulations applicable to the Bank is the responsibility of the Bank's management. As part of obtaining reasonable assurance about whether the statements referred to above are free of material misstatement, we performed tests of the Bank's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of the financial statement amounts. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under Government Auditing Standards.

This report is intended solely for the information and use of the Inspector General, the Fiscal Assistant Secretary of the U.S. Department of the Treasury, management of the Bank, the Office of Management and Budget, and Congress and is not intended to be and should not be used by anyone other than these specified parties.

Arthur Andersen LLP

Vienna, Virgirua
January 14,1999

Federal Financing Bank

Statements of Financial Position
As of September 30, 1998 and 1997
(in thousands)

Assets

	1998	1997
Funds with U.S. Treasury	$ 348,163	$ 338,104
Loans receivable (Note 3)	46,141,863	50,154,168
Allowance for loan losses (Notes 1 and 2)	(217,269)	(300,827)
Loans receivable, net	45,924,594	49,853,341
Accrued interest receivable	1,051,234	1,240,839
Other	270	-
Total assets	$47,324,261	$51,432,284

Liabilities and Accumulated Deficit

	1998	1997
Borrowings (Note 4)	$49,216,664	$50,147,322
Accrued interest payable	1,379,862	1,966,322
Debt prepayment premium (Note 5)	-	2,201,191
Other liabilities	135	285,409
Total liabilities	50,596,661	54,600,244
Commitments and contingencies (Note 7)		
Accumulated deficit (Notes 2 and 9)	(3,272,400)	(3,167,960)
Total liabilities and accumulated deficit	$47,324,261	$51,432,284

The accompanying notes are an integral part of these statements.

Federal Financing Bank

Statements of Operations and Accumulated Deficit
For the Years Ended September 30,1998 and 1997
(in thousands)

	1998	1997
Interest on loans	$4,506,801	§ 5,261,798
Interest on borrowings	(4,615,223)	(5,317,022)
Net interest expense	(108,422)	(55,224)
Reversal of (provision for) loan losses (Note **1)**	6,019	(43,971)
Administrative expenses	(2,037)	(2,554)
Net loss	(104,440)	(101,749)
Accumulated deficit, beginning of the year (Notes 2 and 9)	(3,167,960)	(3,066,211)
Accumulated deficit, end **of** the year	$(3,272,400)	$(3,167,960)

The accompanying notes are an integral part of these statements.

Federal Financing Bank

Statements of Cash Flows
For the Years Ended September 30,1998 and 1997
(in thousands)

	1998	1997
Cash flows from operating activities:		
Net loss	$ (104,440)	$ (101,749)
Adjustments to reconcile net loss to net cash (used in) provided by operations:		
Decrease in accrued interest receivable	189,605	359,059
Increase in other assets	(270)	-
Decrease in accrued interest payable	(586,460)	(385,762)
Decrease in debt prepayment premium	(2,201,191)	-
(Decrease) increase in other liabilities	(285,274)	284,527
(Reversal of) provision for loan losses	(6,019)	43,971
Premium/ discount amortization	70	(202)
Net cash (used in) provided by operations	(2,993,979)	199,844
Cash flows from investing activities:		
Loan disbursements	(136,182,566)	(6,854,782)
Proceeds from loan principal collections	140,117,262	18,758,582
Net cash provided by investing activities	3,934,696	11,903,800
Cash flows from financing activities:		
Proceeds from borrowings	139,264,084	6,854,782
Repayments of borrowings	(140,194,742)	(18,958,445)
Net cash used in financing activities	(930,658)	(12,103,663)
Net increase (decrease) in cash	10,059	(19)
Cash, beginning of the year	338,104	338,123
Cash, end of the year	$ 348,163	$ 338,104

The accompanying notes are an integral part of these statements.

Federal Financing Bank

Notes to Financial Statements
For the Years Ended September 30,1998 and 1997

1. **Summary of** Significant Accounting Policies:

The Federal Financing Bank (the "Bank") was created by the Federal Financing Bank Act of 1973 **(12** USC 2281, the "Act") **as** an instrumentality of the U. S. Government and a body corporate under the general supervision of the Secretary of the Treasury. The budget and audit provisions of the Government Corporation Control Act are applicable to the Bank in the same manner as they are applied to other wholly owned government corporations.

The Bank was established by Congress at the request of the Treasury Department ("Treasury") in order "to assure coordination of Federal and federally assisted borrowing programs with the overall economic and fiscal policies of the government, to reduce the cost of Federal and federally assisted borrowing from the public, and to assure that such borrowings are financed in a manner least disruptive to private financial markets and institutions." The Bank was given broad statutory authority to finance obligations issued, sold, or guaranteed by Federal agencies so that the Bank could meet these debt management objectives.

The Bank is authorized, with the approval of the Secretary of the Treasury, to issue obligations to the public in amounts not to exceed **$15** billion. Additionally, the Bank is authorized to issue obligations in unlimited amounts to the Secretary of the Treasury and, at the discretion of the Secretary of the Treasury, may agree to purchase any such obligations.

Basis of Accounting

The financial statements are prepared in accordance with generally accepted accounting principles for commercial enterprises and, therefore, are presented on the accrual basis of accounting.

Funds With **U.S. Treasury**

As a government corporation, the Bank maintains a fund balance with Treasury (Fund account 20X4521) and does not hold cash. For the purposes of the statements of cash flows, the funds with Treasury are considered cash. These funds are readily available and meet the definition of cash equivalents established under Statement of Financial Accounting Standards No. 95, "Statement of Cash Flows." Interest paid by the Bank during fiscal years 1998 and 1997 approximated interest on borrowings included in the accompanying statements of operations.

Debt Prepayment Premium

The Debt Prepayment Premium is calculated as the difference between the face amount of the Treasury borrowing being prepaid (which is the amount the Bank receives in prepayment proceeds) and the present value of the expected future cash flows under the original terms, discounted at Treasury's cost of borrowing on the prepayment date (the amount the Bank must pay to Treasury in order to prepay the Bank's borrowings). The nature of the Debt Prepayment Premium is discussed in further detail in Note **5.**

Interest on Loans

Except as discussed in Note 2, the Bank's general policy is to charge borrowers a fee of one-eighth of one percent more than its cost of borrowing from Treasury. Adjustment of the one-eighth of one percent more than the borrower's interest rate may occur due to provisions in the loan agreement which affect the Bank's cost of borrowing. The income resulting from the fee is intended to cover the administrative expenses of the Bank, and the surplus, if any, is returned to the Treasury's General Fund.

Allowances for Loan Losses

Loan principal and interest are generally guaranteed by federal agencies and are backed by the full faith and credit of the U.S. Government. Direct loans to the USPS are an exception since the U.S. Government does not guarantee them. In management's opinion, loans receivable from the USPS as of September 30,1998 and 1997, were fully collectible; accordingly, no allowance for loan losses was recorded. The Bank has not incurred, and does not expect to incur, any credit-related losses on its loans. However, the Bank incurs losses related to certain legislatively mandated loan terms and has recorded an allowance for such losses.

The Bank records losses arising from forgone interest on Rural Utilities Service ("RUS") loans {see Note **2).** The Bank had impaired loans **as** a result of forgone interest as described in Note 2 with a book value of $4.6 billion at September 30,1998 and 1997, before related allowances for loan losses of $217 million and *$301* million, respectively. Interest on impaired loans is recognized using the current interest rate of the loan and the accrual method. The Bank recognized interest income of $496 million on its impaired loans for each of the years ended September 30,1998 and 1997. The Bank calculates its allowance for loan losses based on the total amount of future interest credit that it expects to provide to RUS discounted at the effective interest rate on the underlying loans. The allowance for loan losses is based on estimates, and ultimate losses may vary from current estimates. Adjustments to the allowance for loan losses are reported in the period that they are determined to be necessary.

Activity in the allowance for loan losses for the years ended September 30,1998 and 1997, is as follows:

	1998	1997
	(in thousands)	
Allowance for loan losses, beginning of year	$300,827	$456,880
(Reversal of) provision for loan losses	(6,019)	43,971
Charge-offs	(77,539)	(200,024)
Allowance for loan losses, end of year	$217,269	$300,827

Management periodically evaluates the underlying criteria used to determine the allowance for loan losses. Fluctuations in the allowance are the result of changes in economic conditions that result in an annual reversal of/provision for loan losses.

Management's Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make 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.

Related Parties

The Bank is subject to the general supervision and direction of the Secretary of the Treasury. As provided by law, the Secretary of the Treasury acts as Chairman of the Board of Directors. Employees of Treasury's departmental offices perform the Bank's management and accounting functions; its legal counsel is the General Counsel of the Treasury. The Bank reimburses Treasury for facilities and services that the Treasury provides. These reimbursements totaled $2.0 million and $2.5 million for the years ended September 30,1998 and 1997, respectively.

2. Accumulated Deficit:

As a consequence of the legislative requirements that result in the forgone interest and the loan prepayments as described below and in Note 5, the Bank has incurred significant operating losses. It is unlikely that the Bank's net interest earnings at the current spread will be sufficient to fund its liabilities and eliminate its accumulated deficit. Therefore, management of the Bank is seeking (and, subsequent to year-end, received) an appropriation in fiscal year 1999 from Congress (see Note 9).

Forgone Interest

Under Title III of the Rural Electrification Act of 1936, the Bank receives interest on certain loans to the RUS at an interest rate that is less than the contractual interest rate stated in the loan agreements to RUS. The amount of interest contractually due to the Bank is reduced by the amount of an interest credit to RUS. This interest credit is calculated based on the balance in a

RUS Liquidating Fund. The **Bank** has no control over the balances in the RUS Liquidating Fund. The Bank does not have any recourse against RUS and must absorb the cost of the interest credit (i.e. "forgone interest"). However, the **Bank** is obligated to pay contractual interest on its borrowings from Treasury.

Statement of Financial Accounting Standards ("SFAS") No. 114, "Accounting by Creditors for Impairment of a Loan," requires that impaired loans be measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or based on the fair market value of the loan or underlying collateral. SFAS No. 114 considers a loan to be impaired when, based on current information and events, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the original agreement. Management of the **Bank** has determined that certain RUS loans are impaired as defined by SFAS No. 114 since the **Bank** will not receive all interest due in accordance with the original terms of the loan agreements.

3. Loans Receivable:

Loans receivable includes agency loans purchased, direct loans to federal agencies, and loans to nonfederal entities. Agency loans purchased are either notes or pools of loans sold by federal agencies in the form of certificates representing shares of ownership in the loan pool. The selling agencies guarantee the principal and interest repayments on the notes or certificates. Direct loans to agencies are debt securities issued to the Bank by agencies that Congress has authorized so that these federal agencies can finance their activities. These include loans made to the Export-Import **Bank** of the U.S., the Federal Deposit Insurance Corporation (RTC Resolution Fund), and the USPS. Loans to nonfederal entities are loans made to nonfederal borrowers whose obligation to repay the principal and interest is guaranteed by a federal agency.

Loans receivable at September 30,1998 and 1997, consist of the following:

Agency	1998	1997
	(in thousands)	
Agency Loans Purchased:		
Farmers Home Administration, Department of Agriculture	$13,175,000	$17,205,000
Medical Facilities, Department of Health and Human Services	7,179	17,430
Health Maintenance Organization, Department of Health and Human Services	3,090	-
Rural Utilities Service, Department of Agriculture	4,598,907	4,598,907
Small Business Administration	-	14
Total Agency Loans Purchased	17,784,176	21,821,351
Direct Loans to Agencies:		
Export-Import Bank of the U.S.	-	1,294,550
Federal Deposit Insurance Corporation	-	1,374,983
U. S. Postal Service	5,696,100	1,963,500
Total Direct Loans to Agencies	5,696,100	4,633,033
Guaranteed Loans to Nonfederal Entities:		
Foreign Military Sales, Department of Defense	2,829,035	3,048,293
General Services Administration	2,660,520	2,629,531
Community Development Block Grants - Department of Housing and Urban Development	30,424	1,597,376
Low Rent Public Housing, Department of Housing and Urban Development	1,491,412	-
Ship Leasing, Department of Defense, Navy	1,224,931	1,308,077
Rural Utilities Service, Department of Agriculture	14,166,478	14,818,821
Small Business Administration	233,378	274,877
Virgin Islands, Department of Interior	17,475	18,723
Historical Black Colleges and Universities, Department of Education	4,712	671
Federal Railroad Administration, Department of Transportation	3,822	3,945
Total Guaranteed Loans to Nonfederal Entities	22,662,187	23,700,314
Allowance for Loan Losses (Note 1)	(217,269)	(300,827)
Discount	(600)	(530)
Total Loans Receivable, Net	$45,924,594	$49,853,341

4. Borrowings:

The Bank finances its loan portfolio primarily by borrowing from Treasury. Under the Federal Financing Bank Act of 1973, the Bank may, with the approval of the Secretary of the Treasury, borrow without limit from Treasury. At September 30,1998, the Bank had outstanding amounts owed to Treasury of $34.2 billion, with interest rates ranging from 4.731 to 16.241 percent and maturity dates from October 1,1998, to December 31,2031. At September 30,1997, the Bank had outstanding borrowings of $35.1 billion, with interest rates ranging from 4.578 to 16.241 percent and maturity dates from October 1,1997, to December 31,2029. The outstanding advance amount includes funds of $3.0 billion that the Bank borrowed from Treasury in September 1998 to finance the debt prepayment premium payable and related interest the Bank incurred on the liability as described in Note **5** and $0.2 billion in capitalized interest payable.

Additionally, at September 30,1998, the Bank had borrowings of $15.0 billion from the Civil Service Trust Fund, which is administered by the Office of Personnel Management ("OPM). These borrowings are at interest rates ranging from 8.75 to 9.25 percent with maturity dates ranging from June 30,2003, to June 30,2005.

Scheduled principal repayments of borrowings as of September 30,1998, are as follows:

Year Ending Seutember **30**	Amount (in thousands)
1999	$ 9,897,588
2000	1,987,143
2001	1,726,605
2002	1,743,227
2003	675,438
2004 and thereafter	33,186,663
Total	$49,216,664

5. Debt Prepayment Premium:

Under the terms of its master promissory note with Treasury, the Bank must liquidate its borrowings with Treasury at the same time as loans receivable financed by those borrowings are liquidated. The Bank's normal policy is to match the maturity and, except for a one-eighth of one percent spread, the interest rate on its loans receivable with the interest rate on its borrowings. In addition, for most of its loans, premiums or discounts resulting from loan prepayments are equivalent to the premiums or discounts the Bank paid or received when it simultaneously prepaid its Treasury borrowings. Premiums or discounts arise to the extent that market interest rates at the prepayment date differ from rates stated in the loan agreements. The effect of this policy is to mitigate the **Bank's** risk from interest rate fluctuations.

However, Congress authorized certain **RUS** guaranteed borrowers to prepay their loans at par rather than market value up to a specified dollar limit. Further, legislation also authorized borrowers in the foreign military sales program guaranteed by the Department of Defense to prepay, at par, certain loans meeting specific criteria. The effect of these statutes was to waive premium payments to the Bank, which would otherwise have resulted from the fact that interest rates at the dates of prepayment were less than the rates in the loan agreements. Notwithstanding the fact that the borrowers' premiums were waived, the Bank remained liable for premiums due on its debt to the Treasury and incurred prepayment penalties. The Bank's debt prepayment premium payable at September 30,1997, including interest of **$2.2** billion, was repaid to the Treasury through the issuance in September 1998 of an additional $3.0 billion loan to the **Bank.**

There were no debt prepayments in fiscal years 1998 and 1997. However, the Bank incurred interest expenses of $106 **million** and $108 million for fiscal years 1998 and 1997, respectively, on the debt prepayment premium payable.

6. Fair Value **of** Financial Instruments:

Funds with **U.S.** Treasury

The carrying amount of Funds with **U.S.** Treasury approximates fair value because of the liquid nature of the funds.

Loans Receivable and Borrowings

The fair value of loans receivable and borrowings is calculated using discounted cash flow analysis based on contractual repayment terms. The discount rates used in the loans receivable analysis is based on interest rates currently being offered by the **Bank** on loans of similar maturity and other characteristics. The discount rates used in the borrowings analysis is based on interest rates of current borrowings from Treasury using similar maturity and other characteristics. The fair value and face value of loans receivable at September 30,1998 and 1997, was **$56.4** billion and ***$56.0*** billion, respectively.

Accrued Interest Receivable, Accounts Receivable,
Accrued Interest Payable, Other Liabilities

These assets and liabilities are stated on the statements of financial position at the amount expected to be realized or paid.

Debt Prepayment Premium

The Debt Prepayment Premium, as of September 30,1997, represents a liability to Treasury under an indefinite borrowing agreement. There are no specified repayment terms, and the interest rate is fixed at the prepayment date. For purposes of estimating its fair value, it has been treated as payable on demand, which accrues interest at a floating rate. Therefore, debt prepayment premium on the statement of financial position is stated at fair value.

7. Commitments and Contingencies:

Almost all of the **Bank's** loans are to federal agencies or to private sector borrowers whose loans are guaranteed by a federal agency. When **an** agency has to honor its guarantee because a borrower defaults, that agency must obtain an appropriation or use other resources to pay the Bank. However, if an appropriation is not granted or federal agencies are not allowed to fund the losses by borrowing from the Treasury and the Bank is legislatively required to absorb the debt the agency owes it, then the Bank would incur a loss. The Bank has incurred such a loss related to forgone interest in fiscal years 1998 and 1997 as described in Note 2. Management of the Bank has established an allowance for losses related to forgone interest to be incurred in the future.

As of September 30,1998 and 1997, there were $17 billion and $22 billion, respectively, of loan commitments.

8. Pensions and Accrued Annual Leave:

Either the Civil Service Retirement System ("CSRS") or the Federal Employees Retirement System ("FERS") covers virtually all of the employees whose salary cost is allocated to the Bank by Treasury. For CSRS employees, Treasury withholds a portion of their base earnings. Treasury then matches the employees' contributions and the sum is transferred to the Civil Service Retirement Fund, from which the CSRS employees will receive retirement benefits. For FERS employees, Treasury withholds, in addition to Social Security withholdings, a portion of their base earnings. Treasury contributes an amount proportional to the employees' base earnings towards retirement and a scaled amount toward each individual FERS employee's Thrift Savings Plan, depending upon his or her level of savings. The FERS employees will receive retirement benefits from the Federal Employees Retirement System, Social Security System and the Thrift Savings Plan deposits that have accumulated in their accounts.

Although Treasury funds a portion of pension benefits under the CSRS and FERS relating to its employees and makes the necessary payroll withholdings from them, it has no liability for future payments to employees under these programs and does not account for the assets of the CSRS and FERS, nor does it report actuarial data with respect to accumulated plan benefits or the unfunded pension liability relative to its employees. These amounts are reported by OPM for the Retirement Systems and are not allocated to the individual employers. The OPM also accounts for health and life insurance programs for retired civilian federal employees. Similar to the accounting treatment afforded the retirement programs, the actuarial data related to the health and life insurance programs is maintained and reported by OPM and is not allocated on an individual employer basis.

9. Subsequent Event:

Public Law 105-277, approved by Congress on October 21,1998, appropriated $3,318 million to the Bank to liquidate certain Treasury debts and to eliminate the Bank's accumulated deficit at September 30,1998, as discussed in Note 2.