Note 26. Disclosure Entities and Related Parties

SFFAS No. 47, *Reporting Entity* provides criteria for identifying organizations that are consolidation entities, disclosure entities, and related parties, and how such organizations are reported within the *Financial Report*. For consolidation entities, the assets, liabilities, results of operations, and related activity are consolidated into the government's financial statements. For disclosure entities and related parties, balances and transactions with such entities are included in the financial statements and certain information about their relationship with the federal government is disclosed in the notes to the consolidated financial statements. Disclosure entities and related parties are important to the *Financial Report* but are not consolidated into the government's financial statements.

Disclosure Entities

Disclosure entities are organizations similar to consolidation entities in that they are either a) in the budget; b) majority owned by the government; c) controlled by the government; or d) would be misleading to exclude. Disclosure entities have a greater degree of autonomy with the government than consolidation entities. In addition, organizations may be owned or controlled by the government as a result of a) regulatory actions (such as organizations in receivership or conservatorship); or b) other government intervention actions. Under such regulatory or other intervention actions, if the relationship with the government is not expected to be permanent, such entities generally would be classified as disclosure entities based on their characteristics taken as a whole.

Based on the criteria in GAAP for federal entities, the disclosure entities in the *Financial Report* are FR System, SPVs, Fannie Mae, Freddie Mac, and National Railroad Passenger Corporation (more commonly referred to as Amtrak). In addition, there are additional disclosure entities reported by component reporting entities that do not meet the qualitative or quantitative criteria in SFFAS No. 47 to be reported in the *Financial Report*.

Federal Reserve System

Congress, under the Federal Reserve Act, created the FR System. The FR System includes the Federal Reserve Board, the FRBs, and FOMC. Collectively, the FR System serves as the nation's central bank and is responsible for formulating and conducting monetary policy, issuing and distributing currency (Federal Reserve Notes), supervising and regulating financial institutions, providing nationwide payment systems (including large-dollar transfers of funds, Automated Clearing House operations, and check collections), providing certain financial services to federal entities and fiscal principals, and serving as the U.S. government's bank. Monetary policy includes actions undertaken by the FR System that influence the availability and cost of money and credit as a means of helping to promote national economic goals. The FR System also conducts operations in foreign markets in order to counter disorderly conditions in exchange markets or to meet other needs specified by the FOMC to carry out its central bank responsibilities. The FR System is considered an independent central bank, and the executive branch of the government does not ratify its decisions.

The 12 FRBs are chartered under the Federal Reserve Act, which requires each member bank to own the capital stock of its FRB. Each FRB has a board of directors that exercises supervision and control of each FRB, with three members appointed by the Federal Reserve Board, and six board members elected by their member banks. The FRBs participate in formulating and conducting monetary policy, distributing currency and coin, and serving as the government's fiscal agent, as well as the fiscal agent for other fiscal principals. Fiscal principals, generally speaking, relate to banks, credit unions, and savings and loan institutions. Additionally, the FRBs provide short-term loans to depository institutions and loans to participants in programs or facilities with broad-based eligibility in unusual and crucial circumstances when approved by the Federal Reserve Board and the Secretary of the Treasury.

The government interacts with FRBs in a variety of ways, including the following:

- The FRBs serve as the government's fiscal agent and depositary, executing banking and other financial transactions on the government's behalf. The government reimburses the FRBs for these services, the cost of which is included on the Statements of Net Cost;
- The FRBs hold Treasury and other federal securities in the FRBs' SOMA for the purpose of conducting monetary policy (see Note 12—Federal Debt and Interest Payable);
- The FRBs hold gold certificates issued by the government in which the certificates are collateralized by gold (see Note 2—Cash and Other Monetary Assets);
- The FRBs hold SDR certificates issued by the government which are collateralized by SDRs (see Note 2—Cash and Other Monetary Assets); and
- The FRBs are required by Federal Reserve Board policy to transfer their excess earnings to the government, which are included in Other Taxes and Receipts on the Statements of Operations and Changes in Net Position.

- **Federal Reserve System Structure**

The Federal Reserve Board is an independent organization governed by seven members who are appointed by the President and confirmed by the Senate. The full term of a Federal Reserve Board member is 14 years, and the appointments are staggered so that one term expires on January 31 of each even-numbered year. The Federal Reserve Board has a number of supervisory and regulatory responsibilities for institutions including, among others, state-chartered banks that are members of the FR System, bank holding companies, and savings and loan holding companies. In addition, the Federal Reserve Board has general supervisory responsibilities for the 12 FRBs, and issues currency (Federal Reserve notes) to the FRBs for distribution.

The FOMC is comprised of the seven Federal Reserve Board members and five of the 12 FRB presidents, and is charged with formulating and conducting monetary policy primarily through open market operations (the purchase and sale of certain securities in the open market), the principal tool of national monetary policy. These operations affect the amount of reserve balances available to depository institutions, thereby influencing overall monetary and credit conditions.

- **Federal Reserve Monetary Policy Action**

To begin FY 2020, the FOMC sought to foster maximum employment and price stability. The Committee decided to maintain the target range for the federal funds rate at 1.5 to 1.75 percent. The Committee judged that the current stance of monetary policy was appropriate to support sustained expansion of economic activity, strong labor market conditions, and inflation near the Committee's symmetric 2 percent objective. Prior to the effects of COVID-19, the FOMC announced that it directed the FRBs to purchase Treasury bills for the SOMA at least into the second quarter of 2020 to ensure that the supply of reserves remains ample over time in light of recent and expected increases in the Federal Reserve's non-reserve liabilities. In addition, the FOMC directed the FRBs to conduct overnight and term repurchase agreement operations at least through the first quarter of FY 2020 to ensure that the supply of reserves remains ample even during periods of sharp increases in non-reserve liabilities, and to mitigate the risk of money market pressures that could adversely affect monetary policy implementation. These actions reaffirm the intention to implement monetary policy in a regime in which an ample supply of reserves ensures that control over the level of the federal funds rate and other short-term interest rates is exercised primarily through the setting of the Federal Reserve's administered rates. These are purely technical measures to support the effective implementation of the FOMC's monetary policy, and do not represent a change in the stance of monetary policy.

In light of the effects of COVID-19 on economic activity and on risks to the outlook, the FOMC rapidly lowered the target range for the federal funds rate. In March, the FOMC lowered the target range for the federal funds rate by a total of 1.5 percentage points, bringing it to the current range of 0 to 0.25 percent. The Committee expects to maintain this target range until it is confident that the economy has weathered recent events and is on track to achieve its maximum-employment and price-stability goals. FOMC noted that it would continue to monitor the implications of incoming information for the economic outlook, including information related to public health, as well as global developments and muted inflation pressures, and that it would use its tools and act as appropriate to support the economy. The Federal Reserve eased the stance of monetary policy and has deployed various additional tools to promote smooth functioning of financial markets and the flow of credit to households and businesses. To support the smooth functioning of those credit markets that are critical for the economy, the FRBs purchased Treasury securities and agency residential and commercial MBS, expanded repurchase agreement operations, and introduced several credit and liquidity facilities. Also, the Federal Reserve, with approval of the Secretary of the Treasury, established new credit and liquidity facilities under section 13(3) of the Federal Reserve Act to alleviate severe dislocations that arose in a number of financial markets and to support the flow of credit to households, businesses, and state and local governments. Furthermore, as financial stresses abroad risked spilling over into U.S. credit markets, the Federal Reserve and several other central banks announced the expansion and enhancement of dollar liquidity swap lines. In addition, the Federal Reserve introduced a new temporary repurchase agreement facility for foreign monetary authorities. The Federal Reserve has also made a number of adjustments to its regulatory and supervisory regime to facilitate market functioning and reduce regulatory impediments to banks supporting households, businesses, and municipal customers affected by COVID-19.

- **Federal Reserve System Assets, Liabilities, Revenues, Expenses, Gains, and Losses**

The FRBs hold Treasury and other securities in the SOMA for the purpose of conducting monetary policy. As of September 30, 2020, Treasury securities held by the FRBs totaled $4,050.1 billion, which excludes $395.1 billion in Treasury Securities used in overnight reverse repurchase transactions. As of September 30, 2019, Treasury securities held by the FRBs totaled $1,638.0 billion, which excludes $475.0 billion in Treasury securities used in overnight reverse repurchase transactions. Such securities are included in federal debt and interest payable (see Note 12—Federal Debt and Interest Payable). For fiscal years ended September 30, 2020, and 2019, Treasury incurred interest cost relating to the FRB's Treasury holdings amounting to $64.3 billion and $59.0 billion, respectively, which is included in interest on Treasury securities held by the public on the Statement of Net Cost. Unrestricted Cash held on deposit at the FRBs as of September 30, 2020, and 2019, was $ 1,769.8 billion and $376.1 billion, respectively, and are included in cash and other monetary assets. In addition, restricted cash as of September 30, 2020, and 2019, was $40.8 billion and $44.7 billion, respectively; a significant portion is held on deposit at the FRBs (see Note 2—Cash and Other Monetary Assets). The government issued SDR certificates to the Federal Reserve, valued at $5.2 billion as of September 30, 2020 and 2019, which were reported under Other Liabilities on the government's balance sheet (see Note 17—Other Liabilities).

Treasury securities are generally subject to the same market condition as other financial instruments. In the open market, the FRBs purchase and sell Treasury securities as a mechanism for controlling the money supply.

Financial and other information concerning the FR System, including financial statements for the Federal Reserve Board and the FRBs, may be obtained at https://federalreserve.gov.

- **FRB Residual Earnings Transferred to the Government**

FRBs generate income from interest earned on securities, reimbursable services provided to federal entities, and the provision of priced services to depository institutions, as specified by the *Monetary Control Act of 1980*. Although the FRBs generate earnings from carrying out open market operations (via the earnings on securities held in the SOMA account), their execution of these operations is for the purpose of accomplishing monetary policy rather than generating earnings. Each FRB is required by Federal Reserve Board policy to transfer to the government its residual (or excess) earnings, after providing for the cost of operations, payment of dividends, and surplus funds not to exceed an FRB's allocated portion of an aggregate of $6.8 billion for all FRBs. These residual earnings may vary due to, among other things, changes in the SOMA balance levels that may occur in conducting monetary policy. If an FRB's earnings for the year are not sufficient to provide for the cost of operations, payment of dividends, or allocated portion of $6.8 billion aggregate surplus funds limitation, an FRB will suspend its payments to the government until such earnings become sufficient. These funds are part of restricted cash at the Federal Reserve (see Note 2—Cash and Other Monetary Assets). The FRB residual earnings of $81.9 billion and $52.8 billion for fiscal years ended September 30, 2020, and 2019, respectively, are reported as other taxes and receipts on the Statements of Operations and Changes in Net Position. Accounts receivable, net, includes a receivable for FRB's residual earnings which represents the earnings due to the General Fund as of September 30, but not collected by the General Fund until after the end of the month. As of September 30, 2020, and 2019, accounts receivable on FRB's residual earnings are $0.2 billion and $0.6 billion, respectively (see Note 3—Accounts Receivable, Net).

Special Purpose Vehicles

In response to the COVID-19 pandemic, the government holds equity investments in SPVs established by the Federal Reserve Board for the purpose of enhancing the liquidity of the U.S. financial system. Involvement in these programs represents non-permanent intervention activities designed to help mitigate the economic impacts of the pandemic. Accordingly, the government's equity interests in these SPVs meet the SFFAS No. 47 criteria for classifying our SPV investments as disclosure entities. These entities are not consolidated as part of the government's consolidated financial statements; however, the value of the investments in the SPVs, changes in value, and related activity with the SPVs are included in the government's consolidated financial statements (see Note 8—Investments in Special Purpose Vehicles).

Fannie Mae and Freddie Mac

In 2008, during the financial crisis, the government placed Fannie Mae and Freddie Mac under conservatorship to help ensure their financial stability. These entities meet the criteria in SFFAS No. 47, for disclosure entities as both a) "receiverships and conservatorships,"; and b) as entities wherein "federal government intervention actions resulted in control or ownership" with intervention actions not expected to be permanent. Accordingly, these entities are not consolidated into the government's consolidated financial statements. However, the values of the investments in such entities, changes in value, and related activity with these entities are included in the government's consolidated financial statements (see Note 9—Investments in Government-Sponsored Enterprises for additional information).

Amtrak

Amtrak was incorporated in 1971 pursuant to the *Rail Passenger Service Act of 1970* and is authorized to operate a nationwide system of passenger rail transportation. Amtrak is a private, for-profit corporation under 49 U.S.C. § 24301 and District of Columbia law. It is not a department, entity, or instrumentality of the government. Amtrak's classification as a disclosure entity is attributable to being a) listed in the budget; b) financed mostly by sources other than taxes; and c) governed by an independent Board of Directors, which is comprised of 10 directors. The Secretary of Transportation (Secretary), who is a director by statute, and eight of the other Amtrak directors, are appointed by the President with the advice and consent of the U.S. Senate. The 10th board member, appointed by the board, is the President and Chief Executive Officer of Amtrak. Amtrak does not take actions on behalf of the government but benefits the national economy by providing a transportation option in 46 states and the District of Columbia.

The government (through the DOT) owns 100 percent of Amtrak's preferred stock (109,396,994 shares of $100 par value). Each share of preferred stock is convertible into ten shares of common stock. The common stockholders have voting rights for "amendments to Amtrak's Articles of Incorporation proposed by the Board of Directors and for certain other extraordinary events." Although Section 4.02(g) of the Amtrak Articles of Incorporation allow for the conversion of preferred stock to common stock, current government administrative policy is to not convert its holdings without Congressional authorization. Section 4.02(g) of the Amtrak Articles of Incorporation does not limit the timing of conversion or require any preapprovals. Conversion is effective the business day following receipt of written notice of the holder's election to convert. The government does not recognize the Amtrak preferred stock in its financial statements because, under the corporation's current financial structure, the preferred shares do not have a liquidation preference over the common shares, the preferred shares do not have any voting rights, and dividends are neither declared nor in arrears.

In addition to the purchase/ownership of the Amtrak preferred stock, the government has provided funding to Amtrak, since 1972, primarily through grants and loans. Amtrak receives grants from the government that cover a portion of the corporation's annual operating expenses and capital investments. Funding provided to Amtrak through grant agreements are included in the government's annual budget and the DOT financial statements. For the fiscal year ended September 30, 2020, the net cost amount was $2.6 billion, and total budgetary outlays were $3.0 billion. For the fiscal year ended September 30, 2019, the net cost amount was $2.4 billion, and total budgetary outlays were $1.9 billion.

The government has possession of two long-term notes with Amtrak. The first note is for $4.0 billion and matures in 2975 and, the second note is for $1.1 billion and matures in 2082 with renewable 99-year terms. Interest is not accruing on these notes as long as the current financial structure of Amtrak remains unchanged. If the financial structure of Amtrak changes, both principal and accrued interest are due and payable. The government does not recognize the long-term notes in its financial statements since the notes, with maturity dates of 2975 and 2082, are considered fully uncollectible due to the lengthy terms, Amtrak's history of operating losses, and ability to generate funds for repayment. Amtrak's ability to continue to operate in its current form is dependent upon the continued receipt of subsidies from the government.

Financial and other information concerning Amtrak including financial statements may be obtained at https://www.amtrak.com/reports-documents.

Related Parties

Related parties exist if the existing relationship, or one party to the existing relationship, has the ability to exercise significant influence over the party's policy decisions. Related parties do not meet the principles for inclusion, but are reported in the *Financial Report* if they maintain relationships of such significance that it would be misleading to exclude.

Based on the criteria in SFFAS No. 47, the related parties reported in the *Financial Report* are FHLBanks, IMF, Multilateral Banks, and PEFCO. In addition, there are additional related parties reported by component reporting entities that do not meet the criteria to be reported in the *Financial Report*.

Federal Home Loan Banks

The government is empowered with supervisory and regulatory oversight of the 11 FHLBanks. The government is responsible for ensuring that each regulated entity operates in a safe and sound manner, including maintenance of adequate capital and internal control, and carries out its housing and community development finance missions. Each FHLBank operates as a separate federally chartered corporation with its own board of directors, management, and employees. The FHLBanks are GSEs that were organized under the *Federal Home Loan Bank Act of 1932,* to serve the public by enhancing the availability of credit for residential mortgages and targeted community development. They are financial cooperatives that provide a readily available, competitively-priced source of funds to their member institutions. The FHLBanks do not have any special purpose entities or any other type of off-balance sheet conduits. The FHLBanks are not government entities and do not receive financial support from taxpayers. The government does not guarantee, directly or indirectly, the debt securities or other obligations of FHLBanks.

By law, in the event of certain adverse circumstances, Treasury is authorized to purchase up to $4.0 billion of obligations of the FHLBanks. This authority may be exercised only if alternative means cannot be effectively employed to permit the FHLBanks to continue to supply reasonable amounts of funds to the mortgage market, and the ability to supply such funds is substantially impaired because of monetary stringency and a high level of interest rates. Any funds borrowed from Treasury shall be repaid by the FHLBanks at the earliest practicable date. Treasury has not used such authority. Also, in accordance with the *Government Corporations Control Act*, Treasury prescribes certain terms concerning the FHLBanks issuance of obligations to the public. Due to the market volatility brought about by the COVID-19 pandemic and the resulting decline in interest rates, investors preferred short-term obligations. Despite the market volatility and the fluctuation in investor sentiment during FY 2020, the FHLBanks continued to manage their debt issuance to meet the needs of their members. Financial and other information concerning FHLBanks including financial statements may be obtained at http://www.fhlbanks.com/.

International Monetary Fund and Multilateral Development Banks

The IMF's primary purpose is to ensure the stability of the international monetary system—the system of exchange rates and international payments that enables countries to transact with each other. Member countries provide resources for IMF loans through their subscription quotas (quotas). The IMF also has two pools of resources that can be used in the event of a crisis that requires lending beyond the level available from quota resources: (i) the NAB and (ii) bilateral borrowing arrangements. Participation in the IMF works like an exchange of monetary assets.

Quotas are the principal component of the IMF's financial resources and are denominated in SDRs. The size of each member's quota is based broadly on its relative position in the world economy. The U.S. holds the largest quota of any IMF member. Since 2016, U.S. quota in the IMF has been about SDRs 83 billion. The equivalent dollar value of the quota total U.S. as of September 30, 2020 and 2019, was approximately $116.6 billion and approximately $113.0 billion, respectively. The government has funded a portion of U.S. quota to the IMF for lending, represented by U.S. reserve position at the IMF, while the remainder of the U.S. quota is represented by a letter of credit on which the IMF can draw as needed for lending. The U.S. reserve position was approximately $31.2 billion as of September 30, 2020, and approximately $23.0 billion as of September 30, 2019, with the remaining undrawn letter of credit representing the balance (see Note 2—Cash and Other Monetary Assets and Note 19—Commitments). The government's quota serves as the key determinant for its 16.5 percent share of voting rights in various IMF decisions. Since certain key IMF decisions require approval by at least 85 percent of the voting power, the government (represented by the Secretary of the Treasury) holds a substantial voice in the IMF and exercises significant influence over IMF policies, including veto power over major IMF decisions.

Some IMF members also supplement the IMF's resources through the NAB and bilateral borrowing agreements. Through the NAB, the U.S. and other participating members make additional resources available to the IMF if required to cope with or forestall an impairment of the international monetary system. The government's participation in the NAB as of September 30, 2020 and 2019, was SDR 28.2 billion, which is equivalent to $39.7 billion and $38.4 billion, respectively. When the government transfers funds to the IMF under the NAB, it receives a liquid and interest-bearing claim on the IMF. As of September 30, 2020, and 2019, loans outstanding to the IMF from the government under the NAB stood at $1.7 billion and $2.5 billion, respectively. These loans were reported under Loans Receivable on the Balance Sheet. The NAB is not currently activated, and the U.S. has veto power over its activation, as well as over most changes to its terms or size. The government does not have a bilateral borrowing agreement with the IMF, though it exercises indirect control over their activation, since NAB activation is a prerequisite for the IMF to draw on its bilateral borrowing arrangements.

As of September 30, 2020, and 2019, the government's total undrawn financial commitment to the IMF was $123.4 billion and $125.9 billion, respectively, which is composed of the quota related letter of credit and the undrawn portion of the NAB (see Note 19—Commitments).

Under the IMF Articles of Agreement, the IMF may allocate SDRs to member countries in proportion to their IMF quotas. SDR allocations are an international reserve asset created by the IMF to supplement its member countries' official reserves. The SDR allocation creates an asset and a liability on the Balance Sheet but does not increase the IMF's available lending resources. The SDR asset as of September 30, 2020 and 2019, amounted to $51.7 billion and $50.1 billion, respectively, and includes the SDR allocation as well as purchased SDRs (see Note 2—Cash and Other Monetary Assets). The SDR liability as of September 30, 2020 and 2019, amounted to $49.7 billion and $48.1 billion, respectively (see Note 17—Other Liabilities).

Historically, IMF has never experienced a default by a borrowing country. The government, which is not directly exposed to borrowers from the IMF, has never experienced a loss of value on its IMF quota or an instance of non-repayment, and it is not likely that the government will experience future losses as a result of its additional commitments.

Additionally, the government invests in and provides funding to the MDBs to support poverty reduction and promote sustainable economic growth in developing countries. The MDBs provide financial and technical support by means of strengthening institutions, providing assistance that addresses the root causes of instability in fragile and conflict-affected countries, responding to global crisis, and fostering economic growth and entrepreneurship. The government's participation in the MDBs is in the form of financial contributions used to ensure the effectiveness and impact of the MDBs' global development agenda. The U.S. has voting power in each of the MDBs to which it contributes, ranging from approximately 6 percent to 50 percent (see Note 10—Other Assets and Note 19—Commitments for additional information).

Private Export Funding Corporation

The financial statements reflect the results of agreements with PEFCO. PEFCO, which is owned by a consortium of private-sector banks, industrial companies, and financial services institutions, makes and purchases from private sector lenders, medium-term and long-term fixed-rate, and variable-rate loans guaranteed by EXIM Bank to foreign borrowers to purchase U.S. made equipment “export loans.”

EXIM Bank’s credit and guarantee agreement with PEFCO provides that EXIM Bank will guarantee the due and punctual payment of interest on PEFCO’s secured debt obligations which EXIM Bank has approved. It grants to EXIM Bank a broad measure of supervision over PEFCO's major financial management decisions, including the right to have representatives be present in all meetings of PEFCO’s board of directors, advisory board, and exporters’ council, and to review PEFCO’s financials and other records. However, EXIM Bank does not have voting rights and does not influence normal operations. In September 2020, the EXIM Board of Directors unanimously voted to renew its agreement with PEFCO for 25 years.

In addition, PEFCO has an agreement with EXIM Bank which provides that EXIM Bank will generally provide PEFCO with an unconditional guarantee covering the due and punctual payment of principal and interest on export loans PEFCO makes and purchases. PEFCO’s guarantees on the export loans plus the guarantees on the secured debt obligations aggregating to $3,198.9 million at September 30, 2020 and $4,060.5 million at September 30, 2019, are included by EXIM Bank in the total for guarantee, insurance and undisbursed loans. The allowance related to these transactions is included in the Guaranteed Loan Liability on the Balance Sheets.

EXIM Bank received fees totaling $39.3 million in FY 2020 and $44.7 million in FY 2019 for the agreements, which are included in Earned Revenue on the Statements of Net Cost.