

FEDERAL RESERVE BANK *of* NEW YORK

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THOMAS C. BAXTER, JR.
GENERAL COUNSEL AND
EXECUTIVE VICE PRESIDENT

December 5, 2013

VIA FEDERAL EXPRESS AND ELECTRONIC MAIL

Mr. J.W. Verret
Chief Economist
U.S. House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Dear Mr. Verret:

I am responding to Chairman Hensarling's letter to William Dudley dated November 6, 2013. In that letter, Chairman Hensarling poses certain questions to the Federal Reserve Bank of New York ("New York Fed"), and also requests that we produce certain records.

The questions posed are directed toward issues arising from the way in which the Reserve Banks operate the Fedwire Securities System. As you know, the Fedwire Securities System is used to issue, maintain and transfer, in electronic form, all marketable U.S. Treasury securities, as well as many securities issued by federal government agencies, government sponsored enterprises and certain international organizations. Attached are responses to the questions posed by Chairman Hensarling, which we have prepared on the basis of information received from New York Fed staff.

The letter also requests that we produce certain records, all of which appear to relate to functions performed by the New York Fed as fiscal agent of the Treasury, in accordance with Section 15 of the Federal Reserve Act. Consistent with our duties as fiscal agent,¹ we have sought authorization from our fiscal principal to provide these records to you. Given our belief

¹ Restatement (Third) of Agency (2006) §§ 8.01 (duty of loyalty); 8.05, 8.06 (restrictions on communications of confidential information to third parties without consent); 8.09 (duty to act within scope of authority and to follow lawful instructions); 8.11 (duty to disclose material facts).

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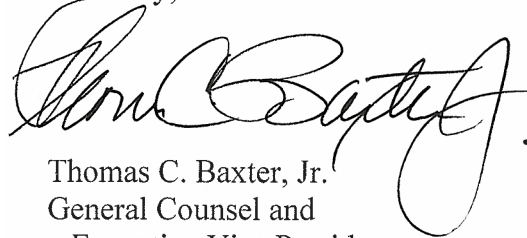
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that the requested records are non-public records, we are unable to produce these records until and unless we receive appropriate authorization from Treasury.

If you have further questions, or if you would like to follow up on the attachment to this letter or the letter itself, please do not hesitate to contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Tom Baxter, Jr.", written in a cursive style.

Thomas C. Baxter, Jr.
General Counsel and
Executive Vice President

Enclosure

cc: Chris Meade, Esq., General Counsel, U.S. Department of the Treasury
Travis Norton, Esq., General Counsel, Committee on Financial Services
Lawranne Stewart, Esq., Chief Counsel, Committee on Financial Services

1. Would the New York Fed, or any other governmental department, agency, or instrumentality involved with the operations of the Fedwire Securities System, be capable of identifying any payments that are not timely made utilizing the Fedwire Securities System.

The Fedwire Securities System is only used to make the following payments: Payments (a) of principal to security holders when securities held in the system are redeemed or mature, (b) of interest to security holders for securities held in the system, and (c) in connection with the purchase of securities on original issuance on the system or, at the request of the seller of the securities, in a secondary market transaction that results in the transfer of the security against payment on the books of the Reserve Banks. We assume for purposes of this question that you are only interested in principal and interest payments on U.S. Treasury securities held on the Fedwire Securities System.

As noted in the Payment System Risk Policy issued by the Board of Governors of the Federal Reserve System and available at http://www.federalreserve.gov/paymentsystems/psr_policy.htm, the Fedwire Securities System is designed such that principal and interest payments relating to U.S. Treasury and government agency securities are automatically credited to Reserve Bank customer accounts by 9:15 a.m. E.T. on the payment date. Accordingly, with respect to a specific Treasury security, in addition to the New York Fed and the Treasury Department, any party that holds such security directly in an account with a Reserve Bank (generally financial institutions) would be capable of identifying any payments of principal and interest that are not timely made under the terms of the Policy with respect to such security.

2. If the Treasury Department instructed the New York Fed to make certain payments over the Fedwire Securities System while directing that it forbear from making certain other payments, or if the Treasury Department gave such instructions directly to the Fedwire Securities System, could the Fedwire Securities System operate consistent with such instructions? If so, please assess the feasibility of accommodating that instruction; if not, please assess the feasibility of programming the Fedwire Securities System so that it could accommodate such an instruction.

As noted in the response to question 1, the only Treasury payments made over the Fedwire Securities System are principal and interest payments on Treasury securities. We therefore interpret your question to be whether the New York Fed could forbear making payments of principal and interest on Treasury securities. So long as the Treasury Department directed the New York Fed to refrain from making a scheduled principal and/or interest payment on a specific security before approximately 7:30 a.m. on the payment date, the New York Fed could take steps to prevent the payment from automatically occurring as scheduled. It is not operationally feasible to direct the New York Fed to pay only certain holders of the security or to

pay all holders of the security some lesser amount, and programming the applicable software to do so would likely require a multi-year development effort and a significant investment of financial resources.

There are other factors that might require the Treasury Department to make its decision to refrain from paying principal known to the New York Fed well before the 7:30 a.m. cutoff noted above. Specifically, in order to enable a Treasury security that is scheduled to mature to remain transferable on the Fedwire Securities Service from one Fedwire Securities account to another on and after the scheduled maturity date, the New York Fed must receive direction from the Treasury that it will not pay principal before the New York Fed completes its Fedwire Securities Service end of day processing on the business day before the scheduled maturity date.

3. Has the New York Fed, in its role as the operator of the Fedwire Securities System, ever engaged in any planning (whether in coordination with or independent from the Treasury Department) to consider how or whether to continue making principal and interest payments on Treasury debt if the nation's borrowing limit is not raised.

The New York Fed has taken steps to determine the operational capabilities of the Fedwire Securities System to continue making a scheduled principal and/or interest payment subject to a determination that the Treasury General Account is projected to have a sufficient cash balance or, upon instruction from Treasury, to refrain from automatically making a scheduled principal and/or interest payment or to make transferable a matured but defaulted Treasury security. The New York Fed has also identified the timeframes within which certain decisions would have to be made in order to allow the New York Fed to delay a scheduled principal and/or interest payment or to ensure the transferability of a matured but defaulted Treasury security, as described above in the response to question 2.