Appendix B

Priced Services

The Monetary Control Act of 1980 requires the Federal Reserve to charge depository institutions for certain services that the Federal Reserve had previously provided without explicit charge and only to member banks. As the act requires, the fees charged for providing these priced services are set to recover, over the long run, all direct and indirect costs of providing the services plus imputed costs, including the interest on items credited before actual collection (float), and the private-sector adjustment factor (PSAF). The intent of the PSAF calculation is to impute the costs that would have been incurred, such as taxes that would have been paid, and the profits that would have been earned had the Federal Reserve Banks' priced services been provided by a private firm. Table B.1 provides details on projected revenue from priced services.

Annual Pricing Process

To meet the requirement for the full recovery of costs over the long term, the Federal Reserve has developed an annual pricing process involving projections of Reserve Bank expenses, volumes, and revenues, as well as the PSAF and net income on clearing balances, for each major service category.

Fees for Federal Reserve services must be approved by the product director for the respective service, by the Financial Services Policy Committee, and ultimately by the Board of Governors.[1]

The cost of float is estimated by applying the federal funds rate to the level of float expected to be generated in the coming year. Estimates of income taxes and the return on capital are based on tax and financing rates derived using a model of the fifty largest U.S. bank holding companies. These rates are applied to the assets the Federal Reserve expects to use in providing priced services in the coming year.

The other components of the PSAF are derived from the budgets of the Reserve Banks and the Board: the imputed sales tax (based on budgeted outlays for materials, supplies, and capital); the imputed assessment for insurance by the Federal Deposit Insurance Corporation (based on expected clearing balances and amounts deferred to depository institutions for items deposited for collection with the Reserve Banks); and the portion of the expenses of the Board of Governors directly related to providing priced services. ▪

Table B.1

Revenue from Priced Services, 2003–2005

Millions of dollars

Service	2003	2004 (estimated)	2005 (budgeted)
Funds transfers and net settlement	51.1	57.9	64.2
Automated clearinghouse	68.2	75.2	82.1
Commercial checks	737.9	758.0	732.7
Book-entry securities transfers	21.8	20.8	21.4
Noncash collection	2.3	1.7	1.3
Special cash services	0.4	0.0	0.0
Total	**881.7**	**913.6**	**901.7**

1. The product directors are the first vice presidents at selected Reserve Banks with responsibility for day-to-day policy guidance over specific services. The Financial Services Policy Committee (FSPC) is responsible for the overall direction of financial services for the Federal Reserve Banks.

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Annual Pricing Process

To meet the requirement for the full recovery of costs over the long run, the Federal Reserve has developed an annual pricing process that involves projecting Reserve Bank expenses, volumes, and revenues, as well as the PSAF and net income on clearing balances, for each major service category.

Fees for Federal Reserve services must be approved by the product director for the respective service, by the Reserve Banks' Financial Services Policy Committee, and ultimately by the Board of Governors.[1]

The cost of float is projected by applying the federal funds rate to an estimate of the level of float to be generated in the coming year. Beginning in 2006, the PSAF targeted return on equity (ROE) capital is based on a simple capital asset pricing model using data from the equity market as a whole.[2] The ROE is applied to the level of priced-services equity that is imputed to finance the assets the Federal Reserve expects to use in providing priced services in the coming year. Estimates of income taxes are based on the tax rates derived using the financial data of the fifty largest U.S. bank holding companies.

The other components of the PSAF are derived from the budgets of the Reserve Banks and the Board: the imputed sales tax (based on budgeted outlays for materials, supplies, and capital); the imputed assessment for insurance by the Federal Deposit Insurance Corporation (based on expected clearing balances and

Table B.1

Revenue from Priced Services, 2004–2006

Millions of dollars

Service	2004	2005 (estimated)	2006 (budgeted)
Funds transfers and net settlement	57.1	64.9	69.3
Automated clearinghouse	75.1	84.6	86.8
Commercial checks	760.1	788.2	734.4
Book-entry securities transfers	20.4	21.0	22.1
Noncash collection	1.9	1.2	0.0
Total	**914.6**	**959.9**	**912.6**

1. The product directors are the first vice presidents at selected Reserve Banks with responsibility for day-to-day policy guidance over specific services. The Financial Services Policy Committee (FSPC) is responsible for the overall direction of financial services for the Federal Reserve Banks.

2. Prior to 2006, the ROE was based on the average return on equity results of three economic models that used bank holding company data.

amounts deferred to depository institutions for items deposited for collection with the Reserve Banks); and the portion of the expenses of the Board of Governors directly related to providing priced services.

Investment income is imputed and netted with related direct costs associated with clearing balances to estimate net income on clearing balances. ▪

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The Monetary Control Act of 1980 requires the Federal Reserve to charge depository institutions for certain services that the Federal Reserve had previously provided without explicit charge and only to member banks. As the act requires, the fees charged for providing these priced services are set to recover, over the long run, all direct and indirect costs of providing the services plus imputed costs, including the interest on items credited before actual collection (float) and the private-sector adjustment factor (PSAF). To calculate the PSAF, the Federal Reserve Banks impute the costs that would have been incurred, such as taxes that would have been paid, and the profits that would have been earned (return on equity) had the priced services been provided by a private business firm. Table B.1 provides details on projected revenue from priced services.

Annual Pricing Process

To meet the requirement for the full recovery of costs over the long run, the Federal Reserve has developed an annual pricing process that involves projecting Reserve Bank expenses, volumes, and revenues, as well as the PSAF and net income on clearing balances, for each major service category. Fees for Federal Reserve services must be approved by the product director for the respective service, by the Reserve Banks' Financial Services Policy Committee (FSPC), and ultimately by the Board of Governors.[1]

The cost of float is projected by applying the federal funds rate to an estimate of the level of float to be generated in the coming year. Beginning in 2006, the PSAF targeted return on equity (ROE) capital is based on a simple capital asset pricing model using data from the equity market as a whole.[2] The ROE is applied to the level of priced-services equity that is imputed to finance the assets the Federal Reserve expects to use in providing priced services in the coming year. Estimates of income taxes are based on the tax rates derived from the financial data of the fifty largest U.S. bank holding companies by deposit balance.

The other components of the PSAF are derived from the budgets of the Reserve Banks and the Board: the imputed sales tax (based on budgeted outlays for materials, supplies, and capital); the imputed assessment for insurance by the Federal Deposit Insurance Corporation (based on expected clearing balances and amounts deferred to depository institutions for

Table B.1

Revenue from Priced Services, 2005–07

Millions of dollars

Service	2005 (actual)	2006 (estimated)	2007 (budgeted)
Funds transfers and net settlement	67.3	71.3	72.7
Automated clearinghouse	87.4	89.7	99.9
Commercial checks	817.5	844.9	785.5
Book-entry securities transfers	21.3	21.8	23.3
Noncash collection[1]	1.2	0.0	0.0
Total	**994.7**	**1,027.7**	**981.3**

1. The Reserve Banks withdrew from the noncash collection service at year-end 2005.

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2. In 2005, the ROE was based on the average return on equity results of three economic models that used bank holding company data.

items deposited for collection with the Reserve Banks); and the portion of the expenses of the Board of Governors directly related to providing priced services.

Investment income is imputed and netted with related direct costs associated with clearing balances to estimate net income on clearing balances. ▪

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Annual Pricing Process

To meet the requirement for the full recovery of costs over the long run, the Federal Reserve has developed an annual pricing process that involves projecting Reserve Bank expenses, volumes, and revenues, as well as the PSAF and net income on clearing balances, for each major service category. Fees for Federal Reserve services must be approved by the product director for the respective service, by the Reserve Banks' Financial Services Policy Committee (FSPC), and ultimately by the Board of Governors.[1]

The cost of float is projected by applying the federal funds rate to the estimated level of float to be generated in the coming year. The PSAF return on equity is calculated by applying an equity financing rate, based on a simple capital asset pricing model using data from the equity market as a whole, to the level of priced-services equity that is imputed to finance the assets the Federal Reserve expects to use in providing priced services in the coming year. Estimates of income taxes are based on the tax rates derived from financial data for the fifty largest U.S. bank holding companies, based on deposit balances.

The other components of the PSAF are derived from the budgets of the Reserve Banks and the Board: the imputed sales tax (based on budgeted outlays for materials, supplies, and capital); the imputed assessment for insurance by the Federal Deposit Insurance Corporation (based on expected clearing balances and amounts deferred to depository institutions for items deposited for collection with the Reserve Banks); and the portion of the expenses of the Board of Governors

Table B.1

Revenue from Priced Services, 2006–2008

Millions of dollars

Service	2006 (actual)	2007 (actual)	2008 (budgeted)
Funds transfers and net settlement	72.3	74.5	72.9
Automated clearinghouse	91.4	102.0	99.1
Commercial checks	845.7	812.0	700.7
Book-entry securities transfers	21.9	23.9	23.6
Total	**1,031.2**	**1,012.3**	**896.2**

NOTE: Components may not sum to totals because of rounding.

1. The product directors are the first vice presidents at selected Reserve Banks with responsibility for day-to-day policy guidance over specific services. The FSPC is responsible for the overall direction of financial services for the Banks.

directly related to providing priced services.

Investment income is imputed and netted with related direct costs associated with clearing balances to estimate net income on clearing balances. ▪

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The Monetary Control Act of 1980 requires the Federal Reserve to charge depository institutions for certain services. The fees charged for providing these priced services are set to recover, over the long run, all direct and indirect costs of providing the services plus imputed costs, including the interest on items credited before actual collection (float) and the private-sector adjustment factor (PSAF). To calculate the PSAF, the Federal Reserve Banks impute the costs that would have been incurred, such as taxes that would have been paid, and the profits that would have been earned (return on equity) had the priced services been provided by a private business firm.

Annual Pricing Process

To meet the requirement for the full recovery of costs over the long run, the Federal Reserve has developed an annual pricing process that involves projecting Reserve Bank expenses, volumes, and revenues, as well as the PSAF and net income on clearing balances, for each service category.

Fees for Federal Reserve services must be approved by the product director for the respective service, by the Reserve Banks' Financial Services Policy Committee (FSPC), and, ultimately, by the Board of Governors.[1]

The cost of float is projected by applying the federal funds rate to an estimate of the level of float to be generated in the coming year. The PSAF targeted return-on-equity (ROE) capital is based on a capital-asset pricing model using data from the equity market as a whole. The ROE is applied to the level of priced services equity that is imputed to finance the assets the Federal Reserve expects to use in providing priced services in the coming year. Estimates of income taxes are based on the tax rates derived from the financial data of the 50 largest U.S. bank holding companies, based on deposit balances.

The other components of the PSAF are derived from the budgets of the Reserve Banks and the Board: the imputed sales tax (based on budgeted outlays for materials, supplies, and capital); the imputed assessment for insurance by the Federal Deposit Insurance Corporation (based on expected clearing balances and amounts deferred to depository institutions for items deposited for collection with the Reserve Banks); and the portion of the expenses of the Board of Governors directly related to priced services.[2]

To estimate net income on clearing balances, the priced services investment income is imputed and netted with related direct costs associated with clearing balances. The pro forma financial statements for the priced services are

1. The product directors are those first vice presidents at selected Reserve Banks with responsibility for day-to-day policy guidance over specific services. The FSPC is responsible for the overall direction of financial services for the Federal Reserve Banks.

2. On March 31, 2009, the Board of Governors requested public comment on a proposal to replace the current correspondent bank model underlying the PSAF calculation with a model based on elements derived from publicly traded firms more broadly.

presented in the *2008 Annual Report of the Board of Governors of the Federal Reserve System*. ■