Chapter 3

Federal Reserve Banks

The 1995 operating budgets for the twelve Federal Reserve Banks approved by the Board of Governors total \$1,869.3 million, an increase of \$64.1 million, or 3.6 percent, over estimated 1994 expenses (table 3.1). Not included in the budgets are the costs of two Bank special projects—Development of Currency Authentication Systems (\$1.3 million) and Automation Consolidation (\$37.8 million).[1] Including the costs of the special projects, the Banks' 1995 budgets total \$1,908.4 million, an increase of \$41.0 million, or 2.2 percent.

Employment excluding the staff associated with FRAS is budgeted at 23,240 ANP (average number of personnel), a decrease of 594 ANP, or 2.5 percent from estimated 1994 employment.[2] Including the FRAS staff, total budgeted employment is 23,832, a decrease of 491 ANP from estimated 1994 employment.

Expenses for personnel (salaries and benefits) account for \$1,183.8 million, or 63 percent of the 1995 operations budget, an increase of \$15.2 million, or 1.3 percent, over estimated 1994 personnel expenses (table 3.2). Nonpersonnel expenses (primarily for building and automation projects) are budgeted at \$685.5 million, an increase of \$48.9 million, or 7.7 percent, over estimated 1994 nonpersonnel expenses.

The following two sections discuss major initiatives and the budget objective for the Reserve Banks in 1995. Subsequent sections provide details for the four operational areas as well as for objects of expense, capital outlays, and long-term trends. Appendix A gives more information on capital outlays, special projects, and other special categories of expense, and appendix D gives additional data by District and operational area.

Major Initiatives

The 1995 Reserve Bank budgets provide for the following initiatives (table 3.3):

- Continuation of the automation consolidation project
- Installation of the Fednet communications network
- Installation of new high-speed currency processors
- Continued expansion of efforts in supervision and regulation
- Upgrading of check-processing equipment
- Continuation of the regionalization of savings bond operations
- Early retirement programs in several Districts.

1. The budget for the Automation Consolidation special project includes expenses for the twelve Districts and FRAS (Federal Reserve Automation Services, the unit responsible for consolidated data processing for the Reserve Banks). FRAS charges to the Automation Consolidation special project in 1995 are budgeted at \$32.7 million.

2. The term *average number of personnel* describes levels and changes in employment at the Banks. ANP measures the number of employees in terms of full-time positions for the time period. For instance, a full-time employee who starts work July 1 counts as 0.5 ANP for that calendar year; two half-time employees who start January 1 count as 1 ANP. Because the Banks' accounting system carries calculations related to employment to two decimal places but employment in this volume is expressed in whole numbers, rounding error may result in slight discrepancies in employment figures among the tables in this volume.

The automation consolidation initiative is budgeted to increase $14.9 million. The largest portion of this amount is related to FRAS production charges. Partially offsetting expenditures for this initiative are savings associated with the closing of local data processing centers and reductions in data processing staff.

The 1995 budgeted increase of $5.4 million for the Fednet communications network is due to additional circuit rentals, network equipment, and maintenance charges. The increase is being partially offset by lower costs for local circuits within Districts and the cost of District communications services being assumed by Fednet.

New projects related to currency are increasing $13.3 million over estimated 1994 expenses. The largest portion of the increase is due to the installation of thirty-eight new currency processors (ISS-3000) in eight Districts in 1995. The remainder of the increase is associated with higher maintenance and depreciation expenses, additional staff at three Reserve Banks to operate the new currency equipment, and the renovation and remodeling of cash areas to accommodate the equipment.

Although economic conditions within the banking industry have improved, the Reserve Banks have budgeted for several specific projects related to supervision and regulation that are increasing the 1995 budget a total of $7.2 million over estimated 1994 expenses. The increase is due mainly to the heightened emphasis on fair lending laws, the development and implementation of new Community

Table 3.1

Expenses and Employment at the Federal Reserve Banks, 1994 and 1995[1]

Category	1994 estimate	1995 budget	Change	
			Amount	Percentage
Expenses (millions of dollars)				
Operations[2]	1,805.2	1,869.3	64.1	3.6
Special projects	62.2	39.1	–23.1	. . .
Total	1,867.4	1,908.4	41.0	2.2
Employment (average number of personnel)[3]				
Operations[2]	23,834	23,240	–594	–2.5
FRAS	489	592	103	. . .
Total	24,323	23,832	–491	–2.0

1. Excludes capital outlays.
2. Includes support and overhead (see appendix D, table D.3, note 1, for definitions).
3. See text note 2 for definition of average number of personnel.

Table 3.2

Operating Expenses of the Federal Reserve Banks, by Object, 1993–95[1]

Millions of dollars, except as noted

Object	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Personnel	1,144.5	1,168.6	1,183.8	2.1	1.3
Nonpersonnel	567.0	636.6	685.5	12.3	7.7
Total	**1,711.5**	**1,805.2**	**1,869.3**	**5.5**	**3.6**

1. Includes the costs of support and overhead (see appendix D, table D.3, note 1, for definitions). Excludes special projects.

Reinvestment Act guidelines and performance measures, and the use of regression analysis in all eligible examinations of state member banks. Also contributing to the increase is the international supervisory program, including enhanced efforts associated with the Foreign Bank Supervision Enhancement Act (FBSEA); training and examinations in the mutual funds and derivatives areas; and the increased complexity of examinations resulting from mergers and consolidations and of supervision of risk-related initiatives.

Upgrading of check-processing equipment is budgeted to increase $2.1 million over estimated 1994 expenses. The upgrades will enhance the Banks' capability to provide high-quality, innovative, cost-effective check services in the long run, mainly by automating manual processes and upgrading equipment and software. Several Banks plan to acquire and install high-speed image equipment for processing of government checks. Many Banks also plan to offer commercial check image products to depository institutions and are upgrading sorters and check-processing control-system software with image-capable equipment.

In 1992, the Department of the Treasury decided to consolidate savings bond operations in the Federal Reserve System. Five Districts were designated as regional processing sites—New York (Buffalo office), Cleveland (Pittsburgh office), Richmond, Minneapolis, and Kansas City. The consolidation is expected to be completed by 1996. Included in the budget for consolidation activities is $24.3 million, a decrease of $1.1 million from estimated 1994 expenses. The decrease is due to staff reductions in the non-processing Districts.

1995 Budget Objective

In 1994, the Board of Governors approved a 1995 Reserve Bank budget objective that provided for an increase in total expenses, including special projects, of $67.9 million, or 3.6 percent, over estimated 1994 expenses. Excluding expenses for special projects, which were expected to decline in 1995, the increase was projected to be 4.9 percent. The Board anticipated that

Table 3.3
Major Initiatives of the Federal Reserve Banks, 1994 and 1995

Million of dollars, except as noted

Initiative	1994 estimate	1995 budget	Change, 1994 to 1995	Change as percentage of 1995 operating budget
Automation consolidation	48.4	63.3	14.9	.8
Fednet	50.2	55.6	5.4	.3
ISS-3000 currency processors	11.8	25.1	13.3	.7
Supervision and regulation	4.8	12.0	7.2	.4
Check-processing equipment	5.2	7.3	2.1	.1
Savings bonds regionalization	25.4	24.3	−1.1	−.1
Early retirement programs	1.1	−18.7	−19.8	−1.1
Total	**146.9**	**168.9**	**22.0**	**1.2**
MEMO				
Total operating expenses	1,805.2	1,869.3	64.1	3.6

Table 3.4

1995 Budget Objective and Budget of the Federal Reserve Banks[1]

Percent change from 1994 expenses

Item	Budget objective	Budget
Continuing operating expenses	2.5	2.0
Budget factors	2.4	1.6
Total excluding special projects	4.9	3.6
MEMO		
Special projects	−1.3	−1.4
Total including special projects	**3.6**	**2.2**

1. See data on expenses in table 3.1.

within this guideline, continuing operations would increase 2.5 percent over estimated 1994 expenses. Expenses for several budget factors—automation consolidation, Fednet, installation of currency processors, and savings bond regionalization—would account for $52.5 million of the overall projected 1995 increase. Table 3.4 compares the 1995 budget objective with the 1995 approved budget.

The 1995 budget increase for continuing operations is $9.8 million less than anticipated in the budget objective. The increase is less than the 2.5 percent target owing to larger-than-anticipated staff reductions, far exceeding the $6.0 million savings target established in the budget objective. The 1995 budget assumes staff reductions of 594 ANP, excluding FRAS, compared with the budget objective projected reduction of 436 ANP. Several Banks have budgeted for lower-than-anticipated staff levels because of lower volume, reduced requirements for data processing staff, and greater operational efficiencies. Staff reductions are projected for all operational areas except supervision and regulation. The most significant staff decrease, 288 ANP, is projected for the commercial check area.

The increase of $32.5 million for budget factors is $20.0 million below the target approved by the Board. The automation consolidation factor is $21.3 million lower than the objective owing to greater-than-anticipated savings from the closing of Reserve Bank data centers, staff reductions, and the move to the communal operating environment. The Fednet factor is also lower than anticipated, increasing $5.4 million rather than the anticipated $8.0 million included in the budget objective, primarily because of savings associated with local circuit costs and services being assumed by Fednet. The budget objective anticipated a savings of $4.3 million related to the savings bond regionalization effort currently under way. The 1995 budget includes

Table 3.5

Operating Expenses of the Federal Reserve Banks, by Operational Area, 1993–95[1]

Thousands of dollars, except as noted

Operational area	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Monetary and economic policy	114,617	124,373	135,055	8.5	8.6
Services to the U.S. Treasury and other government agencies	193,621	212,276	221,099	9.6	4.2
Services to financial institutions and the public	1,076,914	1,108,638	1,118,635	2.9	.9
Supervision and regulation	326,334	359,896	394,529	10.3	9.6
Total	**1,711,486**	**1,805,185**	**1,869,317**	**5.5**	**3.6**

1. Excludes special projects.

a savings of only $1.1 million, mainly because staffing levels will remain higher than projected: The budget objective assumed a net decrease of 73 ANP, but the 1995 budget is based on a net decrease of only 36 ANP.

The 1995 budget for special projects is $2.3 million below the budget objective. Lower-than-anticipated charges to the Automation Consolidation special project by FRAS and the Reserve Banks are primarily responsible for the variance.

Budget by Operational Area

Tables 3.5 and 3.6 summarize expenses and employment for the Reserve Banks' four operational areas. Tables 3.7 through 3.10 give details for each area.

Monetary and Economic Policy

The 1995 budget for the monetary and economic policy operational area is $10.7 million, or 8.6 percent, larger than estimated 1994 expenses. Approximately 40 percent of the increase is due to the impact of the automation consolidation budget factor. The budget also reflects several System and District initiatives, including the new Statistics and Reserves System (STAR) project, the second phase of the Trading Room Automated Processing System (TRAPS) project,

Table 3.6

Employment at the Federal Reserve Banks, by Activity, 1993–95[1]

Average number of personnel, except as noted[2]

Category	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Operational areas					
Monetary and economic policy	751	746	747	–.7	.1
Services to the U.S. Treasury and other government agencies	1,780	1,771	1,725	–.5	–2.6
Services to financial institutions and the public	8,610	8,349	8,065	–3.0	–3.4
Supervision and regulation	2,910	3,080	3,161	5.8	2.6
Support and overhead[3]					
Support	4,762	4,668	4,468	–2.0	–4.3
Overhead	5,183	5,219	5,074	.7	–2.8
Total	**23,996**	**23,833**	**23,240**	**–.7**	**–2.5**

1. Excludes special project and FRAS ANP.
2. See text note 2 for definition of average number of personnel.
3. See appendix D, table D.3, note 1, for definitions.

Table 3.7

Expenses of the Federal Reserve Banks for Monetary and Economic Policy, 1993–95[1]

Thousands of dollars, except as noted

Service	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Economic policy determination	93,018	98,833	108,048	6.3	9.3
Open market trading	21,599	25,540	27,007	18.2	5.7
Total	**114,617**	**124,373**	**135,055**	**8.5**	**8.6**

1. Excludes special projects.

and other automation projects. The staffing level remains flat overall, with slight changes in staffing by District. Early retirement programs resulted in staff reductions in the economic policy determination service that offset the increases needed to expand expertise in the assessment and control of financial system risk resulting from new and complex financial instruments.

Services to the U.S. Treasury and Other Government Agencies

The 1995 budget for services to the Treasury and other government agencies

Table 3.8

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies, 1993–95[1]

Thousands of dollars, except as noted

Service	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Savings bonds	37,843	15,480	0	−59.1	−100.0
Consolidated operations—savings bonds	36,849	64,485	76,493	75.0	18.6
Other Treasury issues	17,677	18,867	20,530	6.7	8.8
Consolidated operations—other Treasury issues	1,139	2,623	2,681	130.3	2.2
Centrally provided Treasury and agency services	22,558	22,955	25,989	1.8	13.2
Government accounts	28,155	34,108	37,525	21.1	10.0
Food coupons	21,443	22,326	23,468	4.1	5.1
Other	27,956	31,432	34,413	12.4	9.5
Total	**193,621**	**212,276**	**221,099**	**9.6**	**4.2**

1. Excludes special projects.

Table 3.9

Expenses of the Federal Reserve Banks for Services to Financial Institutions and the Public, 1993–95[1]

Thousands of dollars, except as noted

Service	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Currency	181,892	194,814	215,839	7.1	10.8
Coin	25,454	26,610	27,819	4.5	4.5
Special cash	6,247	5,797	5,069	−7.2	−12.6
Commercial check	523,584	532,698	521,011	1.7	−2.2
Other check	32,668	36,783	39,797	12.6	8.2
Funds transfer	69,087	72,931	66,413	5.6	−8.9
Automated clearinghouse	90,339	86,962	84,222	−3.7	−3.2
Book-entry securities transfer	33,773	35,846	37,523	6.1	4.7
Definitive securities safekeeping and noncash collection	11,098	8,545	7,118	−23.0	−16.7
Loans to member banks and others	17,204	18,789	21,359	9.2	13.7
Public programs	56,516	59,573	64,365	5.4	8.0
Other	29,053	29,290	28,100	.8	−4.1
Total	**1,076,914**	**1,108,638**	**1,118,635**	**2.9**	**.9**

1. Excludes special projects.

is $8.8 million, or 4.2 percent, higher than estimated 1994 expenses. The automation consolidation budget factor is contributing half of the overall increase. Also in the budget are several projects currently being performed for the Treasury. The staffing level is budgeted to decrease by 46 ANP as savings bond operations are consolidated at the five regional sites.

Services to Financial Institutions and the Public

Expenses for this operational area, which encompasses both priced and nonpriced services, are budgeted to increase $10.0 million, or 0.9 percent, in 1995. The staffing level is budgeted to decrease by 284 ANP, owing mainly to reductions for the commercial check (288) and automated clearinghouse (8) services.

The commercial check service accounts for nearly half of the amount budgeted for this operational area and employs 4,775 ANP. The 1995 budget for this service reflects a decrease in expenses of $11.7 million, or 2.2 percent, a result of projections of lower volume, greater operational efficiencies, and early retirement programs; the staffing level is expected to decline by 288 ANP, or 5.7 percent, from the estimated 1994 level. Although forecasts differ from District to District owing to the varied effect of same-day settlement, growing competition, industry consolidation, and new check products, check volume overall has stabilized from the substantial loss in 1994, and a 0.1 percent decrease is anticipated for 1995. The expense reductions and relatively constant volume lead to a projection of a unit cost reduction of 3.4 percent for the commercial check service in 1995.

Expenses for the currency service are expected to increase $21.0 million, or 10.8 percent, in 1995, mainly because of the installation of the new cash processors. While offices that have completed installation of the new ISS-3000 processors are trimming staff owing to improved efficiencies, offices that will migrate to second-generation equipment in 1995 are increasing staff during the transition period. Overall, currency operations will show a net increase of 10 ANP. A 3.4 percent volume increase is projected in currency operations, with unit cost rising 7.2 percent.

The budget for the automated clearinghouse (ACH) service is declining $2.7 million, or 3.2 percent, primarily

Table 3.10

Expenses of the Federal Reserve Banks for Supervision and Regulation, 1993–95[1]

Thousands of dollars, except as noted

Service	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Supervision of District financial institutions	224,679	219,127	238,782	−2.5	9.0
Consumer affairs	. . .	28,578	33,870	. . .	18.5
Administration of laws and regulations related to banking	86,585	96,087	103,527	11.0	7.7
Studies of banking and financial market structures	15,070	16,105	18,350	6.9	13.9
Total	**326,334**	**359,896**	**394,529**	**10.3**	**9.6**

1. Excludes special projects.

because of the movement toward a centralized applications operating environment. ACH volume is expected to increase 13.3 percent.

Expenses for the funds transfer service are expected to decrease $6.5 million, or 8.9 percent, owing mainly to the full-year impact of savings associated with conversion to the centralized funds transfer software.

Supervision and Regulation

The 1995 budget increase for the supervision and regulation operational area of $34.6 million, or 9.6 percent, over estimated 1994 expenses reflects a staff increase of 81 ANP. The staff increase is necessary mainly to support several initiatives, including a major expansion of the Foreign Banking Organization supervision program, expanded fair lending/CRA initiatives and workloads, examinations related to mutual funds and derivatives, more-complex examinations resulting from mergers and consolidations, and automation and training efforts. Minor staff decreases are planned for several Districts owing to increased productivity and improved banking conditions.

Budget by Object of Expense

Personnel expenses—officer and employee salaries, other compensation to personnel, and retirement and other benefits—account for 63 percent of Reserve Bank operating expenses budgeted for 1995. The amount budgeted for 1995 is 1.3 percent greater than estimated 1994 expenses (table 3.11).

Salaries and other personnel expenses, which account for 49 percent of budgeted 1995 operating expenses, are expected to be $11.5 million, or 1.3 percent, greater than estimated 1994 expenses. Expenses for salaries are expected to

Table 3.11

Operating Expenses of the Federal Reserve Banks, by Object, 1993–95[1]

Thousands of dollars, except as noted

Object	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
PERSONNEL					
Officers' salaries	88,072	91,673	92,674	4.1	1.1
Employees' salaries	774,343	787,148	809,455	1.7	2.8
Other personnel[2]	30,721	30,828	19,048	.3	−38.2
Retirement and other benefits	251,403	258,941	262,639	3.0	1.4
Total personnel	1,144,539	1,168,590	1,183,816	2.1	1.3
NONPERSONNEL					
Forms and supplies	55,726	53,660	54,170	−3.7	1.0
Equipment	183,649	186,889	161,531	1.8	−13.6
Software	32,488	32,089	30,857	−1.2	−3.8
Shipping	79,118	78,989	79,081	−.2	.1
Travel	41,974	42,699	44,086	1.7	3.2
Buildings	148,387	154,166	159,596	3.9	3.5
Recoveries	−46,974	−48,845	−50,148	4.0	2.7
Other[3]	70,580	136,948	206,327	88.7	50.7
Total nonpersonnel	566,947	636,595	685,500	12.3	7.7
Total	**1,711,486**	**1,805,185**	**1,869,317**	**5.5**	**3.6**

1. Excludes special projects and FRAS.
2. Expenses for certain contractual arrangements, and miscellaneous personnel expenses.
3. Communications, fees, contra-expenses, shared costs distributed and received, excess capacity, and other.

increase $23.3 million, or 2.7 percent. Merit pay accounts for a large portion of this increase. Also contributing to additional salary expenses are promotions, reclassifications, and structure adjustments. These increases are being partially offset by savings of $16.4 million from staff reductions. Short-term position vacancies (lag) and lower overtime expenses are also contributing to savings. The decrease in other personnel expenses ($11.8 million) reflects a decline in the use of contract staff after the transition to FRAS and a decline in separation pay in 1995 after significant adjustments for data processing staff in 1994.

Expenditures for retirement and other benefits, which account for 14 percent of budgeted 1995 operating expenses, are expected to be $3.7 million, or 1.4 percent, greater than estimated 1994 expenses. Most of the 1995 increase is due to three factors: Social security expenses are increasing $1.0 million, other benefit payments are increasing $1.6 million, and thrift plan expenses are increasing $0.8 million. The increases in social security and thrift plan expenses, the result of merit salary programs, are being partially offset by staff reductions. The unusually high increase in other benefit payments is due to a subsidy to New York employees who use public transportation. Health care costs, which had been increasing rapidly, are projected to decrease in 1995 for both active and retired employees. Coverage for active employees is budgeted at $0.4 million, or 0.6 percent, below estimated 1994 expenses. Retiree medical expenses are budgeted at $0.3 million, or 0.5 percent, less than estimated 1994 expenses, mainly because of staff reductions, an emphasis on managed care, lower claims experience, and lower rates due to administrative efficiencies.

Nonpersonnel expenses, which account for 37 percent of budgeted 1995 operating expenses, are projected to increase 7.7 percent over estimated 1994 expenses.

Expenses for equipment are budgeted to decrease 13.6 percent, accounting for approximately 9 percent of budgeted 1995 operating expenses. The most significant factor is a shift of $20.2 million from Chicago to FRAS related to the transfer of the Network Management Control Center (NMCC)—equipment rentals of $12.9 million, depreciation expense of $4.6 million, and repairs and maintenance costs of $2.7 million. In addition, equipment rentals excluding rentals related to the NMCC are decreasing $11.6 million, mainly owing to the conversion of local circuits to Fednet. Partially offsetting these decreases are increases in equipment depreciation and equipment maintenance of approximately $7.2 million, which are due mainly to currency- and check-processing equipment.

Shipping expenses, which account for approximately 4 percent of Reserve Bank budgeted 1995 operating expenses, are expected to increase $0.1 million, or 0.1 percent, over estimated 1994 expenses. The increase will be partially offset by reduced use of postal services and a slight decrease in total Interdistrict Transportation Service (ITS) costs from the 1994 level.

Building expenses, which account for about 9 percent of budgeted 1995 operating expenses, are expected to increase 3.5 percent over estimated 1994 expenses. The increase is driven by increased property depreciation resulting from building improvements and renovations, some of which are related to the installation of ISS-3000 currency processors.

"Other" nonpersonnel expenses are budgeted to increase $69.4 million over estimated 1994 expenses, accounting for approximately 11 percent of budgeted 1995 operating expenses. The increase is due primarily to higher data processing charges from FRAS and higher data communications charges as a result of Fednet.

Capital Outlays

For the next three years, the Reserve Banks' capital budget will be dominated by proposed or ongoing building projects in Cleveland, Minneapolis, Atlanta, and New York. Cleveland's building will be extensively renovated to extend its useful life, improve life safety systems, and enhance the security of valuables handled by the Bank. An annex will be constructed on the bank-owned parking lot adjacent to the existing building. During 1995, the structural steel for the annex will be erected and the structure fully enclosed.

Excavation and foundation work for the new building in Minneapolis will proceed in 1995; construction is expected to be completed in 1997. Atlanta has budgeted for a proposed new head office facility and a new building for the Birmingham Branch; funds for land and architectural fees for both projects are included in the 1995 capital budget. New York will continue renovation of its head office building, a project that will be spread over ten years or more and will result in upgrading of the entire building.

For 1995, capital outlays (including funding for FRAS) are budgeted at \$378.5 million, an increase of \$89.1 million, or 31 percent, over estimated 1994 expenses (excluding FRAS, the increase is \$104.2 million) (table 3.12). The increase is driven by the building projects in Cleveland, Atlanta, and Minneapolis.

Outlays for buildings are budgeted at \$123.5 million, about 33 percent of total capital outlays. The budget includes the new building programs in Minneapolis (\$38.5 million), Atlanta (\$3.4 million), and Birmingham (\$3.3 million), the renovation and expansion project in Cleveland (\$37.7 million), and, in New York, floor-by-floor modernization (\$5.6 million) and cafeteria modernization (\$2.9 million). San Francisco has

Table 3.12

Capital Outlays of the Federal Reserve Banks, by Class of Outlay, 1993–95

Thousands of dollars, except as noted

Class of outlay	1993 actual	1994 estimate	1995 budget	Percentage change	
				1993 to 1994	1994 to 1995
Data processing and data communications equipment[1]	143,739	133,301	121,866	−7.3	−8.6
Buildings	53,825	64,795	123,463	20.4	90.5
Furniture, furnishings, and fixtures	20,840	15,240	16,338	−26.9	7.2
Other equipment[2]	36,444	49,129	73,852	34.8	50.3
Land and other real estate	1,016	6,123	15,100	502.7	146.6
Building machinery and equipment	13,435	8,050	14,643	−40.1	81.9
Leasehold improvements	5,010	539	1,054	−89.2	95.5
Software[3]	4,441	12,249	12,206	175.8	−.4
Total	**278,750**	**289,426**	**378,522**	**3.8**	**30.8**

1. Includes FRAS capital of \$78,883 thousand in 1993, \$49,983 thousand in 1994, and \$40,366 thousand in 1995.

2. Includes FRAS capital of \$56 thousand in 1994 and \$17 thousand in 1995.

3. Includes FRAS capital of \$2,475 thousand in 1993, \$9,103 thousand in 1994, and \$3,695 thousand in 1995.

budgeted for several remodeling and renovation projects, mostly for its northern Branches ($7.5 million). Almost all Districts have budgeted for renovation projects in cash-processing areas, mainly to prepare for the installation of ISS-3000 cash processors and materials-handling systems ($7.9 million).

Outlays for data processing and data communications are budgeted at $121.9 million, approximately 32 percent of total capital outlays. Included in the budget is check-imaging equipment for several Banks ($17.1 million), to support image capture, archival, and retrieval functions for the processing of government checks. Several Banks have included this equipment in their capital budgets because the Treasury has requested that all Reserve Banks be fully capable of capturing and archiving images of all government checks by mid-1996, to coincide with the Treasury's capability to access these images through a new image-retrieval system. Dallas has included medium-speed image-processing systems for its Branches ($0.8 million). In addition, the Reserve Banks have budgeted to replace check reader–sorters and related check equipment ($17.4 million), to increase productivity and to position themselves for commercial check image processing.

Other major data processing and data communications outlays in the 1995 Reserve Bank budget include $18.9 million for input devices—mainly PC workstations—in all districts ($18.5 million) and FRAS ($0.3 million). CPU equipment is budgeted at $12.2 million, mainly for FRAS ($10.2 million). The CPU equipment at FRAS is required to support the movement of the remaining Districts to consolidation sites and into a standardized or communal District-unique environment; the remaining CPU equipment is needed for check operations in four Districts. FRAS has also budgeted $16.7 million for network operations equipment to complete the Fednet communications system. Storage devices account for $15.8 million. FRAS has requested $9.1 million for DASD and tape equipment, and New York has budgeted $3.3 million for DASD to meet additional capacity requirements. The remainder of the outlays for data processing and data communications include $4.4 million for LAN equipment, $3.1 million for telephone equipment, $2.3 million for printers, and $1.1 million for video-conferencing equipment.

Furniture and other equipment purchases are budgeted at $90.2 million, about 24 percent of total capital outlays. The planned installation of ISS-3000 cash processors and associated equipment account for approximately 60 percent of these outlays ($54.4 million). The Banks plan to spend another $7.9 million on other cash-related equipment and $12.3 million to replace furniture and workstations.

Land and other real estate purchases are budgeted at $15.1 million; $14.7 million is related primarily to the proposed building projects in Atlanta and Birmingham.

Building machinery and equipment outlays are budgeted at $14.6 million. Included are upgrades in several Districts, including an elevator upgrade in Boston ($2.0 million), replacement of the security, life safety, and HVAC computer in Richmond ($2.0 million), and replacement of central plant equipment in Kansas City ($1.1 million).

Software purchases are budgeted at $12.2 million in 1995. Check-image software accounts for almost one-third of this amount ($3.4 million). FRAS has budgeted $3.7 million for software necessary to operate the four CPUs that will be upgraded in 1995, and Atlanta has budgeted $1.0 million in support of the Fedline system.

Trends in Expenses and Employment

Over the ten years ending with the 1995 budget, operating expenses of the Reserve Banks have increased an average of 5.3 percent per year (chart 3.1). Over the past five years, the increase has averaged 5.9 percent a year. Increases in expenses were higher after 1990 as a result of expanded bank supervision needs and the transition to a consolidated data processing environment.

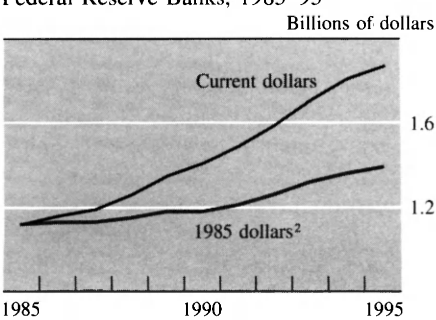
The number of employees at the Reserve Banks, excluding FRAS staff, has increased from 22,984 in 1985 to 23,240 in 1995, an increase of 256 ANP (chart 3.2). Since 1985, staffing has increased in supervision and regulation owing to the Federal Deposit Insurance Corporation Improvement Act of 1991 (1,249 ANP), in the currency service owing to volume growth (90 ANP), and in public programs intended to enhance communications with the public (81 ANP). Partially offsetting these increases have been decreases in the commercial check service (327 ANP), the overhead service (250 ANP), securities/noncash operations (209 ANP), the ACH and funds transfer services (194 ANP), fiscal agency operations (56), and the monetary policy administration service (69 ANP). The decreases have been due largely to consolidation of operations and operational efficiencies throughout the System.

Volume and Unit Costs

The volume of measured services as a whole in 1995 is expected to increase 2.0 percent over 1994 volume, and the unit cost is expected to decline 1.3 percent (table 3.13). Since 1990, volume has increased at an average annual rate of 1.2 percent and unit cost at a rate of 2.2 percent. The decrease in unit cost expected for 1995 reflects a net decrease in the payments area. For commercial check services, the largest component of the overall index, the unit cost is expected to decrease 3.4 percent, and for cash services, the second largest component, to increase 6.3 percent.

Chart 3.1

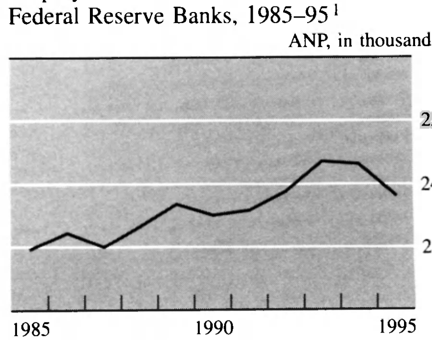
Operating Expenses of the Federal Reserve Banks, 1985–95[1]



1. Excludes expenses for special projects. For 1994, estimate; for 1995, budget.
2. Calculated with the GDP price deflator.

Chart 3.2

Employment at the Federal Reserve Banks, 1985–95[1]



1. Includes staff for special projects and FRAS. For 1994, estimate; for 1995, budget. See text note 2 for definition of ANP.

Table 3.13
Volume and Unit Costs of Measured Federal Reserve Bank Services
Percentage change from 1994 to 1995

Service	Volume	Unit cost
Payments	2.0	−5.2
Commercial check	−.1	−3.4
Automated clearinghouse	13.3	−14.3
Funds transfer	2.8	−11.4
Other checks	−.1	8.0
Cash [1]	3.2	6.3
Fiscal	−.2	8.8
Securities and noncash	.0	1.8
All measured services	**2.0**	**−1.3**

1. Includes currency and coin services.

1994 Budget Performance

The 1994 Reserve Bank operations budgets approved in December 1993 totaled $1,808.2 million, an expected increase of $96.7 million, or 5.6 percent, over actual 1993 expenses. The Reserve Banks now estimate that 1994 expenses were $1,805.2 million, $3.0 million, or 0.2 percent, under the approved budget. At this estimated level of spending, the increase over actual 1993 spending on operations was 5.5 percent.

Six Banks expect to be within 1.0 percent of their approved 1994 budgets. Two Banks expect overruns of more than 1.0 percent—St. Louis (3.1 percent) and Minneapolis (1.2 percent); in both Districts the overruns were due mainly to higher-than-anticipated expenses for automation consolidation and Fednet. Four Banks expect underruns of more than 1.0 percent—San Francisco (2.5 percent), Richmond (1.5 percent), Philadelphia (1.4 percent), and Cleveland (1.1 percent). San Francisco expects benefits costs to have been lower as a result of a capping of the Bank's contribution to retiree medical benefits, lower claims experience, and the switch to managed care. Richmond anticipates greater-than-budgeted recoveries from FRAS for host-site services provided. At Philadelphia, the underrun was due mainly to staff reductions resulting from savings bond regionalization, check volume losses resulting from same-day settlement, and the Bank's early retirement program. Cleveland's underrun resulted from delays in equipment acquisition and favorable health care experience. ■

Chapter 3

Federal Reserve Banks

The 1996 operating budgets for the twelve Reserve Banks approved by the Board of Governors total $1,968.8 million, an increase of $95.2 million, or 5.1 percent, over estimated 1995 expenses (table 3.1). Not included in the budgets is the cost of the Automation Consolidation special project ($36.9 million).[1] Including the cost of this special project, the Reserve Banks' 1996 budgets total $2,005.7 million, an increase of $88.9 million, or 4.6 percent.

Employment, including the staff associated with FRAS, is budgeted at 23,824 ANP (average number of personnel), a decrease of 143 ANP, or 0.6 percent, from estimated 1995 employment. Reserve Bank employment is expected to decrease by 113 ANP, and FRAS employment by 30 ANP.[2]

Expenses for personnel (salaries and benefits) account for $1,234.0 million, or 63 percent of the 1996 operations budget, an increase of $45.8 million, or 3.9 percent, over estimated 1995 personnel expenses (table 3.2). Nonpersonnel expenses (mainly for building and automation projects) are budgeted at $734.8 million, an increase of $49.4 million, or 7.2 percent, over estimated 1995 nonpersonnel expenses.

The following two sections discuss major initiatives and the budget objective for the Reserve Banks in 1996. Subsequent sections provide details for the four operational areas as well as for objects of expense, capital outlays, and long-term trends. Appendix A gives more information on capital outlays, the special project, and other special categories of expense, and appendix D gives additional data by District and operational area.

Major Initiatives

The 1996 Reserve Bank budgets provide for the following initiatives (table 3.3):

- Consolidation of data processing and data communications
- Installation of new high-speed currency processors
- Installation of equipment and software to support image processing of commercial and Treasury checks and archival of Treasury checks
- Changes to ensure compliance with generally accepted accounting principles for self-insured medical and postemployment benefits and compensated absences

1. The budget for the Automation Consolidation special project includes transition expenses associated with the move to a centralized environment and expenses for FRAS (Federal Reserve automation Services, the unit responsible for consolidated data processing for the Reserve Banks). FRAS charges to the Automation Consolidation special project in 1996 are budgeted at $25.8 million.

2. The term *average number of personnel* describes levels and changes in employment at the Reserve Banks. ANP measures the number of employees in terms of full-time positions for the time period. For instance, a full-time employee who starts work July 1 counts as 0.5 ANP for that calendar year; two half-time employees who start January 1 count as 1 ANP. Because the Reserve Banks' accounting system carries calculations related to employment to two decimal places but employment in this volume is expressed in whole numbers, rounding error may result in slight discrepancies in employment figures among the tables and charts in this volume.

- Application of the recently adopted regulations implementing the Community Reinvestment Act
- Office automation, and upgrading of local area networks
- New building programs

Charges to the Reserve Banks by FRAS are expected to increase $20.5 million, mostly because of increases related to data processing ($17.3 million), but also for additional equipment and support as customers are added to the Fednet data communications network ($3.2 million).

Expenditures on new projects related to currency are budgeted to increase $16.8 million over estimated 1995 expenses. Most of the increase is earmarked for the installation of thirty-four new currency processors in eleven Districts; the remainder is associated with higher depreciation and maintenance expenses, additional staff at two Reserve Banks to operate the new currency processors, and renovation and remodeling of cash areas to accommodate the equipment.

The budget includes $8.0 million for the check imaging initiative, $5.0 million more than estimated 1995 expenses. Approximately one-third of the funds are for the imaging project for Treasury checks: In 1996, the Federal Reserve will begin to provide image-supported check truncation services to the Treasury. Also, many Reserve Banks are upgrading their check sorters and their software for processing checks with image-capable equipment in anticipation of

Table 3.1

Expenses and Employment at the Federal Reserve Banks, 1995 and 1996[1]

Category	1995 estimate	1996 budget	Change	
			Amount	Percent
Expenses (millions of dollars)				
Operations[2]	1,873.6	1,968.8	95.2	5.1
Special project	43.2	36.9	–6.3	. . .
Total	1,916.8	2,005.7	88.9	4.6
Employment (average number of personnel)[3]				
Operations[2]	23,375	23,261	–113	–.5
FRAS	593	563	–30	. . .
Total	23,967	23,824	–143	–.6

1. Excludes capital outlays.
2. Includes support and overhead (see appendix D, table D.3, note 1, for definitions).
3. See text note 1 for definition of average number of personnel.

Table 3.2

Operating Expenses of the Federal Reserve Banks, by Object, 1994–96[1]

Millions of dollars, except as noted

Object	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Personnel	1,168.3	1,188.2	1,234.0	1.7	3.9
Nonpersonnel	628.6	685.4	734.8	9.0	7.2
Total	**1,796.9**	**1,873.6**	**1,968.8**	**4.3**	**5.1**

1. Includes the costs of support and overhead (see appendix D, table D.3, note 1, for definitions). Excludes special projects.

offering commercial check image products to depository institutions.

In 1994, the Board decided that the Reserve Banks should conform to generally accepted accounting principles (GAAP) for transactions similar to those in the private sector. Therefore, Reserve Bank accounting has been modified to provide for the accrual of self-insured expenses (medical and dental benefits and workers compensation), of compensated absences, and of postretirement benefits, including life and disability insurance. The change has added $5.6 million to the 1996 budget.

The Reserve Banks have budgeted $1.5 million and 23 ANP for implementation of the recently adopted Community Reinvestment Act (CRA) regulations—an increase of $1.0 million and 15 ANP over resources expended on this initiative estimated for 1995.

1996 Budget Objective

In 1995, the Board approved a 1996 Reserve Bank budget objective that provided for an increase in total expenses, including special projects, of $103.6 million, or 5.4 percent, over estimated 1995 expenses. Excluding expenses for special projects, which were expected to decline in 1996, the increase was projected to be 5.8 percent. The Board anticipated that within this guideline, expenses for ongoing Reserve Bank operations would increase 3.5 percent over estimated 1995 expenses. Expenses for several initiatives—automation consolidation, installation of new currency processors, check imaging activities, and CRA implementation—would account for $47.5 million of the projected 1996 increase. Partly offsetting the increase was an anticipated decrease of $3.9 million due to the nonrecurring transition expense of the move to conform with GAAP for private-sector-like transactions. The objective also included a savings target of $2.5 million. Table 3.4 compares the 1996 budget objective with the approved 1996 budget.

The 1996 increase for ongoing Reserve Bank operations (when the savings target is included) is $19.1 million less than anticipated in the budget objective. The increase is less than the 3.5 percent objective in part because the New York Reserve Bank shifted $4 mil-

Table 3.3
Major Initiatives of the Federal Reserve Banks, 1996

Million of dollars, except as noted

Initiative	1995 estimate	1996 budget	Change, 1995 to 1996	Contribution to total 1996 operating expense increase (percentage points)
FRAS production charges	143.8	164.3	20.5	1.1
Currency processors	26.5	43.3	16.8	.9
Check imaging projects	3.0	8.0	5.0	.3
Compliance with GAAP	3.9	9.5	5.6	.3
Implementation of CRA regulations	.5	1.5	1.0	.1
Office automation/LAN upgrades	1.8	5.5	3.7	.2
New building programs	.9	3.8	2.9	.1
Total	**180.4**	**235.9**	**55.5**	**3.0**
MEMO				
Total operating expenses	1,873.6	1,968.8	95.2	5.1

Table 3.4
1996 Budget Objective and Budget of the Federal Reserve Banks[1]

Percent change from 1995 expenses

Item	Budget objective	Budget
Continuing operating expenses	3.5	2.1
Initiatives	2.3	3.0
Total excluding special projects	5.8	5.1
Memo		
Special project	−.4	−.5
Total including special projects	**5.4**	**4.6**

1. See data on expenses in table 3.1.

lion more than expected from ongoing operations to the special project. Also, expenses for retirement and other benefits are $4.3 million lower than expected because of lower hospital and medical costs as Reserve Banks changed their health plans and benefit plans were reevaluated. In addition, other personnel expenses in 1995 were much higher than budgeted for; this nonrecurring increase in overtime expenses and in the use of outside agency help in 1995 contributed $11.9 million to the difference between the budget objective for ongoing operations and the approved budget.

The increase of $48.9 million for Reserve Bank initiatives is contributing $5.3 million above the target approved by the Board. The cost of compliance with GAAP is increasing from $3.9 million to $9.5 million, instead of decreasing from the $12.2 million to $8.3 million as was anticipated in the budget objective, owing to better information. Also, the cost of installing the new currency processors is $6.0 million greater than anticipated; although the new processors are expected to eventually result in lower staffing levels, staffing levels are expected to increase during the transition period to address inventory backlogs and to staff additional work shifts in two Reserve Banks. In contrast, FRAS production charges are $4.1 million lower than the budget objective: Costs for equipment and software are lower than expected because of a delay in the project to develop ACH application software for use in the consolidation environment.

The 1996 budget objective for special projects was $33.6 million, $5.4 million less than estimated 1995 expenses. The 1996 budget, at $36.9 million, is $3.3 million more than the budget objective, largely because the New York Reserve Bank's charges to the special project are increasing $4.7 million; the elimination in 1996 of the special project on currency authentication is partly offsetting these higher charges.

Table 3.5
Operating Expenses of the Federal Reserve Banks, by Operational Area, 1994–96[1]

Thousands of dollars, except as noted

Operational area	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Monetary and economic policy	120,869	127,528	136,618	5.5	7.1
Services to the U.S. Treasury and other government agencies	209,453	222,176	223,590	6.1	.6
Services to financial institutions and the public	1,105,140	1,127,573	1,177,579	2.0	4.4
Supervision and regulation	361,458	396,298	430,984	9.6	8.8
Total	**1,796,920**	**1,873,575**	**1,968,770**	**4.3**	**5.1**

1. Excludes special projects.

Budget by Operational Area

Tables 3.5 and 3.6 summarize expenses and employment for the Reserve Banks' four operational areas. Tables 3.7 through 3.10 give details for each area.

Monetary and Economic Policy

The 1996 budget for the monetary and economic policy operational area is $9.1 million, or 7.1 percent, more than estimated 1995 expenses. The increase is due to merit salary increases, higher charges by FRAS for data processing, the dollar impact of additional staff, and higher costs for developing and supporting client-server applications. Overhead expenses are increasing $2.1 million, or 6.0 percent, mainly because of the increases in expenses and the number of personnel and because of higher costs for the library activity, which includes responding to specific inquiries for information. The staffing level will increase by 8 ANP, or 1.1 percent, largely because of the full-year impact of filling vacant positions.

Services to the U.S. Treasury and Other Government Agencies

The 1996 budget for services to the Treasury and other government agencies

Table 3.6
Employment at the Federal Reserve Banks, by Activity, 1994–96[1]

Average number of personnel, except as noted[2]

Activity	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Operational areas					
Monetary and economic policy	729	728	736	–.1	1.1
Services to the U.S. Treasury and other government agencies	1,754	1,719	1,627	–2.0	–5.4
Services to financial institutions and the public	8,302	8,249	8,161	–.6	–1.1
Supervision and regulation	3,079	3,115	3,226	1.2	3.6
Support and overhead[3]					
Support	4,603	4,578	4,534	–.5	–1.0
Overhead	5,163	4,985	4,976	–3.5	–.2
Total	**23,630**	**23,375**	**23,261**	**–1.1**	**–.5**

1. Excludes special project and FRAS ANP.
2. See text note 2 for definition of average number of personnel.
3. See appendix D, table D.3, note 1, for definitions.

Table 3.7
Expenses of the Federal Reserve Banks for Monetary and Economic Policy, 1994–96[1]

Thousands of dollars, except as noted

Service	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Economic policy determination	96,192	99,780	107,025	3.7	7.3
Open market trading	24,677	27,748	29,593	12.4	6.6
Total	**120,869**	**127,528**	**136,618**	**5.5**	**7.1**

1. Excludes special projects.

is $1.4 million, or 0.6 percent, more than estimated 1995 expenses. Data processing charges by FRAS are the largest contributor to the increase. Overhead costs are also increasing, owing to increases resulting from initiatives in the bank administration and personnel areas and increases in security and telephone costs. The regionalization of savings bonds operations is partly offsetting the increases; the staffing level for this service is expected to decline by 50 ANP, or 6.8 percent, in 1996.

Services to Financial Institutions and the Public

Expenses for this operational area, which encompasses both priced and nonpriced services, are budgeted to increase

Table 3.8

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies, 1994–96[1]

Thousands of dollars, except as noted

Service	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Savings bonds	14,082	0	0	. . .	. . .
Centralized operations—savings bonds	62,930	72,144	69,344	14.6	–3.9
Other Treasury issues	19,655	22,579	22,456	14.9	–.5
Centralized operations—other Treasury issues	2,325	2,593	2,794	11.5	7.8
Centrally provided Treasury and agency services	23,830	27,501	30,455	15.4	10.7
Government accounts	33,854	38,060	37,152	12.4	–2.4
Food coupons	22,654	24,241	25,143	7.0	3.7
Other	30,123	35,057	36,245	16.4	3.4
Total	**209,453**	**222,176**	**223,590**	**6.1**	**.6**

1. Excludes special projects.

Table 3.9

Expenses of the Federal Reserve Banks for Services to Financial Institutions and the Public, 1994–96[1]

Thousands of dollars, except as noted

Service	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Currency	198,003	223,596	249,729	12.9	11.7
Coin	26,939	26,804	28,696	–.5	7.1
Special cash	5,939	5,010	5,929	–15.7	18.3
Commercial check	531,854	518,174	529,157	–2.6	2.1
Other check	35,936	38,315	41,336	6.6	7.9
Funds transfer	72,577	68,610	67,546	–5.5	–1.6
Automated clearinghouse	83,795	84,622	83,829	1.0	–.9
Book-entry securities transfer	35,654	38,484	38,875	7.9	1.0
Other securities and noncash collection	8,293	7,391	7,911	–10.9	7.0
Loans to member banks and others	18,458	20,596	21,877	11.6	6.2
Public programs	59,022	66,483	71,652	12.6	7.8
Other	28,669	29,489	31,043	2.9	5.3
Total	**1,105,140**	**1,127,573**	**1,177,579**	**2.0**	**4.4**

1. Excludes special projects.

$50.0 million, or 4.4 percent, in 1996. The staffing level is budgeted to decrease by 88 ANP; a decline for the commercial check service (160 ANP) is being partially offset by increases for public programs (28 ANP) and for the noncash collection service (14 ANP).

The commercial check service accounts for nearly half of the amount budgeted for this operational area and employs 4,748 ANP. The 1996 budget for this service is increasing $11.0 million, or 2.1 percent, a result of the installation of equipment and software to support check imaging and higher Fednet costs to support increased electronic products and services to paying financial institutions. Although forecasts differ by District, check volume has continued to stabilize from the substantial losses in 1994. The staffing level for this service is expected to decline by 160 ANP, or 3.2 percent, from the estimated 1995 level.

Expenses for the currency and coin services are budgeted to increase $28.0 million, or 11 percent, in 1996, mainly because of the installation of new currency processors: Offices that have completed installation of the new processors are trimming staff owing to improved efficiencies, but those that are in the transition phase are temporarily increasing staff.

The budget for the funds transfer service is declining $1.1 million, or 1.6 percent, and the budget for the automated clearinghouse (ACH) service is declining $0.8 million, or 0.9 percent, primarily because of the movement toward a centralized-applications operating environment.

Expenses for public programs in the Reserve Banks are expected to increase $5.2 million, or 7.8 percent, because of increased publications, expanded community affairs programs and other outreach programs, additional education for financial institutions about the new CRA regulations, and other economics education and public speaking requirements.

Supervision and Regulation

The 1996 budget increase for the supervision and regulation operational area of $34.7 million, or 8.8 percent, over estimated 1995 expenses reflects a staff increase of 111 ANP. At the New York Reserve Bank, additional staff will support a multiyear document-imaging initiative and expansion in the foreign banking division. Increases at

Table 3.10

Expenses of the Federal Reserve Banks for Supervision and Regulation, 1994–96[1]

Thousands of dollars, except as noted

Service	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Supervision of District financial institutions	219,941	236,598	256,663	7.6	8.5
Consumer affairs	28,959	37,074	42,577	28.0	14.8
Administration of laws and regulations related to banking	95,953	104,069	111,697	8.5	7.3
Studies of banking and financial market structures	16,605	18,557	20,046	11.8	8.0
Total	**361,458**	**396,298**	**430,984**	**9.6**	**8.8**

1. Excludes special projects.

other Reserve Banks are a result of state member bank growth; more-comprehensive supervision; the complexities of reviewing nontraditional banking products, regulatory changes, industry consolidation, and geographic expansion; and the full-year impact of filling vacancies in 1995.

Budget by Object of Expense

Personnel expenses—officer and employee salaries, other compensation to personnel, and retirement and other benefits—account for 63 percent of Reserve Bank operating expenses budgeted for 1996. The amount budgeted for 1996 is 3.9 percent more than estimated 1995 expenses (table 3.11).

Salaries and other personnel expenses, which account for 49 percent of budgeted 1996 operating expenses, are expected to be $32.3 million, or 3.5 percent, greater than estimated 1995 expenses. Expenses for salaries are budgeted to increase $43.3 million, or 4.8 percent. Merit pay accounts for a large portion of the increase; also contributing to higher salary expenses are promotions, reclassifications, changes in the mix of staff, and structure adjustments. Increases for salaries are being partially offset by a reduction of $4.6 million in overtime expenses due to volume declines and the conclusion of some 1995 initiatives in the check area; short-term position vacancies (lag) are also partly offsetting salary increases. The decrease in other personnel expenses ($11.0 million) is due to a decline in outside agency help.

Expenditures for retirement and other benefits, which account for 14 percent of budgeted 1996 operating expenses, are expected to be $13.5 million, or

Table 3.11
Operating Expenses of the Federal Reserve Banks, by Object, 1994–96[1]

Thousands of dollars, except as noted

Object	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
PERSONNEL					
Officers' salaries	90,716	95,007	98,758	4.7	3.9
Employees' salaries	782,238	809,289	848,844	3.5	4.9
Other personnel[2]	38,810	30,002	18,977	–22.7	–36.7
Retirement and other benefits	256,572	253,874	267,422	–1.1	5.3
Total personnel	1,168,337	1,188,172	1,234,000	1.7	3.9
NONPERSONNEL					
Forms and supplies	54,621	55,567	57,467	1.7	3.4
Equipment	183,915	154,568	178,688	–16.0	15.6
Software	31,101	31,221	34,949	.4	11.9
Shipping	78,419	79,157	78,952	.9	–.3
Travel	40,667	45,488	46,575	11.9	2.4
Buildings	154,403	157,561	166,134	2.0	5.4
Recoveries	–49,964	–51,319	–51,799	2.7	.9
Other[3]	135,420	213,160	223,805	57.4	5.0
Total nonpersonnel	628,582	685,403	734,771	9.0	7.2
Total	**1,796,919**	**1,873,575**	**1,968,770**	**4.3**	**5.1**

1. Excludes special projects.
2. Expenses for certain contractual arrangements, and miscellaneous personnel expenses.
3. Communications, fees, contra-expenses, shared costs distributed and received, excess capacity, and other.

5.3 percent, greater than estimated 1995 expenses. Approximately 40 percent of the 1996 increase is due to compliance with GAAP; other contributing factors are higher social security payments and thrift plan contributions, a reflection of higher salaries and staffing levels. Medical expenses are also contributing to the increase.

Nonpersonnel expenses, which account for 37 percent of budgeted 1996 operating expenses, are projected to increase 7.2 percent over estimated 1995 nonpersonnel expenses.

Expenditures on equipment are budgeted to increase 15.6 percent, accounting for approximately 9 percent of budgeted 1996 operating expenses. More than half the increase is due to the installation of the new high-speed currency processors. Equipment depreciation and maintenance costs are also increasing, owing mainly to the installation of check imaging, check processing, and end-user computing equipment.

Shipping expenses, which account for approximately 4 percent of Reserve Bank budgeted 1996 operating expenses, are expected to remain flat.

Building expenses, which account for about 8 percent of budgeted 1996 operating expenses, are expected to increase 5.4 percent over estimated 1995 building expenses. The increase is being driven by increased property depreciation resulting from building improvements and renovations, building projects related to the installation of new currency processors, and the new building projects in Minneapolis and Cleveland.

"Other" nonpersonnel expenses are budgeted to increase $10.6 million over estimated 1995 expenses, accounting for approximately 11 percent of budgeted 1996 expenses. The increase is due mainly to higher charges by FRAS for data processing and data communications.

Capital Outlays

For the next several years, the Reserve Banks' capital budget will be dominated by building projects. The New York Reserve Bank will continue the renovation of its head office building, a project that will be spread over ten years or more and will result in upgrading of the entire building. In Cleveland, an annex will be constructed adjacent to the existing building to house a new operations center. This project is scheduled to be completed in late 1996, followed by a complete renovation of the existing building to extend its useful life, improve life safety systems, and enhance the security of valuables handled by the Bank. In 1995, new building programs were approved for the head office in Atlanta and its Branch office in Birmingham; both projects are scheduled to be completed around the end of the century. In Minneapolis, the new office building will be ready for occupancy in July 1997.

For 1996, capital outlays (including funding for FRAS) are budgeted at $411.0 million, an increase of $45.4 million, or 12.4 percent over estimated 1995 outlays (excluding FRAS, the increase is $64.9 million) (table 3.12).

Outlays for buildings in 1996 are budgeted at $125.6 million, about 30 percent of total capital outlays. Included in the budget are the new building programs in Minneapolis ($40.8 million), Atlanta ($3.7 million), and Birmingham ($2.4 million); the renovation and expansion project in Cleveland ($35.3 million); the floor-by-floor modernization and renovations in New York ($13.6 million); and general renovation and modification projects in several other Districts ($16.4 million). Renovations in currency-processing areas are adding $3.4 million.

Outlays for data processing and data communications are budgeted at $113.3 million, approximately 28 percent of total capital outlays. Included in the budget is check-imaging equipment for eleven Districts ($24.8 million). In 1996, the Federal Reserve will begin to provide image-supported check truncation services to the U.S. Treasury. The budget includes funds for the System's image archival and retrieval system, for high-speed image-processing systems, and for other equipment and upgrades related to the Treasury's effort ($9.8 million). The remainder of the check-imaging capital budget covers upgrades to medium- and high-speed sorters and the installation of image-enhanced truncation equipment to support the Treasury and to position the Banks to provide commercial check image processing.

Other major data processing and data communications outlays budgeted for 1996 include $21.8 million for input devices—mainly PC workstations—in all Districts. More than $8 million is earmarked for CPU equipment, mostly for CPU upgrades at FRAS to meet production, testing, and contingency processing requirements ($6.1 million); the remainder of the CPU outlays is related to check operations in five Districts. Storage devices account for $11.4 million, including $6.2 million for DASD and tape equipment at FRAS; support for check-processing operations in several Districts will require an additional $5.1 million. Outlays of $12.1 million are needed to replace existing LAN communications equipment and to implement several upgrades. FRAS has budgeted $7.2 million for operations equipment for the Fednet network; the final milestone for the Fednet project, the conversion of District leased-line connections to Fednet, is scheduled to be completed in 1996. In addition, FRAS has budgeted $4.7 million for parallel sysplex equipment, which is expected to help manage workloads more efficiently, improve application availability, and reduce software costs. The remaining data processing and data communications outlays include $5.8 million for several

Table 3.12

Capital Outlays of the Federal Reserve Banks, by Class of Outlay, 1994–96

Thousands of dollars, except as noted

Class of outlay	1994 actual	1995 estimate	1996 budget	Percentage change	
				1994 to 1995	1995 to 1996
Data processing and data communications equipment[1]	143,121	113,405	113,345	–20.8	–.1
Buildings	43,385	108,045	125,609	149.0	16.3
Furniture, furnishings, and fixtures	12,487	16,555	27,997	32.6	69.1
Other equipment[2]	45,330	78,888	85,069	74.0	7.8
Land and other real estate	6,866	22,761	11,526	231.5	–49.4
Building machinery and equipment	5,194	12,822	21,286	146.8	66.0
Leasehold improvements	304	1,209	3,503	298.1	189.9
Software[3]	10,431	11,901	22,643	14.1	90.3
Total	**267,117**	**365,584**	**410,979**	**36.9**	**12.4**

1. Includes FRAS capital of $63,959 thousand in 1994, $48,995 thousand in 1995, and $27,747 thousand in 1996.

2. Includes FRAS capital of $1,820 thousand in 1994, $38 thousand in 1995, and $111 thousand in 1996.

3. Includes FRAS capital of $6,275 thousand in 1994, $3,171 thousand in 1995, and $4,808 thousand in 1996.

projects at the New York Reserve Bank, $3.9 million for telephone systems, and $3.6 million for printers.

Furniture and other equipment purchases are budgeted at $113.1 million, about 27 percent of total capital outlays. The continued installation of new currency processors and associated equipment accounts for about half of the total ($57.4 million). The Reserve Banks plan to spend another $13.1 million on other cash-related equipment and $23.1 million to replace furniture and workstations.

Building machinery and equipment outlays are budgeted at $21.3 million. Included are items related to Minneapolis's new building ($5.9 million) and replacements and upgrades in several Districts, including chiller replacements and upgrades ($3.2 million), boiler-generator upgrades ($1.0 million), elevator upgrades ($2.0 million), and an HVAC computer in Richmond ($2.6 million).

Land and other real estate purchases are budgeted at $11.5 million, for the new building in Birmingham and for the Dallas Reserve Bank's purchase of a lot adjacent to its building to improve the security of the building's perimeter.

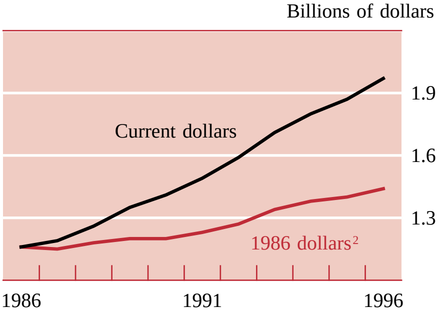
Software purchases in 1996 are budgeted at $22.6 million. Check-image software accounts for more than half of the total ($11.6 million). FRAS has budgeted $4.8 million for software associated mainly with the CPUs that will be upgraded.

Trends in Expenses and Employment

Over the ten years ending with the 1996 budget, Reserve Bank operating expenses have increased an average of 5.4 percent a year (chart 3.1). The number of employees at the Reserve Banks, excluding FRAS staff, has increased from 23,240 in 1986 to 23,261 in 1996, an increase of 21 ANP (chart 3.2). Since 1986, staffing has increased in supervision and regulation owing to the implementation of the Federal Deposit Insurance Corporation Improvement Act (1,139 ANP), in the currency service owing to volume growth (113 ANP), and in public programs owing to enhanced communications with the public (115 ANP). Partly offsetting these increases have been decreases in the commercial check service (403 ANP), the overhead services

Chart 3.1

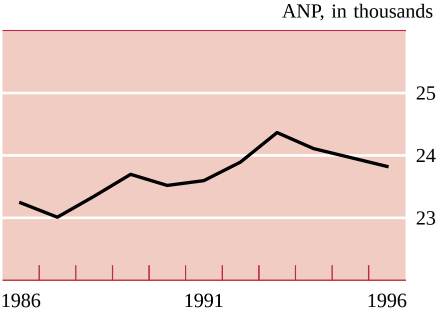
Operating Expenses of the Federal Reserve Banks, 1986–96[1]



1. Excludes expenses for special projects. For 1995, estimate; for 1996, budget.
2. Calculated with the GDP price deflator.

Chart 3.2

Employment at the Federal Reserve Banks, 1986–96[1]



1. Includes staff for special projects and FRAS. For 1995, estimate; for 1996, budget. See text note 2 for definition of ANP.

(297 ANP), securities and noncash operations (204 ANP), the ACH and funds transfer services (225 ANP), fiscal agency services (192 ANP), and the monetary policy service (55 ANP). These decreases are due largely to consolidation of operations and to operational efficiencies throughout the System.

Over the five years ending with the 1996 budget, Reserve Bank operating expenses have increased an average of 5.7 percent a year. Increases have been higher since 1991 because of expanded bank supervision and the transition to a consolidated data processing environment. Nonpersonnel costs have been increasing at a much faster rate than personnel costs as the Reserve Banks downsize labor-intensive operations and substitute technology for labor: Since 1991, nonpersonnel expenses have grown an average of 6.9 percent a year, and personnel expenses an average of 5.0 percent a year.

Over the five years, increases have been highest for the supervision and regulation operational area—an average of 12.7 percent a year—as the area continues to expand. Expenses for services to the U.S. Treasury and other government agencies have increased at the five-year average of 5.7 percent a year. Before 1993, when regionalization of savings bonds operations took place, the savings bond service accounted for the bulk of the annual increase for this operational area; since then, the consolidation of savings bonds processing sites has resulted in savings. The monetary and economic policy operational area has grown at an average rate of 5.1 percent a year, reflecting increases in overhead and support. The services to financial institutions and the public operational area has had the lowest average annual increase over the five years, 3.7 percent. Expenses for the currency service have grown an average of 12.0 percent a year, primarily because of installation of the currency processors, and expenses for public programs have grown an average of 8.4 percent a year. These increases have been partly offset by downsizing in the commercial check service due to volume declines and by centralization efforts in the funds transfer and ACH services.

About half of the expenses in the Reserve Banks' 1996 budget are recoverable through pricing or are reimbursable from the Treasury and other agencies. The proportion of recoverable expenses is down from 60 percent in 1991 because recoverable services have been growing at a slower rate than nonrecoverable services: Between 1991 and 1996, recoverable services have grown an average of 2.2 percent a year, and nonrecoverable services an average of 10.1 percent a year.

Volume and Unit Costs

In 1996, the volume of measured services as a whole is expected to increase 2.1 percent over 1995 volume, and the unit cost is expected to increase 0.8 percent (table 3.13). Since 1991, volume has increased at an average

Table 3.13

Volume and Unit Costs of Measured Federal Reserve Bank Services

Percentage change from 1995 to 1996

Service	Volume	Unit cost
Payments	3.0	–2.2
Commercial check	.7	.0
Automated clearinghouse	16.1	–14.7
Funds transfer	2.9	–4.4
Other checks	.9	7.0
Cash [1]	3.9	6.5
Fiscal	–6.1	4.8
Securities and noncash	3.4	–1.8
All measured services	**2.1**	**.8**

1. Includes currency and coin services.

annual rate of 1.9 percent and unit cost at an average annual rate of 1.5 percent. The increase in unit cost expected for 1996 reflects a net decrease for the payments services. For the commercial check service, the largest component of the overall index, the unit cost is expected to remain essentially flat, and for the cash service, the second largest component, to increase 6.5 percent.

1995 Budget Performance

The Reserve Banks estimate that 1995 expenses were $1,873.6 million—$4.3 million, or 0.2 percent, over the approved budget. At this estimated level of spending, the increase over actual 1994 spending on operations was 4.3 percent.

Seven Reserve Banks expect to be within 1.0 percent of their approved 1995 budgets. Three Banks expect overruns of 1.0 percent or more—Cleveland (2.2 percent), Minneapolis (1.4 percent), and San Francisco (1.0 percent). Major factors in Cleveland's overrun were higher-than-expected costs for Fednet and FRAS production and unbudgeted accounting changes related to the GAAP compliance initiative; in Minneapolis, the most significant reason for the overrun was the GAAP accounting changes; and in San Francisco, backlogs during transition to the new currency processing equipment required the addition of unbudgeted resources. Two Banks expect underruns of more than 1.0 percent—Atlanta (2.0 percent) and Boston (1.2 percent). Atlanta's expenses were lower in 1995 because of the recognition of credits for self-insured medical related to the GAAP compliance initiative; Boston's expenses were lower because the cost of transporting checks within the System, a Systemwide cost included in Boston's budget, was lower than expected. ▪

Chapter 3

Federal Reserve Banks

The 1997 budgets for the twelve Reserve Banks approved by the Board of Governors total $2,031.9 million, an increase of $34.2 million, or 1.7 percent, over estimated 1996 expenditures (table 3.1). Excluding the cost of the Automation Consolidation special project ($34.7 million), the Reserve Banks' 1997 operating budgets total $1,997.2 million, an increase of $37.9 million, or 1.9 percent.[1]

Employment, including the staff associated with FRAS, is budgeted at 23,258 ANP (average number of personnel), a decrease of 335 ANP, or 1.4 percent, from estimated 1996 employment.[2] Reserve Bank employment is expected to decline by 292 ANP, and FRAS employment by 43 ANP.

Expenses for personnel account for $1,252.3 million, or 63 percent of the 1997 operations budget, an increase of $24.3 million, or 2.0 percent, over estimated 1996 personnel expenses (table 3.2). Nonpersonnel expenses (mainly for building and automation projects) are budgeted at $744.9 million, an increase of $13.6 million, or 1.9 percent, over estimated 1996 nonpersonnel expenses.

The following two sections discuss major projects and the budget objective for the Reserve Banks in 1997. Subsequent sections provide details for the four operational areas as well as for objects of expense, capital outlays, and long-term trends. Appendix A gives more information on capital outlays, the special project, and other special categories of expense, and appendix D gives additional data by Federal Reserve District and operational area.

Major Projects

The 1997 Reserve Bank budgets provide for the following major projects (table 3.3):

- Installation of new high-speed currency processors
- Installation of equipment and software to support image processing of commercial and government checks
- Building construction programs
- Office automation and upgrading of local area networks
- Reengineering programs
- Consolidation of data processing and data communications.

The ongoing project to replace older-generation currency processors that have been in use since 1978 with new high-speed processors is adding $40.7 million to the 1997 operations

1. The budget for the Automation Consolidation special project includes transition expenses associated with the move to a centralized environment and expenses for FRAS (Federal Reserve Automation Services, the unit responsible for consolidated data processing and data communications for the Reserve Banks). FRAS charges to the Automation Consolidation special project in 1997 are budgeted at $24.5 million.

2. *Average number of personnel* (ANP) is a measure of the number of employees in terms of full-time equivalents for the time period. For instance, a full-time employee who starts work on July 1 counts as 0.5 ANP for that calendar year; two half-time employees who start on January 1 count as 1 ANP. Because the Reserve Banks carry calculations related to employment to two decimal places but employment in this volume is expressed in whole numbers, rounding error may result in slight discrepancies in employment figures among the tables and charts in this volume.

budget, an increase of $0.9 million over estimated 1996 expenditures. This project is in its final phase, and the last of the new processors will be installed in early 1997. In addition to the new processors, the project provides for the installation of reconciliation stations, sensors and detectors, and upgraded software to accommodate the newly designed currency. Of the total, $0.8 million is associated with software upgrades, approximately the same amount as was budgeted for 1996.

Expenses for the ongoing check-imaging project are budgeted at $15.8 million, an increase of approximately $10.8 million over estimated 1996 expenditures. The budget increase for 1997 is associated with additional equipment depreciation and maintenance, software amortization, and related programming and data processing requirements for both commercial and government check processing. Approximately 40 percent of the funds are earmarked for a government check-imaging project requested by the U.S. Treasury whereby the Federal Reserve will begin to provide image-supported check truncation services to the Treasury in early 1997. Also, in keeping with the System's effort to expand the electronic delivery of check services, many Reserve Banks plan to offer imaging of commercial checks to depository institutions and are upgrading sorters and check-processing control software to make them image-capable.

Table 3.1

Expenses and Employment at the Federal Reserve Banks, 1996 and 1997[1]

Category	1996 estimate	1997 budget	Change	
			Amount	Percent
Expenses (millions of dollars)				
Operations[2]	1,959.3	1,997.2	37.9	1.9
Special project	38.4	34.7	–3.7	–9.7
Total	**1,997.7**	**2,031.9**	**34.2**	**1.7**
Employment (average number of personnel)[3]				
Operations[2]	23,001	22,709	–292	–1.3
FRAS	592	549	–43	–7.3
Total	**23,593**	**23,258**	**–335**	**–1.4**

1. Excludes capital outlays.
2. Includes support and overhead (see appendix D, table D.3, note 1, for definitions).
3. See text note 2 for definition of average number of personnel.

Table 3.2

Operating Expenses of the Federal Reserve Banks, by Object, 1995–97[1]

Millions of dollars, except as noted

Object	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Personnel	1,183.5	1,228.0	1,252.3	3.8	2.0
Nonpersonnel	681.2	731.3	744.9	7.4	1.9
Total	**1,864.7**	**1,959.3**	**1,997.2**	**5.1**	**1.9**

1. Excludes special projects.

A total of $15.1 million has been budgeted for Board-approved building projects in Cleveland and Minneapolis, an increase of $10.9 million over estimated 1996 expenditures.

Office automation projects are adding an additional $3.2 million to the 1997 budget. Two Reserve Banks have identified plans to improve their local area networks (LANs) by improving the existing infrastructure and addressing backup and contingency needs; these projects account for $2.0 million of the 1997 increase. Another Bank has budgeted $1.2 million to convert the District's paper-based filing system to electronic images.

Several Reserve Banks are projecting savings, totaling $9.7 million and 168 ANP, associated with reengineering projects (efforts to restructure business processes) and other operational improvements. While three Districts have identified initiatives to pursue opportunities to improve operations and reduce expenses, one District's projections are driving the savings. New York's reengineering program is expected to reduce expenses by $7.8 million and 130 ANP below estimated 1996 levels. A significant portion of these savings is due to the closing of the Jericho, New York, check-processing facility in October 1996.

Reserve Bank data processing and data communications operations have been consolidated at FRAS. Charges to the Reserve Banks by FRAS for these two services are expected to decrease $6.9 million, or 4.3 percent, from estimated 1996 charges. The reduction is due to an overall cost reduction anticipated by FRAS as it moves closer to a steady-state environment.

1997 Budget Objective

In 1996 the Board approved a 1997 Reserve Bank budget objective that provided for an increase in total expenses, including special projects, of $64.3 million, or 3.2 percent, over estimated 1996 expenditures. Excluding special project expenses, which were expected to decrease in 1997, the increase was projected to be 3.5 percent. The Board anticipated that within this guideline, expenses for continuing

Table 3.3
Major Federal Reserve Bank Projects, 1997

Million of dollars, except as noted

Project	1996 estimate	1997 budget	Change, 1996 to 1997	Contribution to total 1997 change in operations budget (percentage points)
Currency processors	39.8	40.7	.9	*
Check imaging projects	5.0	15.8	10.8	.6
Building construction programs	4.2	15.1	10.9	.6
Office automation/LAN upgrades	5.2	8.4	3.2	.2
Reengineering programs	. . .	–9.7	–9.7	–.5
FRAS production charges	159.7	152.8	–6.9	–.4
Total	**213.9**	**223.1**	**9.2**	**.5**
Memo				
Total operating expenses	1,959.3	1,997.2	37.9	1.9

* Less than 0.05.

Table 3.4
Contribution to Total 1997 Change in Reserve Bank Operations Budget

Percentage points

Item	Budget objective	Approved budget
Continuing operating expenses	2.6	1.1
Major projects	.9	.8
Total excluding special project	**3.5**	**1.9**
MEMO		
Special project	–.3	–.2
Total including special project	**3.2**	**1.7**

Reserve Bank operations (including the impact of an overall savings target of $19.0 million) would increase 2.6 percent over estimated 1996 expenditures. Two major projects, check imaging and installation of new currency processors, were expected to account for $18.0 million of the projected 1997 increase, and another project, building construction in two Districts, for $8.3 million. Partly offsetting these increases would be a decrease of $8.7 million due to lower FRAS production charges, for a net increase of $17.6 million. Table 3.4 compares the 1997 budget objective with the approved 1997 budget.

The 1997 increase for continuing Reserve Bank operations (when the savings target is included) is $28.5 million less than anticipated in the budget objective. The increase is less than the 2.6 percent target, by 1.5 percentage points, for two main reasons: Expenses for merit pay programs are budgeted at 1.2 percentage points less than projected (3.0 percent vs. 4.2 percent), and expenses for retirement and other benefits are budgeted at 2.5 percentage points less than projected (1.7 percent vs. 4.2 percent).

Major Reserve Bank projects are expected to contribute $6.3 million less than the target approved by the Board. The decrease is due largely to a $6.7 million decrease in costs for the currency-processing project resulting from a financial accounting change that extended the useful life of the equipment and to the renegotiation of the maintenance contract.

Offsetting the expected lower costs for the currency-processing project are higher-than-expected costs for building construction, which is adding $10.9 million to the budget instead of the $8.3 million anticipated in the budget objective. The increase over the budget objective is due primarily to the inclusion in the

Table 3.5
Operating Expenses of the Federal Reserve Banks, by Operational Area, 1995–97[1]

Thousands of dollars, except as noted

Operational area	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Monetary and economic policy	128,303	138,143	145,693	7.7	5.5
Services to the U.S. Treasury and other government agencies	216,790	217,200	213,090	.2	–1.9
Services to financial institutions and the public	1,127,320	1,177,565	1,194,002	4.5	1.4
Supervision and regulation	392,294	426,385	444,431	8.7	4.2
Total	**1,864,707**	**1,959,294**	**1,997,216**	**5.1**	**1.9**

1. Includes the costs of support and overhead (see appendix D, table D.3, note 1, for definitions). Excludes special projects.

budget of real estate taxes for the new buildings in Minneapolis and Cleveland, the amounts for which were unknown at the time the budget objective was established. Also, FRAS production charges are declining less than anticipated in 1997 because a larger portion of expected long-term savings was realized in 1996.

The 1997 budget objective for the Automation Consolidation special project was $33.0 million. The budgeted amount is $34.6 million, somewhat more than the target but considerably less than estimated 1996 expenditures. Contributing to the 1997 budget are charges to the special project of $10.0 million by the New York Reserve Bank and $24.5 million by FRAS.

Budget by Operational Area

Tables 3.5 and 3.6 summarize expenses and employment for the Reserve Banks' four operational areas. Tables 3.7 through 3.11 give details.

Monetary and Economic Policy

The 1997 budget for the monetary and economic policy operational area is

Table 3.6

Employment at the Federal Reserve Banks, by Activity, 1995–97[1]

Average number of personnel, except as noted[2]

Activity	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Operational areas					
Monetary and economic policy	737	728	731	–1.3	.5
Services to the U.S. Treasury and other government agencies	1,683	1,566	1,524	–7.0	–2.7
Services to financial institutions and the public	8,209	8,099	7,851	–1.3	–3.1
Supervision and regulation	3,074	3,126	3,100	1.7	–.8
Support and overhead[3]					
Support	4,511	4,531	4,540	.4	.2
Overhead	4,949	4,952	4,963	.1	.2
Total	**23,162**	**23,001**	**22,709**	**–.7**	**–1.3**

1. Excludes special project and FRAS ANP.
2. See text note 2 for definition of average number of personnel.
3. See appendix D, table D.3, note 1, for definitions.

Table 3.7

Expenses of the Federal Reserve Banks for Monetary and Economic Policy, 1995–97[1]

Thousands of dollars, except as noted

Service	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Economic policy determination	100,616	108,864	113,805	8.2	4.5
Open market trading	27,687	29,279	31,887	5.8	8.9
Total	**128,303**	**138,143**	**145,693**	**7.7**	**5.5**

1. Excludes special projects.

$145.7 million, an increase of $7.5 million, or 5.5 percent, over estimated 1996 expenditures. The increase is due to merit pay increases, higher charges by FRAS, and higher costs for centralized end-user automation related to enhancing client-server platforms. The staffing level is increasing by 3 ANP, or 0.5 percent, over estimated 1996 employment, mainly because of the full-year impact of filling positions that were vacant during part of 1996.

Services to the U.S. Treasury and Other Government Agencies

The 1997 budget for services to the U.S. Treasury and other government agencies of $213.1 million is $4.1 million, or 1.9 percent, below estimated 1996

Table 3.8

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies, 1995–97[1]

Thousands of dollars, except as noted

Service	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Centralized operations—savings bonds	70,240	69,525	63,019	–1.0	–9.4
Other Treasury issues	22,493	21,855	14,412	–2.8	–34.1
Centralized operations—other Treasury issues	2,394	1,970	1,950	–17.7	–1.0
Centrally provided Treasury and agency services	29,552	26,343	34,348	–10.9	30.4
Government accounts	34,186	37,016	33,209	8.3	–10.3
Food coupons	24,202	25,789	26,659	6.6	3.4
Other	33,724	34,702	39,493	2.9	13.8
Total	**216,790**	**217,200**	**213,090**	**.2**	**–1.9**

1. Excludes special projects.

Table 3.9

Expenses of the Federal Reserve Banks for Services to Financial Institutions and the Public, 1995–97[1]

Thousands of dollars, except as noted

Service	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Currency	224,729	246,513	248,101	9.7	.6
Coin	26,803	28,921	29,264	7.9	1.2
Special cash	5,155	5,600	4,943	8.6	–11.7
Commercial check	519,337	541,943	540,375	4.4	–.3
Other check	38,656	37,887	41,876	–2.0	10.5
Funds transfer	68,361	62,001	68,352	–9.3	10.2
Automated clearinghouse	83,879	78,917	76,940	–5.9	–2.5
Book-entry securities transfer	38,338	37,396	38,972	–2.5	4.2
Other securities and noncash collection	7,710	8,041	7,201	4.3	–10.5
Loans to member banks and others	20,595	22,037	23,019	7.0	4.5
Public programs	64,159	74,184	78,313	15.6	5.6
Other	29,598	34,125	36,647	15.3	7.4
Total	**1,127,320**	**1,177,565**	**1,194,002**	**4.5**	**1.4**

1. Excludes special projects.

expenditures. The reduction is due mainly to staff reductions and lower charges by FRAS. These reductions are being partly offset by higher costs due to merit pay increases and for software being developed for the Treasury. Employment is projected to be 42 ANP, or 2.7 percent, lower than estimated 1996 employment. Staffing levels are being reduced in nearly all services. Staffing is declining by 15 ANP for the government accounts service as a result of anticipated lower volume associated with new tax filing requirements and by 10 ANP for the food coupon service as a result of expanded debit card programs. Reductions for other services are resulting from reengineering efforts in several Districts.

Services to Financial Institutions and the Public

Expenses for providing services to financial institutions and the public are budgeted at $1,194.0 million, an increase of $16.4 million, or 1.4 percent, over estimated 1996 expenditures. The budget for priced services is up $5.5 million, or 0.8 percent, over estimated 1996 expenditures, and the budget for nonpriced services is up $10.9 million, or 2.2 percent. Staffing is budgeted to decline by 248 ANP, or 3.1 percent, from estimated 1996 employment. Reductions are occurring in both priced and nonpriced services, including a decline of 173 ANP for the commercial check service due to the closing of the Jericho, New York, check-processing facility and improved efficiency at several Banks; a decline of 40 ANP resulting from efficiency gains as experience with the new currency processors increases; and a decline of 13 ANP for the ACH and funds transfer services due to improved efficiency resulting from the transition to centralized applications at FRAS. Partly offsetting these reductions are projected staff increases for public programs (21 ANP) in support of efforts to raise the Banks' visibility, improve the communication of economic policy, and expand community outreach programs.

Expenses for the commercial check and other check services are increasing $2.4 million, or 0.4 percent, over estimated 1996 expenses. Offsetting the

Table 3.10

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies and to Financial Institutions and the Public, 1995–97[1]

Thousands of dollars, except as noted

Service	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
U.S. government services[2]	310,061	303,893	301,119	–2.0	–.9
Cash services	251,532	275,434	277,365	9.5	.7
Priced services	668,166	685,092	690,630	2.5	.8
Other	114,351	130,346	137,978	14.0	5.9
Total	**1,344,109**	**1,394,765**	**1,407,093**	**3.8**	**.9**

1. Excludes special projects

2. The Federal Reserve Banks also incur some expenses for the provision of services to the U.S. government that are recorded in the monetary and economic policy operational area. These expenses for 1995 were $647 thousand, bringing the total cost of services provided to U.S. government agencies by the Reserve Banks as fiscal agents and depositories of the United States to $310,708 thousand.

savings associated with the staff reductions described above are greater expenses for the check-imaging project ($5.3 million for commercial checks and $5.5 million for government checks). Also increasing is the budget for the interdistrict transportation system (ITS), a result of network enhancements, higher fuel costs, and new contracts. The volume of commercial checks processed (including return items) is projected to increase 1.6 percent, with projections for individual Districts ranging from a decline of 2.4 percent to an increase of 7.8 percent. The volume of government checks processed is projected to decline 1.1 percent.

Expenses for the funds transfer service are budgeted to increase $6.4 million, or 10.2 percent, over estimated 1996 expenditures, primarily because of higher charges by FRAS resulting from a change in the way data processing and data communications costs are redistributed ($7.0 million). Expenses for the ACH service are budgeted to decrease $2.0 million from estimated 1996 expenditures; reductions due to a decline in the staffing level (11 ANP) and lower software development costs are being partly offset by increased data processing and data communications expenses associated with the change in the FRAS cost accounting methodology.

Supervision and Regulation

The 1997 budget for the supervision and regulation operational area is $444.4 million, an increase of $18.0 million, or 4.2 percent, over estimated 1996 expenditures. Changes in individual Reserve Bank budgets vary considerably from District to District and range from a decline of 4.2 percent to an increase of 14.2 percent. Overall, direct expenses are increasing 2.7 percent, mainly because of merit pay increases, more travel due to an increased number of foreign examinations, and greater expenses for equipment and software associated with a Systemwide effort to standardize and upgrade PC equipment and software. Support expenses are increasing 10.6 percent because of automation projects and higher occupancy costs. The staffing level is budgeted to decrease by 26 ANP, or 0.8 percent, from the estimated 1996 level; reductions associated with the supervision of District financial institutions are being partly offset by a slight increase associated with consumer affairs examinations.

Table 3.11

Expenses of the Federal Reserve Banks for Supervision and Regulation, 1995–97[1]

Thousands of dollars, except as noted

Service	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Supervision of District financial institutions	234,029	251,974	263,526	7.7	4.6
Consumer affairs	37,257	44,884	48,617	20.5	8.3
Administration of laws and regulations related to banking	102,329	108,858	111,138	6.4	2.1
Studies of banking and financial market structures	18,679	20,669	21,151	10.7	2.3
Total	**392,294**	**426,385**	**444,431**	**8.7**	**4.2**

1. Excludes special projects.

Budget by Object of Expense

Personnel expenses—officer and employee salaries, other compensation to personnel, and retirement and other benefits—account for 63 percent of Reserve Bank operating expenses budgeted for 1997. The amount budgeted is 2.0 percent more than estimated 1996 personnel expenses (table 3.12).

Salaries and other personnel expenses, which account for 49 percent of budgeted 1997 operating expenses, are expected to be $20.0 million, or 2.1 percent, greater than estimated 1996 expenses. Salaries for officers and employees are budgeted to increase $23.1 million, or 2.5 percent. Contributing to the increase are merit increases (3.0 percent of salary liability, or $28.6 million), promotions and reclassifications ($8.5 million), and structure adjustments ($0.8 million). Partly offsetting these increases are a reduction in overtime ($5.1 million), lower expenses resulting from short-term position vacancies or lag ($6.2 million), and a decline in the staffing level of 292 ANP ($3.7 million). The decrease in "other" personnel expenses ($3.1 million) is due to a decline in the use of outside agency help.

Expenditures for retirement and other benefits, which account for 14 percent of budgeted 1997 operating expenses, are expected to increase $4.4 million, or 1.7 percent, over estimated 1996 expenses. Benefits tied to salaries, such as social security payments and thrift plan contributions, are budgeted to increase 2.4 percent, and costs related to health care for active employees and retirees are budgeted to increase 1.0 percent. Other benefit expenses are increasing 0.9 percent.

Nonpersonnel expenses, which account for 37 percent of Reserve Bank operat-

Table 3.12

Operating Expenses of the Federal Reserve Banks, by Object, 1995–97[1]

Thousands of dollars, except as noted

Object	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
PERSONNEL					
Officers' salaries	94,919	100,585	106,026	6.0	5.4
Employees' salaries	803,188	837,473	855,118	4.3	2.1
Other personnel[2]	33,895	26,694	23,565	–21.2	–11.7
Retirement and other benefits	251,543	263,230	267,624	4.6	1.7
Total personnel	1,183,545	1,227,982	1,252,332	3.8	2.0
NONPERSONNEL					
Forms and supplies	58,788	58,847	57,684	.1	–2.0
Equipment	152,027	164,683	180,534	8.3	9.6
Software	28,396	34,630	39,393	22.0	13.8
Shipping	78,067	79,028	79,932	1.2	1.1
Travel	45,463	46,728	45,229	2.8	–3.2
Buildings	156,610	167,163	176,000	6.7	5.3
Recoveries	–51,306	–52,069	–53,031	1.5	1.8
Other[3]	213,119	232,302	219,144	9.0	–5.7
Total nonpersonnel	681,162	731,312	744,884	7.4	1.9
Total	**1,864,707**	**1,959,294**	**1,997,216**	**5.1**	**1.9**

1. Excludes special projects.
2. Expenses for certain contractual arrangements, and miscellaneous personnel expenses.
3. Communications, fees, contra-expenses, shared costs distributed and received, excess capacity, and other.

ing expenses budgeted for 1997, are projected to increase 1.9 percent over estimated 1996 nonpersonnel expenses.

Expenditures for equipment are expected to increase $15.9 million, or 9.6 percent, accounting for 9 percent of budgeted 1997 operating expenses. Depreciation and maintenance costs are increasing for equipment related to major Reserve Bank projects, including check-imaging equipment and upgraded local area networks and end-user computing equipment. Expenses are also increasing as a result of depreciation on upgraded check-processing equipment, document-imaging equipment, and telephone and voice response upgrades.

Shipping expenses, which account for 4 percent of budgeted 1997 operating expenses, are expected to increase $0.9 million, or 1.1 percent, mainly because of increased costs for the ITS network associated with new contracts, enhancements to the network, and the reinstatement of the federal airplane fuel user fee.

Building expenses, which account for 9 percent of budgeted 1997 operating expenses, are expected to increase $8.8 million, or 5.3 percent. The increase is due partly to increased property depreciation subsequent to building improvements and renovations ($3.6 million) and to increased real estate taxes ($6.1 million) associated with building projects and with one-time credits in 1996 in two Districts for earlier overpayments. Also, the Cleveland Reserve Bank has budgeted an additional $1.5 million for rent while its main building is being renovated.

‘‘Other’’ nonpersonnel expenses are budgeted to decrease $13.2 million from estimated 1996 expenses, accounting for 11 percent of budgeted 1997 operating expenses. The decrease is due mainly to lower charges by FRAS for data processing and data communications services and to a reduction in fees paid to outside consultants.

Expenditures for foreign travel are budgeted at $4.2 million, or 0.2 percent of budgeted 1997 operating expenses. The increase of $0.6 million, or 15 percent, over estimated 1996 expenses is due largely to increased travel associated with the examination of foreign banks.

Capital Outlays

Capital outlays for 1997 are budgeted at $346.4 million, a decrease of $21.7 million, or 5.9 percent, from estimated 1996 expenses (table 3.13). The budget includes FRAS capital outlays of $32.4 million, an increase of $5.2 million, or 19.2 percent, over estimated 1996 expenses. The budgets of ten of the twelve Reserve Banks are below estimated 1996 outlays.

Building projects will continue to dominate the Reserve Banks’ capital budget over the next few years, with outlays for buildings budgeted at $120.9 million, accounting for about 35 percent of total capital outlays budgeted for 1997. Included are funds for building projects in Minneapolis ($26.2 million), Atlanta ($5.5 million), and Birmingham ($8.3 million) and funds for building renovation and a new operations center in Cleveland ($44.0 million). Several major building refurbishment projects totaling approximately $36.9 million are under way or planned for 1997, including a floor-by-floor renovation of the New York Reserve Bank building ($7.9 million).

The building in Minneapolis will be ready for occupancy in July 1997, and occupancy of the operations center in Cleveland adjacent to the existing building is scheduled to begin in early 1997. Renovation of the existing Cleveland building is scheduled for completion in 1998, and the building programs in Atlanta and for the Birmingham Branch should be completed around the end of the century.

Outlays for data processing and data communications equipment, budgeted at $109.4 million, account for approximately 32 percent of capital outlays budgeted for 1997. Included in the budget is $22.9 million for input devices, mainly personal computers and peripherals. More than $14.0 million is earmarked for CPU equipment, largely for equipment at FRAS ($10.7 million), including the acquisition of two processors ($5.8 million), the upgrading of five processors ($3.0 million), and the renewal of leases on two processors ($1.9 million). The other significant CPU outlay ($2.2 million) is related to government check operations in the Atlanta District. Storage devices account for $12.4 million in the 1997 budget, including $4.2 million for equipment at FRAS and $7.7 million for government check image archive equipment. Other major data processing and data communications outlays budgeted for 1997 include $10.9 million for LAN equipment to replace existing equipment and to upgrade equipment in several Districts and $9.1 million for check operations equipment unrelated to image services, mainly for replacement of medium- and high-speed sorters. The remaining data processing and data communications outlays include $3.1 million for telephone systems and $3.0 million for printers. In addition, FRAS has budgeted $10.3 million for network operations equipment. Upgrading of backbone equipment ($2.6 million) and data transport node (DTN) equipment ($3.4 million) and expenditures on access equipment ($3.0 million) will provide increased service levels and support for new customers. FRAS has also budgeted $1.5 million for parallel sysplex equipment to help manage workloads more efficiently.

These figures reflect the $16.7 million budgeted for check-imaging equipment, including $7.6 million for the image archive and retrieval system and related equipment for government checks and

Table 3.13

Capital Outlays of the Federal Reserve Banks, by Class of Outlay, 1995–97

Thousands of dollars, except as noted

Class of outlay	1995 actual	1996 estimate	1997 budget	Percentage change	
				1995 to 1996	1996 to 1997
Data processing and data communications equipment[1]	97,474	97,528	109,414	.1	12.2
Buildings	89,086	110,951	120,864	24.5	8.9
Furniture, furnishings, and fixtures	11,991	23,098	35,412	92.6	53.3
Other equipment[2]	77,360	81,135	28,578	4.9	–64.8
Land and other real estate	22,580	7,985	7,333	–64.6	–8.2
Building machinery and equipment	7,550	28,510	28,614	277.6	.4
Leasehold improvements	1,160	2,655	2,190	128.8	–17.5
Software[3]	6,955	16,249	14,038	133.6	–13.6
Total	**314,156**	**368,112**	**346,444**	**17.2**	**–5.9**

1. Includes FRAS capital of $38,826 thousand in 1995, $23,556 thousand in 1996, and $27,557 thousand in 1997.

2. Includes FRAS capital of $2,884 thousand in 1995, $107 thousand in 1996, and $0 in 1997.

3. Includes FRAS capital of $2,440 thousand in 1995, $3,503 thousand in 1996, and $4,812 thousand in 1997.

$9.1 million for image-enabled sorters and other equipment for commercial checks.

Purchases of furniture and other equipment are budgeted at $64.0 million, or about 18 percent of total capital outlays. The continuing installation of high-speed currency processors, reconciliation stations, and sensors and detectors and the upgrading of other equipment account for approximately 15 percent of the total ($9.3 million). Another $34.6 million is budgeted for new and replacement furniture and workstations associated mainly with the building projects in Cleveland and Minneapolis and the floor-by-floor renovation program in New York.

Building machinery and equipment outlays are budgeted at $28.6 million, or about 8 percent of total capital outlays. Included are items related to the building projects in Cleveland ($9.4 million) and Minneapolis ($1.6 million) and replacements and upgrades in several Districts, including chiller replacements and upgrades ($5.3 million) and elevator upgrades ($2.7 million).

Software purchases in 1997 are budgeted at $14.0 million. Check-image software accounts for about 35 percent of the total ($5.0 million). FRAS has budgeted $4.8 million for software associated mainly with the CPUs that will be upgraded. The New York Reserve Bank plans to replace its market data software ($0.8 million), and the Banks also plan to purchase software for accounts payable systems, check and adjustment systems, and personnel systems.

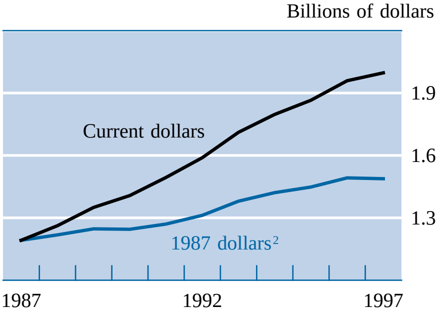
Land and other real estate expenses are budgeted at $7.3 million. The most significant outlay is associated with the building project in Birmingham ($3.1 million).

Trends in Expenses and Employment

Over the ten years ending with the 1997 budget, Reserve Bank expenses have increased an average of 5.3 percent a year (chart 3.1). Over the same period, employment at the Reserve Banks (including FRAS) has increased by 248 ANP, from 23,010 in 1987 to 23,258 in 1997 (chart 3.2). Since 1987, staff increases have occurred in supervision and regulation mainly because of implementation of the Federal Deposit

Chart 3.1

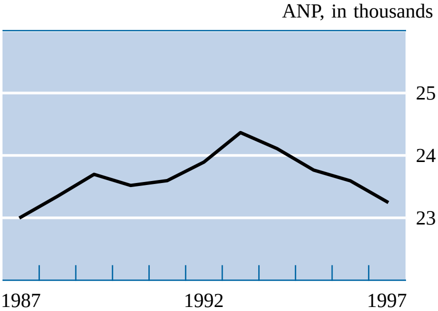
Operating Expenses of the Federal Reserve Banks, 1987–97[1]



1. Excludes expenses for special projects. For 1996, estimate; for 1997, budget.
2. Calculated with the GDP price deflator.

Chart 3.2

Employment at the Federal Reserve Banks, 1987–97[1]



1. Includes staff for special projects and FRAS. For 1996, estimate; for 1997, budget. See text note 2 for definition of ANP.

Insurance Corporation Improvement Act and the Community Reinvestment Act (952 ANP), in data services because of expanded automation requirements and the transition to consolidated processing at FRAS (444 ANP), in the currency service because of volume growth (80 ANP), and in public programs because of efforts to enhance consumer education and communications with the public (128 ANP). Partly offsetting these increases have been reductions in the commercial check service (610 ANP), the overhead services (61 ANP), the securities safekeeping and noncash services (184 ANP), the ACH and funds transfer services (270 ANP), services to the Treasury and other government agencies (312 ANP), and the monetary policy service (44 ANP). These staff reductions have been due largely to the consolidation of operations and increased operational efficiencies throughout the System.

The average annual growth of operating expenses has slowed in recent years and is projected to be 4.7 percent over the five years ending with the 1997 budget. Expanded bank supervision needs and the transition to a consolidated data processing and data communications environment at FRAS affected growth during this period. Mainly because of production charges from FRAS, nonpersonnel costs have been increasing at a faster rate than personnel costs—6.7 percent compared with 3.6 percent—as the Reserve Banks downsize labor-intensive and computer operations and substitute technology for labor. By operational area, expense increases over the five years have been highest for supervision and regulation (average annual increase of 10.0 percent), followed by monetary and economic policy (5.8 percent, reflecting increases in support and overhead services) and services to the Treasury and other government agencies and services to financial institutions and the public (both 3.2 percent). The slowing of growth in recent years has resulted from several offsetting factors. Expenses for the currency service have increased an average of 8.7 percent a year, primarily because of the installation of new currency processors, and expenses for public programs have risen an average of 8.8 percent a year. Partly offsetting these increases have been decreases due to downsizing in the commercial check service resulting from declining volume and to centralization efforts in the funds transfer and ACH services.

Just over half of the expenses in the Reserve Banks' 1997 budget (about 52 percent) are recoverable through revenues or are reimbursable by the Treasury and other government agencies. The proportion of recoverable expenses is down from the 58 percent that was recoverable in 1992 because recoverable services are growing at a slower rate than nonrecoverable services: Between 1992 and 1997, recoverable services have grown an average of 1.8 percent a year and nonrecoverable services an average of 7.5 percent a year.

Volume and Unit Costs

The volume of measured services in 1997 is expected to increase 1.4 percent over estimated 1996 volume, and the unit cost is expected to decrease 0.7 percent (table 3.14). Since 1992, volume has grown at an average annual rate of 1.6 percent and unit cost at an average annual rate of 0.9 percent. The decrease in unit cost between 1996 and 1997 reflects net decreases for the payments, cash, and fiscal services. Commercial checks, the largest component of the payments service (and of the overall index), anticipates a 2.4 percent decline in unit cost in 1997, and cash

Table 3.14

Volume and Unit Cost of Measured Federal Reserve Bank Services

Percentage change from 1996 to 1997

Service	Volume	Unit cost
Payments	1.9	–.8
Commercial check	1.6	–2.4
Funds transfer	4.2	5.8
Other checks	1.7	8.7
Cash [1]	1.6	–.7
Fiscal	1.8	–5.5
Securities and noncash	–7.0	9.1
All measured services	**1.4**	**–.7**

1. Includes currency and coin services.

services, the second largest component, a 0.7 percent decline.

1996 Budget Performance

In mid-1996 the Reserve Banks estimated that their expenses for the calendar year would be $1,959.3 million—$9.5 million, or 0.5 percent, less than the approved 1996 budget of $1,968.8 million. The 1996 budget approved by the Board in December 1995 represented an increase of $95.2 million, or 5.1 percent, over estimated 1995 expenses; at the estimated 1996 level of spending, the increase over actual 1995 expenditures would also be 5.1 percent.

Eight Reserve Banks expect to be under their approved 1996 District budgets, by as much as $3.0 million. The other four banks expect overruns of less than 1.0 percent, none more than $0.7 million. ■

Chapter 3

Federal Reserve Banks

The 1998 Reserve Bank operating budgets approved by the Board of Governors total $2,054.7 million, an increase of $43.1 million, or 2.1 percent, over estimated 1997 expenditures (table 3.1). Including the cost of the Automation Consolidation special project ($4.7 million), the Reserve Banks' 1998 budgets total $2,059.4 million, an increase of $13.1 million, or 0.6 percent.[1]

Employment, including the staff associated with FRAS (Federal Reserve Automation Services), is budgeted at 22,754 ANP (average number of personnel), a decrease of 467 ANP, or 2.0 percent, from estimated 1997 employment.[2] Reserve Bank employment is expected to decline by 516 ANP, and FRAS employment will increase by 49 ANP.

Expenses for personnel (salaries and benefits) account for $1,286.0 million or 63 percent of the 1998 operations budget, an increase of $20.7 million, or 1.6 percent, over estimated 1997 personnel expenses (table 3.2). Nonpersonnel expenses (mainly for building and automation projects) are budgeted at $768.7 million, an increase of $22.4 million, or 3.0 percent, over estimated 1997 nonpersonnel expenses.

The following two sections discuss major initiatives and the budget objective for the Reserve Banks in 1998. Subsequent sections provide details for the four operational areas as well as for objects of expense, capital outlays, and long-term trends. Appendix A gives more information on capital outlays, the special project, and other special categories of expense, and appendix D gives additional data by District and operational area.

Major Initiatives

The 1998 Reserve Banks budgets provide for the following initiatives (table 3.3):

System-defined
- Century date change compliance
- Installation of equipment and software to support image processing of commercial and government checks and archiving of the images
- Enhancements to high-speed currency processors

District-defined
- Office automation and upgrading of local area networks
- Reengineering programs

Contributing significantly to the 1998 operations budget are expenses associated with efforts to ensure century date change (CDC) compliance for all automated systems. The total cost of the CDC project in 1998 is expected to be $31.9 million and will involve 226 ANP.

1. The budget for the Automation Consolidation special project includes transition expenses associated with the move to a centralized environment and expenses for FRAS (Federal Reserve Automation Services, the unit responsible for consolidated data processing and data communications for the Reserve Banks). FRAS charges to the Automation Consolidation special project in 1998 are budgeted at $2.0 million.

2. The term *average number of personnel* describes levels and changes in employment at the Reserve Banks. ANP is the number of employees in terms of full-time positions for the time period. For instance, a full-time employee who starts work on July 1 counts as 0.5 ANP for that calendar year; two half-time employees who start on January 1 count as 1 ANP.

The majority of these costs ($22.8 million or 71 percent) represents a reallocation of current resources. The remaining incremental expense of $9.1 million is primarily for consulting services and contract programmers. The total CDC initiative includes $6.5 million and 52 ANP at FRAS; these expenses are reflected in the Reserve Bank budgets as FRAS charges for infrastructure.

Expenses for the ongoing check-imaging initiative are budgeted at $26.9 million, an increase of approximately $11.2 million over estimated 1997 expenditures. Approximately 45 percent of the funds are earmarked for a government check-imaging project, requested by the U.S. Treasury, whereby the Federal Reserve provides image-supported check truncation services to the Treasury. The plans also include funding for two additional government imaging services, EZ Clear Savings Bonds and Postal Money Orders.

In keeping with the System's effort to expand electronic delivery of check services, many Reserve Banks plan to expand the commercial check image services they offer to depository institutions and are upgrading sorters and check-processing control software to make them image-capable. The budget increase for 1998 is associated with

Table 3.1

Expenses and Employment at the Federal Reserve Banks, 1997–98

Category	1997 estimate	1998 budget	Change	
			Amount	Percent
Expenses (millions of dollars)				
Operations [1]	2,011.6	2,054.7	43.1	2.1
Special project	34.7	4.7	–30.0	–86.5
Total	**2,046.3**	**2,059.4**	**13.1**	**.6**
Employment (average number of personnel) [2]				
Operations [1]	22,672	22,156	–516	–2.3
Federal Reserve Automation Services	549	598	49	8.9
Total	**23,221**	**22,754**	**–467**	**–2.0**

NOTE. See general note to table 1.1, chapter 1. Excludes capital outlays.

1. Includes support and overhead (see appendix D, table D.3, note 1, for definitions).

2. See text note 2 for definition. The costs of the special project do not involve personnel.

Table 3.2

Operating Expenses of the Federal Reserve Banks, by Object, 1996–98

Millions of dollars except as noted

Object	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Personnel	1,236.6	1,265.3	1,286.0	2.3	1.6
Nonpersonnel	719.5	746.3	768.7	3.7	3.0
Total	**1,956.1**	**2,011.6**	**2,054.7**	**2.8**	**2.1**

NOTE. Includes support and overhead (see appendix D, table D.3, note 1, for definitions). Excludes special project.

additional equipment depreciation and maintenance, software amortization, and related programming and data processing for both commercial and government check processing. This initiative will also add 68 ANP in 1998, mainly in the New York, Philadelphia, Richmond, and Atlanta Districts to support imaging of commercial checks.

The initiative to enhance currency processors that have been installed over the last few year is budgeted at $2.9 million, an increase of $2.2 million over estimated 1997 expenditures. The enhancements to the currency processors will improve operating efficiency, automate processing functions, ensure CDC compliance, allow for currency design changes, and improve management information reporting.

Funding for office automation projects is projected to increase $3.0 million. Five Banks identified plans to improve their local area networks (LANs) by improving the existing infrastructure and addressing backup and contingency. Another Bank has budgeted funds to continue the conversion of the District's paper-based system to electronic images.

Several Reserve Banks are projecting savings, totaling $22.1 million and 280 ANP, associated with reengineering efforts—that is efforts to restructure business processes—and other operational improvements. Although the bulk of the savings are associated with Bankwide programs, three districts have identified specific cost reductions and realized efficiencies in their check operations. Reductions in the Supervision and Regulation examination staff are also contributing to cost savings and staff reductions.

1998 Budget Objective

In 1997 the Board approved a 1998 Reserve Bank budget objective that provided for an increase in total expenses, including special projects, of

Table 3.3

Contribution of Change in Major Initiatives to the Change in Operating Expenses of the Federal Reserve Banks, 1997 to 1998

Millions of dollars except as noted

Initiative	1997 estimate	1998 budget	Contribution of change to change in total operating expenses, 1997 to 1998	
			Amount	Percentage points
System-defined				
Century date change	14.4	31.9	17.5	.9
Check imaging	15.7	26.9	11.2	.6
Currency processors	.7	2.9	2.2	.1
District-defined				
Office automation and network upgrades	7.1	10.1	3.0	.1
Reengineering	. . .	–22.1	–22.1	–1.1
Total	**37.9**	**49.7**	**11.8**	**.6**
MEMO				
Other operating expenses	1,973.7	2,005.0	31.3	1.5
Total operating expenses	**2,011.6**	**2,054.7**	**43.1**	**2.1**

$24.9 million, or 1.2 percent above budgeted 1997 expenditures. Excluding expenses for a special project, which was expected to decrease in 1998, the increase was projected to be 2.8 percent. The Board anticipated that within this guideline expenses for ongoing Reserve Bank operations (including the impact of an overall savings target of $12.6 million) would increase 2.0 percent over budgeted 1997 expenditures. Expenses for three initiatives, century date change compliance, check imaging, and new currency processor enhancements, were expected to account for $16.6 million of the projected 1998 expenses. Table 3.4 shows the 1998 budget objective relative to the 1997 budget and the approved 1998 budget relative to estimated 1997 expenditures.

The 1998 increase for ongoing Reserve Bank operations (when the savings target is included) is $15.0 million less than anticipated in the budget objective. The increase is less than the 2.0 percent target, by 0.9 percentage point, for three main reasons: (1) lower-than-anticipated building expenses for the Cleveland and Minneapolis facilities projects; (2) 1997 expenses higher than budgeted because of unbudgeted costs for CDC compliance; unplanned one-time costs associated with closing the Lewiston office; unanticipated check write-offs; unbudgeted severance payments; and higher-than-planned use of outside agency help, primarily in the check and automation areas; and (3) savings greater than anticipated from various reengineering programs throughout the organization.

Spending on Reserve Bank initiatives is expected to be $3.1 million more than the target approved by the Board. The increase is due largely to a $5.5 million increase in costs for the check imaging initiative resulting from additional equipment requirements for this project because better information was available related to customer demands for commercial imaging products and the requirements for two additional services, EZ Clear Savings Bond and Postal Money Order image processing.

Offsetting the expected higher costs for the check imaging initiative are incremental costs for century date change efforts, which are $0.3 million less than projected, and costs associated with currency processor enhancements, which are $1.9 million less.

Both the 1998 budget objective and the 1998 Reserve Bank budget for the Automation Consolidation special project were $4.7 million. This project, which will be ending during 1998, is budgeted at $30.1 million less than in 1997.

Table 3.4

Change in Budget Objective and Budget of the Federal Reserve Banks, 1997 to 1998

Percent

Item	1998 budget objective[1]	1998 budget[2]
Operating expenses	2.0	1.1
System-defined initiatives[3]	.8	1.0
Total, excluding special project	2.8	2.1
Special project	–1.6	–1.5
Total, including special project	**1.2**	**.6**

1. As a change from 1997 budget.
2. As a change from 1997 estimated expenses.
3. Century date change, check imaging, and currency processors.

Budget by Operational Area

Tables 3.5 and 3.6 summarize employment and expenses for the Reserve Banks' four operational areas. Tables 3.7 through 3.11 give details for each area.

Monetary and Economic Policy

The 1998 budget for the monetary and economic policy operational area is $152.7 million, an increase of $8.0 million, or 5.5 percent, over estimated 1997 expenditures. The increase is due to merit pay increases, slightly higher staff levels, century date change initiatives, and higher FRAS and local automation costs. Local automation initiatives include expansion of distributed processing platforms and applications and the expansion of electronic services to the public, including electronic reference services. The staffing level is increasing by 4 ANP, or 0.6 percent, over estimated 1997 employment, mainly because of the full-year impact of filling positions that were vacant during part of 1997.

Services to the U.S. Treasury and Other Government Agencies

The 1997 budget for services to the Treasury and other government agencies of $220.9 million is $8.9 million,

Table 3.5

Employment at the Federal Reserve Banks, by Activity, 1996–98

Average number of personnel except as noted[1]

Activity	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Operational areas					
Monetary and economic policy	734	720	724	–2.0	.6
Services to the U.S. Treasury and other government agencies	1,542	1,469	1,397	–4.8	–4.8
Services to financial institutions and the public	8,083	7,958	7,773	–1.5	–2.3
Supervision and regulation	3,111	3,022	2,953	–2.9	–2.3
Support and overhead[2]					
Support	4,538	4,640	4,535	2.2	–2.3
Overhead	4,901	4,863	4,773	–.8	–1.9
Total	**22,909**	**22,672**	**22,156**	**–1.0**	**–2.3**

NOTE. Excludes Federal Reserve Automation Services. The costs of the special project do not involve personnel.

1. See text note 2 for definition.
2. See appendix D, table D.3, note 1, for definitions.

Table 3.6

Operating Expenses of the Federal Reserve Banks, by Operational Area, 1996–98

Thousands of dollars except as noted

Operational area	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Monetary and economic policy	138,649	144,712	152,699	4.4	5.5
Services to the U.S. Treasury and other government agencies	215,609	212,010	220,939	–1.7	4.2
Services to financial institutions and the public	1,177,444	1,214,810	1,226,243	3.2	.9
Supervision and regulation	424,402	440,025	454,791	3.7	3.4
Total	**1,956,104**	**2,011,557**	**2,054,672**	**2.8**	**2.1**

NOTE. Includes support and overhead (see appendix D, table D.3, note 1, for definitions); excludes special project.

or 4.2 percent, above estimated 1997 expenditures. Increased costs are due mainly to higher FRAS charges for Treasury and agency services, due primarily to the CDC compliance project, and continued efforts to automate and enhance Treasury-related systems. Employment is projected to be 72 ANP, or 4.8 percent, lower than estimated 1997 employment. Staffing levels are being reduced in all services. Over one-third of the reduction is associated with a 26 ANP reduction in the Food Coupon processing area, resulting from expanded Electronic Benefits Transfer programs. Reductions in other areas are the result of reengineering efforts in several districts.

Services to Financial Institutions and the Public

Expenses for providing services to financial institutions and the public are budgeted at $1,226.2 million, an increase of $11.4 million, or 0.9 percent, over estimated 1997 expenditures. The budget for priced services is declining $6.1 million, or 0.9 percent, over estimated 1997 expenditures, and the budget for nonpriced services is increasing $17.5 million, or 3.5 percent.

The Reserve Banks budgeted $26.9 million in 1998 to provide commercial check, postal money order, and Treasury check imaging services; funding for this project is $11.2 million

Table 3.7

Expenses of the Federal Reserve Banks for Monetary and Economic Policy, 1996–98

Thousands of dollars except as noted

Service	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Economic policy determination	109,040	114,419	120,478	4.9	5.3
Open market trading	29,609	30,293	32,221	2.3	6.4
Total	**138,649**	**144,712**	**152,699**	**4.4**	**5.5**

NOTE. Excludes special project.

Table 3.8

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies, 1996–98

Thousands of dollars except as noted

Service	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Centralized operations—savings bonds	67,888	62,395	64,625	–8.1	3.6
Other Treasury issues	22,065	14,862	16,278	–32.6	9.5
Centralized operations—other Treasury issues	2,112	1,790	1,488	–15.2	–16.9
Centrally provided Treasury and agency services	26,474	35,048	36,268	32.4	3.5
Government accounts	37,491	34,085	36,563	–9.1	7.3
Food coupons	25,002	25,922	26,588	3.7	2.6
Other	34,577	37,908	39,129	9.6	3.2
Total	**215,609**	**212,010**	**220,939**	**–1.7**	**4.2**

NOTE. Excludes special project.

higher than the 1997 estimate. Commercial check processed volume is projected to increase 3.4 percent, with individual district volume projections ranging from a decline of 1.8 percent to an increase of 9.1 percent. The volume for government checks processed is projected to decline 5.1 percent. Funding for BPS 3000 currency software enhancements is projected to be $2.9 million.

Staffing is budgeted to decline 185 ANP, or 2.3 percent, from estimated 1997 employment. Staff reductions are occurring in both priced and nonpriced services, including a decline of 89 ANP for the commercial check service due to extensive reengineering projects in several banks, and the closing of the Lewiston check processing facility. Staffing for ACH, Funds Transfer, and Book-Entry Securities services are

Table 3.9

Expenses of the Federal Reserve Banks for Services to Financial Institutions and the Public, 1996–98

Thousands of dollars except as noted

Service	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Currency	243,421	249,145	257,973	2.4	3.5
Coin	29,164	28,959	29,734	–.7	2.7
Special cash	5,117	4,765	2,481	–6.9	–47.9
Commercial check	547,674	569,115	570,549	3.9	.3
Other check	37,081	42,001	47,161	13.3	12.3
Funds transfer	62,507	68,643	64,930	9.8	–5.4
Automated clearinghouse	79,254	68,215	69,763	–13.9	2.3
Book-entry securities transfer	37,215	40,324	36,084	8.4	–10.5
Other securities and noncash collection	7,616	6,884	5,259	–9.6	–23.6
Loans to member banks and others	22,583	23,901	23,654	5.8	–1.0
Public programs	72,184	76,299	80,321	5.7	5.3
Other	33,628	36,559	38,334	8.7	4.9
Total	**1,177,444**	**1,214,810**	**1,226,243**	**3.2**	**.9**

NOTE. Excludes special project.

Table 3.10

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies and to Financial Institutions and the Public, 1996–98

Thousands of dollars except as noted

Service	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
U.S. government services[1]	303,395	301,413	306,309	–.7	1.6
Cash services	272,584	278,104	287,707	2.0	3.5
Priced services	690,744	713,115	707,001	3.2	–.9
Other	126,331	134,188	146,165	6.2	8.9
Total	**1,393,054**	**1,426,821**	**1,447,182**	**2.4**	**1.4**

NOTE. Excludes special project.

1. The amounts shown here do not include expenses in this service that are recorded in the monetary and economic policy operational area. For 1996, these expenses were $647 thousand; for 1997, they are estimated at $606 thousand; and for 1998, they are budgeted at $880 thousand. These expenses increase the total costs of services provided by the Reserve Banks as fiscal agents and depositories of the United States.

projected to decline by 29 ANP due to efficiencies gained as a result of the transition to FRAS centralized applications. Consolidation continues in the Noncash service; one office will provide all processing for the Banks. Expenses for the CDC compliance project will be $1.2 million greater than estimated 1997 expenditures.

Supervision and Regulation

The 1998 budget for the supervision and regulation operational area is $454.8 million, an increase of $14.8 million, or 3.4 percent, over estimated 1997 expenditures. Changes in individual Reserve Bank budgets vary considerably from District to District and range from a decline of 4.4 percent to an increase of 7.7 percent. Additional funding for market-based merit pay programs is partially offset by savings associated with staff reductions.

The supervision and regulation area continues to allocate resources toward enhancing distributed processing platforms and implementing new applications. Automation initiatives include expanding off-site access for examiners, automating resource tracking and scheduling functions, and implementing system software for examiner and consumer compliance applications.

The staffing level is budgeted to decrease by 69 ANP, or 2.3 percent, from the estimated 1997 level; reductions associated with the increased use of risk-based examinations, changes in examination frequency, and efficiencies gained through automation are partially offset by slight staff increases in three districts due to the full-year effect of filling positions that were vacant during part of 1997.

Table 3.11

Expenses of the Federal Reserve Banks for Supervision and Regulation, 1998

Thousands of dollars

Service	1998 budget
Supervision of large multistate, multi-District banking organizations	64,615
Supervision of domestic regional and community banking organizations	177,752
Supervision of foreign banking organizations	48,638
Administration of laws and regulations related to banking	95,758
Supervision activities benefiting the banking system	46,003
Studies of banking and financial markets	22,025
Total	**454,791**

NOTE. Excludes special project. The services in this operational area have been redefined for 1998, and thus the budgets for them cannot be compared with service budgets of previous years.

Budget by Object of Expense

Personnel expenses—officer and employee salaries, other compensation to personnel, and retirement and other benefits—account for 63 percent of Reserve Bank operating expenses budgeted for 1998. The amount budgeted is 1.6 percent more than estimated 1997 personnel expenses (table 3.12).

Salaries and other personnel expenses, which account for 49 percent of budgeted 1998 operating expenses, are expected to be $12.8 million, or 1.3 percent, greater than estimated 1997 expenses. Salaries for officers and employees are budgeted to increase $24.0 million, or 2.5 percent. Contributing to the increase are merit increases (4.0 percent of salary liability, or $36.6 million), promotions and reclassifications ($8.0 million), and market adjustments ($2.1 million). Partly offsetting these increases are a reduction in overtime ($6.2 million), lower expenses resulting from short-term position vacancies or lag ($5.6 million), and a decline in the staffing level of 516 ANP ($11.2 million). The decrease in other personnel expenses ($11.1 million) is due to a decline in the use of outside agency help and reduced severance and retention payments, partially offset by increased payments for cash awards and incentive-based programs.

Expenditures for retirement and other benefits, which account for 14 percent of budgeted 1998 operating expenses, are expected to increase $7.9 million, or 2.9 percent, over estimated 1997 expenses. Benefits tied to salaries, such as social security payments and thrift plan contributions, are budgeted to increase 2.2 percent, and costs for non-salary-related benefits, such as insurance and health care for active employees and retirees, are budgeted to increase 4.3 percent.

Nonpersonnel expenses, which account for 37 percent of Reserve Bank operating expenses budgeted for 1998, are projected to increase 3.0 percent over estimated 1997 expenditures.

Expenditures on equipment are expected to increase $10.3 million, or 5.9 percent, accounting for 9 percent of budgeted 1998 expenses. Depreciation and maintenance costs are increasing for equipment related to Reserve Bank initiatives, including check-imaging equipment and upgraded local area networks and end-user computing equipment. Expenses are also increasing as a result of depreciation on upgraded check-processing equipment, document-imaging equipment, dedicated systems for check adjustment and cash management, and upgraded telephone and voice response systems. These cost increases are partially offset by the planned release of the data processing mainframe computer in New York as the Bank completes the transition to FRAS.

Shipping expenses, which account for 4 percent of budgeted 1998 operating expenses, are expected to decrease $2.2 million, or 2.8 percent, mainly

Table 3.12
Operating Expenses of the Federal Reserve Banks, by Object, 1996–98

Thousands of dollars except as noted

Object	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Personnel					
Officers' salaries	100,161	104,955	109,957	4.8	4.8
Employees' salaries	834,913	853,070	872,021	2.2	2.2
Other[1]	34,151	38,548	27,433	12.9	–28.8
Retirement and other benefits	267,376	268,699	276,578	.5	2.9
Total	1,236,600	1,265,272	1,285,989	2.3	1.6
Nonpersonnel					
Forms and supplies	59,557	52,960	52,774	–11.1	–.4
Equipment	160,123	173,308	183,615	8.2	5.9
Software	32,726	37,128	36,940	13.5	–.5
Shipping	77,849	80,058	77,825	2.8	–2.8
Travel	44,931	45,059	42,848	.3	–4.9
Buildings	167,659	174,680	180,130	4.2	3.1
Recoveries	–52,319	–53,231	–56,619	1.7	6.4
Other[2]	228,978	236,323	251,169	3.2	6.3
Total	719,504	746,285	768,683	3.7	3.0
Total	**1,956,104**	**2,011,557**	**2,054,672**	**2.8**	**2.1**

NOTE. Excludes special project.

1. Certain contractual arrangements and miscellaneous other personnel expenses.

2. Communications, fees, contra-expenses, shared costs distributed and received, excess capacity, and miscellaneous other expenses.

because of the implementation of the Interdistrict Transportation network design changes in late 1997.

Within the travel budget, expenditures on foreign travel are budgeted at $3.9 million, or 0.2 per cent of total budgeted 1998 operating expenses. Decreased examiner travel associated with the examination of foreign banks is offset by an increase in foreign travel by bank staff supporting research efforts related to newly industrializing countries and emerging markets.

Building expenses, which account for 9 percent of budgeted 1998 operating expenses, are expected to increase $5.5 million, or 3.1 percent. The increase is driven by increased real estate taxes and property depreciation resulting from various building improvements, building renovations, and completion of the Minneapolis' new building and Cleveland's operations center.

Recoveries will increase by $3.4 million. Nearly half of this increase ($1.4 million) is the result of the Reserve Bank's 1998 implementation of the Uniform Cash Access policy.

"Other" nonpersonnel expenses are budgeted to increase $14.8 million from estimated 1997 expenses, accounting for 12 percent of budgeted 1998 operating expenses. The increase is due mainly to the Banks receiving higher production charges from FRAS for infrastructure, data processing, and data communications services. These increases are partially offset by decreased fees to consultants and lower check write-offs.

Capital Outlays

Capital outlays for 1998 are budgeted at $310.8 million, an increase of $26.1 million, or 9.2 percent, from estimated 1997 expenses (table 3.13). The budget includes FRAS capital outlays of $44.1 million, an increase of $11.1 million, or 33.8 percent, over estimated 1997 expenses. The budgets of six of the twelve Banks are below estimated 1997 outlays.

Table 3.13

Capital Outlays of the Federal Reserve Banks, by Class, 1996–98

Thousands of dollars except as noted

Class	1996 actual	1997 estimate	1998 budget	Percentage change	
				1996 to 1997	1997 to 1998
Data processing and data communications equipment[1]	81,580	107,573	126,583	31.9	17.7
Buildings	125,391	76,918	80,417	–38.7	4.5
Furniture, furnishings, and fixtures	16,934	26,814	25,303	58.3	–5.6
Other equipment[2]	73,449	27,433	16,196	–62.7	–41.0
Land and other real estate	7,107	8,518	2,323	19.9	–72.7
Building machinery and equipment	20,422	20,707	29,634	1.4	43.1
Leasehold improvements	1,542	1,368	14,695	–11.3	974.2
Software[3]	8,628	15,406	15,647	78.6	1.6
Total	**335,053**	**284,737**	**310,798**	**–15.0**	**9.2**
MEMO					
FRAS	19,714	33,004	44,146	67.4	33.8

1. For Federal Reserve Automation Services (FRAS), includes capital of $16,337 thousand in 1996, $28,725 thousand in 1997, and $39,465 thousand in 1998.

2. For FRAS, includes no outlay in 1996, $30 thousand in 1997, and $20 thousand in 1998.

3. For FRAS, includes $3,377 thousand in 1996, $4,249 thousand in 1997, and $4,661 thousand in 1998.

Outlays for data processing and data communications equipment, budgeted at $126.6 million, account for approximately 41 percent of capital outlays budgeted for 1998. Included in the budget is $38.4 million for the purchase of personal computers and to upgrade local area networks. Other significant outlays include $18.1 million for check imaging systems, check sorters, and related equipment, $10.4 million for central processing units (CPUs), storage devices, printers, and related equipment, and $12.8 million for various projects that include the replacement of systems in the Markets Group and Central Bank Services functions in New York and the purchase of a Counterfeit Catalogue and Retrieval system for the Currency Technology Office.

FRAS has budgeted $39.4 million for data processing and data communications equipment in 1998. Outlays for CPUs account for $14.3 million. The FRAS budget also includes $15.0 million for computer peripheral and desk top equipment and $10.1 million for data communications equipment to improve and expand FEDNET (the Federal Reserve System's communication network) and enhance its security.

Building outlays are budgeted at $80.4 million, an increase of $3.5 million from the 1997 estimate. Cleveland is budgeting $21.8 million for renovation of its head office. Atlanta's building budget is $17.5 million; the funds are primarily for long-term facilities initiatives, which include architectural and engineering fees for the Atlanta and Birmingham projects and funds to begin construction in Birmingham. Building renovation and modernization projects in New York total $18.5 million. San Francisco is budgeting $11.2 million, largely for renovation projects at all offices in the district. A variety of smaller building projects accounts for the remaining building outlays included in the 1998 budget. Leasehold improvements, budgeted at $14.7 million, are primarily associated with New York's plans to improve and occupy newly leased space adjacent to its main building.

Purchases of furniture and other equipment are budgeted at $41.5 million and account for about 13 percent of total capital outlays. The majority of the furniture and equipment included in the 1998 budget is associated with the various remodeling, renovation, and leasehold improvement projects that are occurring in most districts. Year-over-year expenses in this category are declining due to the completion of major construction projects in Minneapolis and Cleveland and the final installation of BPS 3000 currency processors in those two locations.

Land and other real estate expenses are budgeted at $2.3 million, a reduction of $6.2 million from the 1997 estimate. The reduction is primarily due to the completion of the Minneapolis building during 1997 and a delay in the two land improvement projects associated with new buildings in the Atlanta District. The most significant outlay during 1998 is associated with the new building projects in Atlanta and Birmingham.

Building machinery and equipment outlays are budgeted at $29.6 million, or about 10 percent of total capital outlays. Included are items related to the building and renovation projects in New York ($6.4 million), Cleveland ($5.9 million) and Atlanta ($4.7 million) and San Francisco ($2.7 million). Other districts are also budgeting for a variety of smaller items, including replacement of elevators to comply with the Americans with Disabilities Act.

Software purchases in 1998 are budgeted at $15.6 million. FRAS has budgeted $4.7 million for software. The budget of the New York Reserve Bank includes $3.8 million for a new check adjustment system and replacement of the Bank's market data software. Check-image software in Boston accounts for about $2.1 million of the total, and smaller software purchases throughout the Reserve Banks account for the balance.

Trends in Expenses and Employment

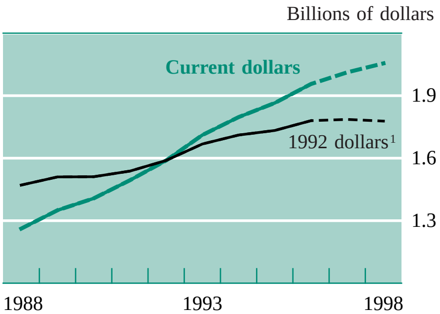
Over the ten years ending with the 1998 budget, Reserve Bank expenses have increased an average of 5.0 percent per year (chart 3.1), and the average number of employees at the Reserve Banks (including FRAS) has decreased by 591, from 23,345 to 22,754 (chart 3.2). Since 1988, staff levels have decreased in the commercial check service (783 ANP), the overhead services (180 ANP), securities safekeeping and noncash services (131 ANP), the ACH and funds transfer services (321 ANP), services to the Treasury and other government agencies (421), and the monetary policy service (42 ANP). These staff reductions have been due largely to consolidation of operations and increased operational efficiencies throughout the System.

Partly offsetting the decreases are staff additions in supervision and regulation (745 ANP) due mainly to implementation of the Federal Deposit Insurance Corporation Improvement Act and the Community Reinvestment Act, in data services due to the consolidation of data processing and data communications at FRAS (401 ANP), and in public programs due to efforts to enhance consumer education and communications with the public (93 ANP).

The average annual growth of operating expenses has slowed in recent years and is projected to be 3.7 percent over the five years ending with the 1998 budget. Affecting growth during this period were expanded bank supervision needs and the transition to a consolidated data processing and data communications environment at FRAS. Mainly because of production charges from FRAS, nonpersonnel costs have been increasing at a faster rate than personnel costs—5.5 percent compared with 2.3 percent—as the Reserve Banks downsize labor-intensive and computer

Chart 3.1

Operating Expenses of the Federal Reserve Banks, 1988–98

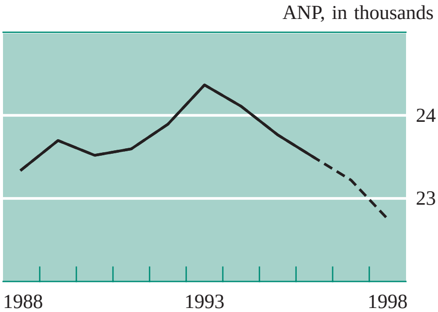


NOTE. Excludes special project. For 1997, estimate; for 1998, budget.

1. Calculated with the GDP price deflator.

Chart 3.2

Employment at the Federal Reserve Banks, 1988–98



NOTE. Includes Federal Reserve Automation Services. The costs of the special project do not involve personnel. For 1997, estimate; for 1998, budget. See text note 2 for definition of ANP.

operations and substitute technology for labor.

By operational area, expense increases over the five years have been highest for supervision and regulation (average annual increase of 6.9 percent), followed by monetary and economic policy (5.9 percent, reflecting increases in support and overhead services) and services to the Treasury and other government agencies and services to financial institutions and the public (both 3.7 percent).

Under services to financial institutions and the public, expenses for the currency service have increased an average of 6.5 percent per year, primarily because of the installation of new currency processors, and expenses for public programs have risen an average 7.3 percent per year. Nonetheless, overall growth in this service has slowed in recent years because of downsizing in the commercial check service resulting from declining volume and centralization efforts in the funds transfer and ACH services.

Just over half of the expenses in the Reserve Banks' 1998 budget (about 55 percent) are recoverable through revenues or are reimbursable by the Treasury and other government agencies. Recoverable expenses are increasing slightly from those of earlier years because of an increase in reimbursable claims for services provided to the U.S. Treasury and other agencies associated with the 1998 implementation of the System initiative "Accounting and Reporting for Government Services." The initiative requires that claims for services provided to the government be based on the full cost of the service.

Volume and Unit Costs

The volume of measured services in 1998 is budgeted to increase 3.2 percent over estimated 1997 volume, and the unit cost is expected to decrease 2.7 percent (table 3.14). Since 1993, volume has grown at an average annual rate of 2.3 percent, and unit costs have decreased at an average annual rate of 0.5 percent.

Table 3.14

Change in Volumes and Unit Costs of Measured Federal Reserve Bank Services, 1997 to 1998

Percent

Service	Volume	Unit cost
Payments	3.9	–4.8
Commercial check	2.7	–3.6
Automated clearinghouse	12.0	–8.7
Funds transfer	3.8	–8.9
Cash [1]	1.1	.5
Fiscal	1.9	3.1
Securities and noncash	–3.3	–7.5
All measured services	**3.2**	**–2.7**

1. Currency, coin, and special cash services.

The decrease in unit cost expected for 1998 reflects net decreases for the payments mechanism, book-entry securities, and fiscal services. The unit cost for commercial checks, the largest component in the overall index, is expected to decline 2.5 percent.

1997 Budget Performance

The Reserve Banks estimate that 1997 expenditures will be $2,011.6 million—$14.3 million, or 0.7 percent, more than the approved 1997 budget of $1,997.2 million. The 1997 budget approved by the Board in December 1996 represented an increase of $37.9 million, or 1.9 percent, over estimated 1996 expenses; at the estimated 1997 level of spending, the increase over actual 1996 expenditures will be 2.8 percent.

Four Reserve Banks expect their 1997 spending will come in below budget, by 1 percent or less. Six Banks expect to exceed their 1997 budgets by less than 1 percent, and two Banks expect larger overruns—Boston (4.7 percent) and St. Louis (2.3 percent). Boston's 1997 expenses were affected by a change in the allocation of costs among the twelve Banks, causing Boston to retain rather than share about $4.8 million. The overrun in St. Louis is due primarily to unbudgeted fees related to CDC compliance ($1.5 million). ■

Chapter 3

Federal Reserve Banks

The 1999 operating budgets approved by the Board of Governors for the twelve Reserve Banks total $2,159.2 million, an increase of $75.8 million, or 3.6 percent, over 1998 expenditures (table 3.1). The 1999 budgets include no special projects.

Employment, including the staff associated with FRIT (Federal Reserve Information Technology), is budgeted at 23,271 ANP (average number of personnel), an increase of 276 ANP, or 1.2 percent, from estimated 1998 employment.[1] Reserve Bank employment is expected to increase 242 ANP and FRIT employment will increase 34 ANP.[2]

Expenses for personnel (salaries and benefits) account for $1,373.2 million, or 64 percent, of the 1999 operations budget, an increase of $67.1 million, or 5.1 percent, over estimated 1998 personnel expenses (table 3.2). Nonpersonnel expenses (mainly building and automation projects) are budgeted at $786.0 million, an increase of $12.5 million, or 1.6 percent, over estimated 1998 nonpersonnel expenses.

The following two sections discuss major initiatives and the budget objective for the Reserve Banks in 1999. Subsequent sections provide details on the four operational areas and on objects of expense, capital outlays, and long-term trends. Appendix A gives more information on capital outlays and other special categories of expense; appendix D gives additional data by District and operational area.

Major Initiatives

The 1999 Reserve Banks budgets provide for the following initiatives (table 3.3):

System-defined

- Installation of equipment and software to support check image processing and archiving
- Research and development in the retail payments area
- Century date change compliance
- Capitalization of software developed for internal use that was expensed in previous years

District-defined

- Initiatives in support of fiscal services.

Reserve Bank budgets reflect a continued commitment to expand the check imaging business. Expenses for the ongoing check imaging initiative are budgeted at $38.0 million, an increase of approximately $10.0 million over estimated 1998 expenditures. This projection also includes costs associated with the national check image archive at the Boston Reserve Bank. Currently, the national archive supports the imaging and retrieval of government checks for the U.S. Department of the Treasury. In 1999, services will be expanded

1. FRIT encompasses Federal Reserve Automation Services (FRAS) and Information Technology Planning and Standards.

2. The term *average number of personnel* describes levels and changes in employment at the Reserve Banks. ANP is the average number of employees in terms of full-time positions for the period. For instance, a full-time employee who starts work on July 1 counts as 0.5 ANP for that calendar year; two half-time employees who start on January 1 count as 1 ANP.

to include commercial checks, postal money orders, and E-Z Clear savings bonds.

Marketing and research and development initiatives in retail payments account for a year-over-year increase of $3.8 million. Costs associated with these initiatives are expected to be $8.7 million. All Reserve Bank budgets include funding for a national automated clearinghouse (ACH) marketing and education effort and for research on payment issues. The enterprise-wide adjustments system (EWA) for checks will be a nationwide, integrated check adjustment processing platform that will replace stand-alone applications currently located throughout the System.

Reserve Banks continue to devote resources to Year 2000 projects. Year-over-year costs are projected to decrease $6.8 million, from $35.9 million in the 1998 estimate to $29.1 million in the 1999 budget. Total ANP devoted to the Year 2000 initiatives is expected to decrease from 303 in 1998 to 276 in 1999. The majority of the 1999 projection represents a reallocation of current resources. Resources are also provided for consulting services and contract

Table 3.1

Expenses and Employment at the Federal Reserve Banks, 1998–99

Category	1998 estimate	1999 budget	Change	
			Amount	Percent
Expenses (millions of dollars)				
Operations[1]	2,079.6	2,159.2	79.6	3.8
Special project[2]	3.8	.0	–3.8	–100.0
Total	**2,083.4**	**2,159.2**	**75.8**	**3.6**
Employment (average number of personnel)[3]				
Operations[1]	22,409	22,652	242	1.1
Federal Reserve Information Technology	585	619	34	5.8
Total	**22,995**	**23,271**	**276**	**1.2**

NOTE. See general note to table 1.1, chapter 1. Excludes capital outlays.

1. Includes support and overhead (see appendix D, table D.3, note 1, for definitions).

2. The Automation Consolidation special project began in 1992 and ended in 1998.

3. See text note 2 for definition.

Table 3.2

Operating Expenses of the Federal Reserve Banks, by Object, 1997–99

Millions of dollars except as noted

Object	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Personnel	1,259.0	1,306.1	1,373.2	3.7	5.1
Nonpersonnel	752.8	773.5	786.0	2.7	1.6
Total	**2,011.8**	**2,002.6**	**2,159.2**	**3.4**	**3.8**

NOTE. Includes support and overhead (see appendix D, table D.3, note 1, for definitions). The data for 1997 and 1998 exclude the special projects for those years; no special project is budgeted for 1999.

programmers. In addition to Reserve Bank expense projections, the FRIT budget includes an estimate of $8.2 million and 45 ANP in 1999.

District-defined fiscal initiatives totaling $10.0 million are included in the 1999 budget projection, an increase of $4.4 million over 1998 estimates. Major initiatives at the St. Louis, Richmond, and New York Banks account for most of this total. Initiatives such as the Automated Standard Applications for Payments system (ASAP), the Treasury Investment Program (TIP), Treasury Offset Program (TOP), Treasury Tax and Loan Paper (PATAX), Treasury International Capital Flows (TIC) surveys, and TIP/PATAX consolidation are aimed at maintaining high-quality services to the Treasury. Costs for these projects are fully reimbursable by the Treasury.

Expenses for these major initiatives are partially offset by a decrease of $18.1 million resulting from the Reserve Banks' interpretation of new accounting standards; the interpretation requires the capitalization of computer software developed for internal use.[3] Under this new accounting treatment, software previously charged to expense will be capitalized.

1999 Budget Objective

The approved 1999 budget objective for Reserve Banks was $2,146.0 million, an increase of $86.7 million, or 4.2 percent, from the 1998 budget of $2,059.3 million. Excluding the 1998 special project expense, the target was $91.3 million, or 4.4 percent, higher than the 1998 budget. The 1999 budget objective included funding for ongoing Year 2000 efforts and several multiyear strategic initiatives within financial services: to move paper check processing toward

3. The Federal Reserve will implement Statement of Position (SOP) 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use.

Table 3.3

Contribution of Change in Major Initiatives to the Change in Operating Expenses of the Federal Reserve Banks, 1998 to 1999

Millions of dollars except as noted

Initiative	1998 estimate	1999 budget	Contribution of change to change in total operating expenses, 1998 to 1999	
			Amount	Percentage points
System-defined				
Check imaging	28.0	38.0	10.0	.5
Retail R&D	4.9	8.7	3.8	.2
Century date change (total)	35.9	29.1	–6.8	–.3
Software capitalization	. . .	–18.1	–18.1	–.9
District-defined				
Fiscal services	5.6	10.0	4.4	.2
Total	**74.4**	**67.7**	**–6.7**	**–.3**
MEMO				
Other operating expenses	2,005.2	2,091.5	86.3	4.1
Total operating expenses	**2,079.6**	**2,159.2**	**79.6**	**3.8**

imaging and electronics, to increase the use of the ACH, and to conduct research and development on new payment strategies. The budget objective also included resources to respond to an expected increase in customer demand for check and currency services, to continue the development of applications for Treasury, and to provide competitive compensation to officers and employees. The staffing target reflected the first projected ANP increase since 1993. Higher employment was projected primarily because of higher workloads in the check and currency areas.

The 1999 budget objective was evaluated against the approved 1998 budget. The current estimate of 1998 spending ($2,079.6 million) is $24.9 million higher than the approved 1998 budget. The budget objective, when compared with the higher base of the 1998 estimate, reflects expense growth of $66.4 million or 3.2 percent, excluding the special project expense for 1998 (table 3.4).

The approved 1999 budget objective assumed a spending level of $2,146.0 million; the Reserve Banks 1999 budgets total $2,159.2 million, or $13.2 million more than the budget objective.

Two factors, identified as unquantifiable risks when the budget objective was developed, accounted for most of the difference. First, the budget objective process did not include the $27 million increase in expenses added in 1998 to process unanticipated check and currency volume. Second, as a partial offset to this increase, the budget objective did not reflect the $18.1 million expense reduction resulting from the accounting change to capitalize software developed for internal use.

Total Reserve Bank and FRIT employment is projected to be 23,271 ANP, 267 ANP higher than projected in the budget objective. Higher employment levels in priced services produced 255 ANP of this variance and are due to higher demand for traditional check and new imaging products.

Table 3.4

Change in Budget Objective and Budget of the Federal Reserve Banks, 1998 to 1999

Percent

Item	1999 budget objective[1]	1999 budget[2]
Operating expenses	3.8	3.2
System-defined initiatives[3]	.6	.6
Total, excluding special project	4.4	3.8
Special project	–.2	–.2
Total, including special project	**4.2**	**3.6**

1. As a change from 1998 budget.
2. As a change from 1998 estimated expenses.
3. Check imaging, retail research and development, century date change, and software capitalization.

Budget by Operational Area

Tables 3.5 and 3.6 summarize employment and expenses for the Reserve Banks' four operational areas. Tables 3.7 through 3.11 provide details for each area.

Monetary and Economic Policy

The monetary and economic policy budget is $167.1 million, $13.6 million, or 8.8 percent, higher than the 1998 estimate. Its growth rate is the highest of the four operational areas and largely results from a 1999 cost accounting change in the allocation of protection costs for property, assets, and staff. Employment in this area is projected to be 728 ANP, an increase of 16 ANP, or 2.2 percent, and reflects the effects of turnover and lags in filling open positions during 1998. Initiatives in this service line include continued investment in automation that will expand information retrieval and delivery systems and improve data management processes. Other initiatives in this area include increasing the visibility of, and access to, District research products for relevant audiences; expanding partnerships with local universities and other academic organizations; and increasing research on international issues.

Services to the U.S. Treasury and Other Government Agencies

Expenses for services to the Department of the Treasury and other government agencies are budgeted at $222.7 million, a decrease of $0.6 million, or 0.3 percent, from the 1998 estimate. The 1999 capitalization of software developed for internal use results in a one-time reduction in expenses of approximately

Table 3.5

Employment at the Federal Reserve Banks, by Activity, 1997–99

Average number of personnel except as noted[1]

Activity	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Operational areas					
Monetary and economic policy	718	712	728	–.8	2.2
Services to the U.S. Treasury and other government agencies	1,438	1,422	1,394	–1.1	–2.0
Services to financial institutions and the public	7,954	8,096	8,138	1.8	.5
Supervision and regulation	2,980	2,890	2,927	–3.0	1.3
Support and overhead[2]					
Support	4,572	4,552	4,691	–.4	3.0
Overhead	4,821	4,737	4,774	–1.7	.8
Total	**22,483**	**22,410**	**22,652**	**–.3**	**1.1**

NOTE. Excludes Federal Reserve Information Technology. The costs of the special project in 1997 and 1998 do not involve personnel; the special project ended during 1998.

1. See text note 2 for definition.
2. See appendix D, table D.3, note 1, for definitions.

Table 3.6

Operating Expenses of the Federal Reserve Banks, by Operational Area, 1997–99

Thousands of dollars except as noted

Operational area	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Monetary and economic policy	144,103	153,559	167,125	6.6	8.8
Services to the U.S. Treasury and other government agencies	207,079	223,309	222,735	7.8	–.3
Services to financial institutions and the public	1,215,069	1,250,554	1,292,505	2.9	3.4
Supervision and regulation	436,392	452,178	476,857	3.6	5.5
Total	**2,002,643**	**2,079,600**	**2,159,222**	**3.8**	**3.8**

NOTE. Includes support and overhead (see appendix D, table D.3, note 1, for definitions). The data for 1997 and 1998 exclude the special projects for those years; no special project is budgeted for 1999.

$5.9 million. Total 1999 employment is 1,394 ANP, down 28 ANP, or 2.0 percent, from the 1998 estimate.

The Reserve Banks continue to research, develop, and implement applications to improve and expand funds collection and disbursement processes for the Treasury and other government agencies and to eliminate paper-based products and processing. For example, the Reserve Banks are working with the Bureau of the Public Debt to archive paid savings bonds, to expand web-based applications for savings bonds and Treasury Direct, and to deploy optical scanning technology to collect savings bond data previously entered manually.

The effects of technology and regulatory changes are particularly evident in the processing of food coupons. Resource requirements in this area are projected to decline $2.8 million (11.3 percent) and 13 ANP because of the electronic benefits transfer program.

Efforts to align resources with changing technology and volumes through re-engineering and other realignment programs continue in several Districts.

Table 3.7

Expenses of the Federal Reserve Banks for Monetary and Economic Policy, 1997–99

Thousands of dollars except as noted

Service	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Economic policy determination	112,741	120,605	131,305	7.0	8.9
Open market trading	31,362	32,954	35,820	5.1	8.7
Total	**144,103**	**153,559**	**167,125**	**6.6**	**8.8**

NOTE. The data for 1997 and 1998 exclude the special projects for those years; no special project is budgeted for 1999.

Table 3.8

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies, 1997–99

Thousands of dollars except as noted

Service	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Centralized operations—savings bonds	59,030	72,103	72,972	22.1	1.2
Other Treasury issues	14,569	14,839	12,425	1.9	–16.3
Centralized operations—other Treasury issues	1,984	1,639	3,742	–17.4	128.3
Centrally provided Treasury and agency services	35,051	36,266	37,241	3.5	2.7
Government accounts	34,022	36,046	35,733	5.9	–.9
Food coupons	25,210	25,002	22,165	–.8	–11.3
Other	37,213	37,414	38,457	.5	2.8
Total	**207,079**	**223,309**	**222,735**	**7.8**	**–.3**

NOTE. See general note to table 3.7.

Services to Financial Institutions and the Public

Expenses for services to financial institutions and the public, an area that includes both priced and nonpriced services, is budgeted at $1,292.5 million, an increase of $42.0 million, or 3.4 percent, over the 1998 estimate. Expense growth in two areas, currency and check processing, accounts for $40.9 million of this increase. Staffing is budgeted at 8,138 ANP, an increase of 42 ANP, or 0.5 percent, from the 1998 estimate, with approximately one-half of this increase coming from currency

Table 3.9

Expenses of the Federal Reserve Banks for Services to Financial Institutions and the Public, 1997–99

Thousands of dollars except as noted

Service	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Currency	248,474	261,246	275,763	5.1	5.6
Coin	28,845	31,618	24,242	9.6	–23.3
Special cash	4,491	2,468	2,474	–45.0	.2
Commercial check	577,226	603,745	630,102	4.6	4.4
Other check	41,870	38,665	41,128	–7.7	6.4
Funds transfer	66,732	65,202	64,633	–2.3	–.9
Automated clearinghouse	66,375	66,697	69,721	.5	4.5
Book-entry securities transfer	38,220	33,803	32,485	–11.6	–3.9
Other securities and noncash collection	6,919	4,840	4,015	–30.0	–17.0
Loans to member banks and others	23,878	22,960	23,185	–3.8	1.0
Public programs	74,964	82,018	85,963	9.4	4.8
Other	37,075	37,292	38,794	.6	4.0
Total	**1,215,069**	**1,250,554**	**1,292,505**	**2.9**	**3.4**

NOTE. See general note to table 3.7.

Table 3.10

Expenses of the Federal Reserve Banks for Services to the U.S. Treasury and Other Government Agencies and to Financial Institutions and the Public, 1997–99

Thousands of dollars except as noted

Service	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
U.S. government services[1]	291,650	294,806	295,239	1.1	.1
Cash services	277,319	292,864	300,006	5.6	2.4
Priced services	690,744	738,145	767,955	6.9	4.0
Other	162,435	148,048	152,040	–8.9	2.7
Total	**1,422,148**	**1,473,863**	**1,515,240**	**3.6**	**2.8**

NOTE. See general note to table 3.7.

1. The amounts shown here do not include expenses in this service that are recorded in the monetary and economic policy operational area. For 1997 these expenses were $673 thousand, for 1998 they are estimated at $1,227 thousand, and for 1999 they are budgeted at $1,438 thousand. These expenses increase the total costs of services provided by the Reserve Banks as fiscal agents and depositories of the United States.

processing and one-fourth from check processing.

Customer demand for currency and check processing increased unexpectedly in several Districts during 1998 and is projected to continue expanding at that rate through 1999. Estimated volume growth in these two areas accounts for an additional $4.5 million in the 1999 budget.

Higher expenses in the 1999 budget are being generated not only by increases in traditional demand but also by several strategic initiatives to provide a consistent product to the increasing number of national customers and to provide efficiencies in the development and management of applications and products: expanding the application of imaging to commercial checks, postal money orders, and government checks; stimulating demand for electronic check presentment and the electronic cash letter; and moving toward System-standard check automation platforms and applications.

The Reserve Banks continue to seek efficiencies by consolidating the location of services that use highly centralized electronic applications such as funds transfer, book-entry securities, and ACH. The latest example is consolidation of the twelve sites providing off-line processing for funds and book-entry securities into two sites by the end of 1999.

Priced service costs are projected to be $738.1 million in 1998 and $768.0 million in 1999. All of these costs, plus the private sector adjustment factor, are budgeted for recovery through fees to depository institutions and others that use the services. The Reserve Banks' recovery rate is estimated to be 103.9 percent for 1998 and 101.2 percent for 1999.

Supervision and Regulation

Supervision and regulation expenses are budgeted to be $476.9 million in 1999, an increase of $24.7 million, or 5.5 percent, over the 1998 estimate. The 1999 change in accounting of the allocation of protection costs for property, assets, and staff is a significant

Table 3.11

Expenses of the Federal Reserve Banks for Supervision and Regulation, 1997–99

Thousands of dollars except as noted

Service	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Supervision of large multistate, multi-District banking organizations	...	70,975	76,355	...	7.6
Supervision of domestic regional and community banking organizations	...	165,507	174,822	...	5.6
Supervision of foreign banking organizations	...	57,069	60,641	...	6.3
Administration of laws and regulations related to banking	...	89,093	91,544	...	2.8
Supervision activities benefiting the banking system	...	46,976	49,395	...	5.1
Studies of banking and financial markets	...	22,558	24,100	...	6.8
Total	**436,393**	**452,178**	**476,857**	**3.6**	**5.5**

NOTE. Expenses in 1997 for this operational area were recorded under a structure redefined as of 1998. The data for 1997 and 1998 exclude the special projects for those years; no special project is budgeted for 1999.

source of the budgeted increase in this area. The size of the cost increases varies by District and ranges from 0.5 percent to 10.8 percent. The range of expense changes reflects the response to District-specific environmental factors and the degree of efficiencies realized through risk-focused examinations and improved automation.

Employment is projected to be 2,927 ANP, an increase of 37 ANP, or 1.3 percent, over the 1998 estimate. Only three Districts are projecting declines in staffing. Several Districts were hesitant to reduce staffing in this area because of uncertainty regarding the level of support needed for century date change (CDC) efforts in 1999.

Along with ongoing examination responsibilities, CDC is expected to remain a high priority during the coming year. In addition, the supervision and regulation area continues to broaden the application of technology to streamline the examination process, expedite information retrieval capabilities and lessen the on-site burden to financial institutions, and reduce the internal administrative burden through the automation of tracking and scheduling functions.

Budget by Object of Expense

Personnel expenses are projected to increase 5.1 percent, while nonpersonnel-related expenses are increasing 1.6 percent. Personnel expenses include officer and employee salaries, other compensation to personnel, and retirement and other benefits, and account for 64 percent of Reserve Bank expenses (table 3.12).

Table 3.12

Operating Expenses of the Federal Reserve Banks, by Object, 1997–99

Thousands of dollars except as noted

Object	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Personnel					
Officers' salaries	105,185	114,354	123,400	8.7	7.9
Employees' salaries	850,825	874,630	929,563	2.8	6.3
Other[1]	40,992	44,694	34,976	9.0	–21.7
Retirement and other benefits	263,141	272,377	285,247	3.5	4.7
Total	1,260,142	1,306,056	1,373,185	3.6	5.1
Nonpersonnel					
Forms and supplies	53,406	52,738	52,292	–1.3	–.8
Equipment	171,500	177,806	196,557	3.7	10.5
Software	35,322	39,425	41,304	11.6	4.8
Shipping	79,278	77,918	78,881	–1.7	1.2
Travel	42,853	44,085	45,594	2.9	3.4
Buildings	174,843	174,762	186,695	.0	6.8
Recoveries	–53,764	–66,398	–60,769	23.5	–8.5
Other[2]	239,064	273,207	245,483	14.3	–10.1
Total	742,502	773,544	786,037	4.2	1.6
Total	**2,002,644**	**2,079,600**	**2,159,222**	**3.8**	**3.8**

NOTE. See general note to table 3.7.

1. Certain contractual arrangements and miscellaneous other personnel expenses.

2. Communications, fees, contra-expenses, shared costs distributed and received, excess capacity, and miscellaneous other expenses.

Salaries and other personnel expenses account for about 50 percent of 1999 budgeted expense, and anticipated growth is $54.3 million, or 5.2 percent. Salaries for officers and employees are expected to increase $64.0 million, or 6.5 percent. Merit programs averaging 4.2 percent will increase salary expenses by $41.2 million. Also contributing to higher salary expenses are staff increases, promotions and reclassifications, and structure and market adjustments. These increases are partially offset by a $9.7 million decrease in other personnel expenses, which reflects a decline in the use of outside agency help and reduced severance and retention payments. Also offsetting the increase in salaries are a $4.2 million reduction in overtime and a $4.9 million decrease in costs associated with short-term position vacancies or lags in hiring.

Retirement and other benefits expenses, which account for 13 percent of Reserve Bank budgets, are anticipated to increase $12.9 million, or 4.7 percent, in 1999. Contributing factors include increases in salary-related benefits, such as social security and the thrift plan. Health care costs are estimated to increase by 5.5 percent in 1999 because of an expected increase in medical insurance costs. To minimize future increases in the cost of health care, the Banks are collectively seeking consolidated purchasing of employee and retiree benefits.

Nonpersonnel expenses account for 36 percent of Reserve Bank expenses and are projected to increase 1.6 percent in 1999.

Equipment expenses are expected to increase $18.8 million, or 10.5 percent, and account for 9 percent of total expenses in 1999. In addition to 1999 purchases, the variance in equipment expense is driven primarily by an increase in depreciation ($14.9 million) and maintenance costs ($4.2 million). The increase in depreciation results from the full-year effect of 1998 purchases of equipment for check imaging, voice mail, and PBX; local area network upgrades required for CDC compliance; and the effect of capital purchases planned for 1999. Increases in maintenance costs are primarily driven by local area networks (LANs), servers, and hardware equipment contracts.

Shipping expenses account for 4 percent of Reserve Bank expenses and are expected to increase $1.0 million, or 1.2 percent, primarily because of higher rates for courier contracts and shipping.

Within the travel budget, expenditures on foreign travel are projected to be $4.4 million in 1999 and account for 0.2 percent of total 1999 expenses. Foreign travel expenses budgeted for 1999 are $0.5 million, or 13.2 percent, higher than 1998; the increase covers, in part, an anticipated rise in foreign examinations, the consolidation of System examinations, and a rise in targeted visitations at troubled institutions, where extra monitoring is required.

Building expenses, which account for 8.6 percent of total expenses, are expected to increase $11.9 million, or 6.8 percent, in 1999. The increase is driven by higher real estate taxes, primarily in Cleveland, Minneapolis, and San Francisco; higher property depreciation associated with the completion of building improvements and renovations; andn higher rental expenses resulting from several lease agreements.

Other nonpersonnel expenses are projected to decrease $27.7 million, or 10.1 percent. Of the decrease, $18.1 million is due to the Reserve Banks' implementation of the new accounting standards that require the capitalization of computer software developed or obtained for internal use.

Capital Outlays

The 1999 capital budget submitted by the twelve Reserve Banks and FRIT totals $405.6 million, a $129.3 million increase over the 1998 estimated levels (table 3.13). The budget consists of $366.9 million for the Banks and $38.6 million for FRIT.

The 1999 capital budgets developed by the Reserve Banks and FRIT include funding for a number of projects that support the strategic direction outlined in the Banks' plans. These strategic directions include improving operational efficiency and effectiveness, promoting customer service, and providing a quality work environment. In support of these strategies, the 1999 budget identifies four major categories of capital outlay: building and facility improvements, automation-related initiatives, check and other payment service improvements, and building security enhancements.

The proposed capital budget includes $182.8 million for building-related projects. These projects are geared toward renovation and modernization of physical facilities, replacement or upgrading of critical systems, energy conservation, and compliance with the Americans with Disability Act. More than 71 percent of the 1999 budget comprises six major projects: four in the New York District (improvements to 33 Maiden Lane, head office modernization, stone facade restoration, and tenant improvements at the East Rutherford Operations Center) and two in the Atlanta District (head office building and Birmingham Branch building). These six projects have a total estimated cost of $377.2 million ($76.3 million before 1999, $130.3 million in 1999, and $170.6 million in later years). Funding is also provided for the replacement of routine building-related equipment as well as replacements of furniture and fixtures.

Table 3.13

Capital Outlays of the Federal Reserve Banks, by Class, 1997–99

Thousands of dollars except as noted

Class	1997 actual	1998 estimate	1999 budget	Percentage change	
				1997 to 1998	1998 to 1999
Data processing and data communications equipment[1]	70,714	111,952	140,167	58.3	25.2
Buildings	72,726	67,863	114,970	–6.7	69.4
Furniture, furnishings, and fixtures	23,299	23,364	29,562	.3	26.5
Other equipment[2]	30,337	23,414	24,140	–22.8	3.1
Land and other real estate	4,695	3,044	9,551	–35.2	213.8
Building machinery and equipment	16,528	24,183	22,279	46.3	–7.9
Leasehold improvements	1,889	8,166	15,985	332.3	95.8
Software[3]	5,548	14,301	48,902	157.8	241.9
Total	**225,736**	**276,287**	**405,556**	**22.4**	**46.8**
MEMO					
FRIT	21,356	34,722	38,641	62.6	11.3

1. For Federal Reserve Information Technology (FRIT), includes capital of $18,848 thousand in 1997, $32,291 thousand in 1998, and $29,698 thousand in 1999.

2. For FRIT, includes $28 thousand in 1997, $20 thousand in 1998, and $20 thousand in 1999.

3. For FRIT, includes $2,481 thousand in 1997, $2,412 thousand in 1998, and $8,894 thousand in 1999.

The proposed capital budget includes $122.3 million in funding for automation initiatives. Approximately $18 million of this total is attributable to the capitalization of software. These initiatives do not include the automation components of building projects, check and payment services, or security projects that are discussed separately. The strategic directions outlined in the budgets of the individual Reserve Banks include enhanced technological capabilities, the continued implementation of LAN technology, the development of common office environments and web-based applications, and various improvements and replacements to ensure CDC compliance.

Aside from the $38.6 million included for FRIT, the major automation-related projects are $3.8 million for the Consolidated Process Encryption Center, $2.7 million for the continued development of the Statistics and Reserves System, and $2.6 million for the Foreign/Domestic Trading, Analysis, and Accounting System. The largest share of the remaining funds supports the Districts' strategies for distributed technology and PC replacement. A majority of the Banks are operating under a three-year replacement schedule and continue to push for the conversion of mainframe applications to a LAN environment and, to a lesser extent, to web-based solutions.

The 1999 capital budget includes $75.5 million for initiatives to improve check operations and other payment services. Nearly every District is funding reader/sorter/endorser upgrades and high-speed imaging projects. In addition, several projects are aimed at improving savings bond operations in the consolidation sites, and others are for currency-related initiatives throughout the System.

District-specific initiatives include the Unisys check support hosted by the Cleveland District, the continued development of an electronic check presentment environment in the Minneapolis District, and a number of Treasury-related projects in the Richmond District.

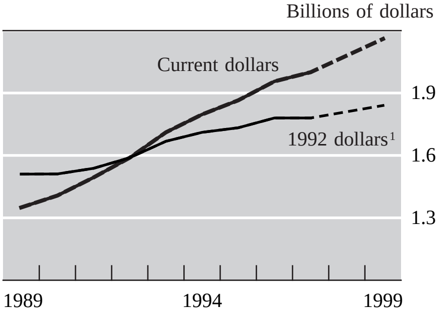
The last major category of capital expenditures included in the 1999 budget is for projects to improve security within the Reserve Banks. These projects include upgrades and replacements of building security features, including video surveillance systems, card readers and access systems, and fire alarms, for a total of $11.9 million. Tables 10 and 11 in the statistical appendix provide additional data on capital expenditures.

Trends in Expenses and Employment

Over the ten years ending with the 1999 budget, Reserve Bank expenses have increased an average of 4.8 percent per year (chart 3.1), and the average number of employees at the Reserve Banks (including FRAS) has decreased 426, from 23,697 in 1989 to 23,271 in 1999

Chart 3.1

Operating Expenses of the Federal Reserve Banks, 1989–99



NOTE. See general note to table 3.7. For 1998, estimate; for 1999, budget.

1. Calculated with the GDP price deflator.

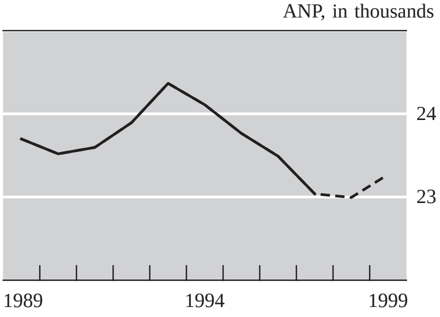
(chart 3.2). Since 1989, staff levels have decreased in the commercial check service (746 ANP), the overhead service (199 ANP), securities safekeeping and noncash services (183 ANP), the ACH and funds transfer services (317 ANP), services to the Treasury and other government agencies (377), and the monetary policy service (55 ANP). These staff reductions have been due largely to consolidation of operations and increased operational efficiencies throughout the System.

Partly offsetting the decreases are additions to the staff in supervision and regulation (730 ANP), needed mainly because of implementation of the Federal Deposit Insurance Corporation Improvement Act and the Community Reinvestment Act; in data services (494 ANP) because of an increase in LAN applications; and in public programs (130 ANP) because of efforts to enhance consumer education and communications with the public.

The average annual growth of operating expenses, which has slowed in recent years, is projected to be 3.7 percent over the five years ending with the 1999 budget. Mainly because of production charges from FRIT, nonpersonnel costs have been increasing at a faster rate than personnel costs, 4.2 percent compared with 3.2 percent, as the Reserve Banks downsize labor-intensive and computer operations and substitute technology for labor.

Chart 3.2

Employment at the
Federal Reserve Banks, 1989–99



NOTE. See general note to table 3.5. For 1998, estimate; for 1999, budget. See text note 2 for definition of ANP.

Over this five-year period, the average annual increases in expenses by service line have been the highest for monetary and economic policy (6.7 percent) and supervision and regulation (5.7 percent). Expenses in both functional areas have been affected by the 1999 change in the method for allocating protection costs and by increases from various support areas. Expenses in the supervision and regulation function have also been affected by the ongoing changes in the financial services industry and century date change issues. Expenses for services to financial institutions and the public grew 3.2 percent per year, primarily because of increases in currency and check volumes.

The average number of employees at the Reserve Banks decreased 975 ANP, from 23,627 ANP in 1994 to 22,652 ANP in 1999. Overall, decreases in employment are due largely to the consolidation of operations, the realization of operational efficiencies throughout the Reserve Banks, and reduced check volumes following the 1994 implementation of the same-day settlement rule under the Federal Reserve's Regulation CC.

Employment in services to Treasury and other government agencies has decreased primarily because of the continuing rollout of the electronic benefits transfer program and centralization efforts for savings bonds. In services to financial institutions and the public, employment has decreased because of efficiencies gained in check processing, reduced check volumes, more efficient currency processors, and centralization in funds and book-entry processing. The increase in the support service area is primarily due to additional staff needed to support ongoing information technology requirements.

Volume and Unit Costs

The volume of measured services in 1999 is budgeted to increase 3.9 percent over estimated 1998 volume, and the unit cost is expected to decrease 1.9 percent (table 3.14). The decrease in expected unit costs reflects net decreases for retail payments, wholesale payments, and cash services. A 0.6 percent decline in unit cost is anticipated in the commercial checks area, the largest component in the overall index.

Table 3.14

Change in Volumes and Unit Costs of Measured Federal Reserve Bank Services, 1998 to 1999

Percent

Service	Volume	Unit cost
Payments	3.7	–1.2
Commercial check	2.8	–.6
Automated clearinghouse	10.0	–5.0
Cash[1]	5.8	–3.2
Fiscal	.8	.2
Wholesale payments	2.8	–4.5
Transfer of reserve account balances	5.8	–6.3
Book-entry securities	–3.0	–.5
All measured services	**3.9**	**–1.9**

1. Currency, coin, and food coupon services.

1998 Budget Performance

The Reserve Banks estimate that 1998 expenses will be $2,079.6 million, which represents an increase of $24.9 million, or 1.2 percent, from the approved 1998 budget of $2,054.7 million. The 1998 budgets, which were approved by the Board in December 1997, resulted in an increase of $43.1 million or 2.1 percent over estimated 1997 expenses. At the 1998 estimated level of spending, the increase over the actual 1997 level would be 3.8 percent.

Nine Banks expect to exceed their approved 1998 budget, six of them by 1.0 percent or more. The three largest overruns are expected at Boston (2.0 percent), Atlanta (6.4 percent) and St. Louis (6.3 percent). Boston's overall budget has increased because of higher-than-anticipated costs for the national government check image archive and because of Interdistrict Transportation System costs associated with check shipments; both are Systemwide expenses retained in Boston's budget. Atlanta's projected overrun is due primarily to staffing additions necessitated by increased check and cash volumes. In addition, the Atlanta District has worked aggressively to address issues arising from a 1997 staff ‘‘Vision’’ survey that found a need to staff functions appropriately, reduce overtime and turnover, and compensate in accordance with the market. The overrun at St. Louis is due primarily to check write-offs and increased overtime in the check area. ■