Chapter 3

Federal Reserve Banks

The 2010 operating budgets of the 12 Reserve Banks total $3,221.3 million.[1] The 2010 total is $78.8 million, or 2.5 percent, above 2009 actual expenses. This growth is driven by increases in central bank functions, specifically those related to supervision and regulation, loans to depository institutions and others, as well as cash operations. These increases are significantly offset by decreases in priced services as a result of the decline in paper-check volume, reductions in the check-processing infrastructure, and the substantial reductions in check transportation costs. In addition, the increase in expenses is further offset by a reduction in vendor fees incurred by the New York Federal Reserve Bank.

Budgeted net expenses for 2010, after revenue and reimbursements, are expected to increase by $175.5 million, or 8.7 percent, over 2009 actual net expenses (table 3.1). Approximately 32 percent of Reserve Bank expenses in the 2010 budget are offset by priced service revenues (18 percent) and reimbursable claims for services provided to the Treasury and other agencies (14 percent).[2] Budgeted 2010 priced services revenue is lower than the 2009 actual level, primarily because of declining paper-check volume. Reimbursable claims are expected to increase only slightly in 2010, a reflection of an ongoing effort by the Treasury and the Reserve Banks to contain costs while maintaining support for key programs and advancing new initiatives.

Total 2010 projected employment for the Reserve Banks, Federal Reserve In-

1. These expenses include those budgeted by the Federal Reserve Information Technology and the Office of Employee Benefits that are chargeable to the Reserve Banks.

2. Reimbursable claims include costs of fiscal agency and depository services provided to the U.S. Treasury, other government agencies, and other fiscal principals that are billed to and reimbursed by these agencies.

Table 3.1 Operating Expenses of the Federal Reserve Banks, Net of Receipts and Claims for Reimbursement, 2009 and 2010

Millions of dollars, except as noted

Item	2009 (actual)	2010 (budgeted)	Change	
			Amount	Percent
Total operating expenses	3,142.5	3,221.3	78.8	2.5
LESS				
Revenue from priced services	675.4	565.9	−109.5	−16.2
Claims for reimbursement[1]	450.3	463.2	12.9	2.9
Other income	1.3	1.2	−0.1	−7.1
EQUALS				
Net expenses	**2,015.5**	**2,191.0**	**175.5**	**8.7**

NOTE: Excludes capital outlays. Includes expenses budgeted by the Federal Reserve Information Technology and the Office of Employee Benefits. Expenses from these entities have been charged to the Reserve Banks, as appropriate, and included in their budgets. Components may not sum to totals and may not yield percentages shown because of rounding. Operating expenses reflect redistributions for support and allocation of overhead.

1. Costs of fiscal agency and depository services provided to the U.S. Treasury, other government agencies, and other fiscal principals that are billed to these agencies.

Table 3.2 Employment at the Federal Reserve Banks, FRIT, and OEB, 2009 and 2010
Average number of personnel, except as noted

Item	2009 (actual)	2010 (budgeted)	Change	
			Amount	Percent
Reserve Banks	16,910	16,628	–282	–1.7
Federal Reserve Information Technology (FRIT)	925	904	–21	–2.3
Office of Employee Benefits (OEB)	45	47	2	4.4
Total	**17,880**	**17,578**	**–302**	**–1.7**

Note: Components may not sum to totals and may not yield percentages shown because of rounding. See text note 3 for definition of *average number of personnel* (ANP).

formation Technology (FRIT), and the Office of Employee Benefits (OEB) is 17,578 "average number of personnel (ANP)," a decrease of 302 ANP, or 1.7 percent, from the 2009 actual staff level (table 3.2).[3] The 2010 staffing decrease is the result of a continuing trend of workforce reductions that began in the late 1990s; staffing levels are at their lowest point in more than 30 years. The 2010 budgeted staff reductions are largely due to the effect of infrastructure changes and paper-check volume declines; these decreases are slightly offset by staffing increases in central bank functions. Given the current financial market and banking conditions, the Reserve Banks have increased resources dedicated to fulfilling their central bank responsibilities, which include research, supervision and regulation, loans and credit, and public information.

2009 Budget Performance

Total 2009 actual expenses are $3,142.5 million, an increase of $56.4 million, or 1.8 percent, from the approved 2009 budget of $3,086.2 million. Total 2009 actual staffing is 17,880 ANP, a decrease of 140 ANP from the 2009 budgeted level of 18,020 ANP.

The expense increase compared with budget was driven in part by the expanded responsibilities in response to the economic crisis ($107.0 million, or 110 percent). Reflected in the increase are additional staffing and data needs and unforeseen fees related to the Federal Agency Mortgage-Backed Securities Purchase and Term Asset-Backed Securities Loan Facility programs. Also contributing to the increase over budget is the growth in supervision and regulation staffing in response to the financial conditions of the banking industry ($11.0 million and 78 ANP).

Partially offsetting the overrun are decreased expenses in the check function ($47.1 million, or 10 percent). The Reserve Banks significantly accelerated the closing of the check-processing sites in 2009, substantially reduced check transportation, and reduced staff in the check adjustments function because of paper-check volume declines. By the end of 2010, only one full-service paper-check processing site will remain.

Also offsetting the overrun is lower expenses for Treasury services ($13.3 million, or 3.0 percent). Treasury services were under budget largely because of a reduction in Treasury Web

3. ANP is the average number of employees in terms of full-time positions for the period. For instance, a full-time employee who works one-half of the year counts as 0.5 ANP for that calendar year; two half-time employees who work the full year count as 1 ANP.

Application Infrastructure (TWAI) expenses, resulting from the TWAI optimization program, an effort begun in 2007 to identify efficiencies and cost savings, and delays in the Treasury's Collections and Cash Management Modernization (CCMM) initiative.[4]

The underrun in total staffing of 140 ANP, as compared with the approved budget, reflects lower staffing in several areas, partially offset by crisis-related overruns (99 ANP). Check operations are 253 ANP under budget because the System's legacy infrastructure was downsized beyond the budgeted projection and because inter-District check transportation was eliminated. Treasury services are 28 ANP below budget, reflecting CCMM project delays and volume. Cash operations are 23 ANP under budget, primarily because of volume declines and productivity gains. In addition, the Reserve Banks continue to reduce staffing in internal support functions in response to the declines in operation areas. Overall support functions are 49 ANP under budget. The facilities management function is 22 ANP under budget because of outsourced housekeeping in one District. Also contributing to the underrun in support functions are lower staffing levels in law enforcement (25 ANP) and food services (10 ANP) resulting from process improvements.

Initiatives Affecting the 2010 Budget

For 2010, the Reserve Banks' budgets reflect several initiatives that will continue to address financial stability and deteriorating banking conditions, as well as enhance resiliency.

Central Bank Services

In the central bank area, which includes monetary policy, public programs, supervision and regulation, and cash operations, expenses are increasing $162.8 million, or 7.7 percent, in the 2010 budget. The staffing level is increasing 233 ANP, in part because of the full-year effect of staff additions in 2009, including 118 ANP to support loans to depository institutions and others. Total costs for monetary policy are budgeted to remain relatively flat, reflecting higher salary-related costs, offset by nonrecurring crisis-related expenses.

The budget for the supervision and regulation function is increasing $59.0 million, or 8.1 percent, as the function plans for additional staffing resources (133 ANP) to address the deterioration in the banking industry's performance and condition, sharply higher numbers of 3/4/5-rated state member banks and bank holding companies, and accelerated frequency of mandated examinations and inspections.

Expenses in cash operations are increasing $36.2 million, or 7.6 percent. The Currency and Coin Handling Environment (CACHE) project and upgrades to the currency processing sorters and related sensors are driving the increase.[5] These expenses are partially offset by staffing reductions (42 ANP) resulting from lower-than-expected volumes.

4. CCMM is a comprehensive multiyear enterprise architecture initiative to streamline, modernize, and improve the services, systems, and processes supporting the Treasury's collections and cash-management programs. The goal is to improve efficiency and reduce costs to the Treasury, which provides a savings to the taxpayers.

5. The CACHE project is being re-evaluated, and the effect on the budget is unknown at this time.

Treasury-Related Functions

The budget for services to the Treasury, which are fully reimbursable, is increasing $14.7 million, or 3.4 percent. Expenses related to the TWAI are increasing as the number of applications hosted in the infrastructure expands in connection with the CCMM initiative. In addition, several projects under the CCMM umbrella are expected to gain momentum in 2010; one portion of the project is being delayed from 2009 until 2010. These increases are partially offset by lower staffing needs (21 ANP) and lower costs associated with the continued volume declines in Treasury retail securities, government checks, and postal money orders, as well as the completion of the Treasury Debt Management System application development effort.

Priced Services

Total check expenses are decreasing $111.6 million, or 26.5 percent, reflecting the check restructuring costs and continued paper-check volume declines. In response to the continuing decline in paper-check volumes, the Federal Reserve announced that the Federal Reserve Bank of Cleveland will serve as the System's single paper-check processing and adjustments site and that the Federal Reserve Bank of Atlanta will serve as the System's single electronic-check processing site. This transition to a single paper-check processing site was completed in February 2010. As a result, the check staffing level is decreasing 502 ANP. Even with these cost reduction efforts, the Reserve Banks have budgeted a recovery rate of 94.5 percent in 2010. The Reserve Banks continue to identify additional opportunities to meet long-term cost-recovery objectives.

Support Services

Support costs are increasing $30.8 million, or 3.1 percent. The expense increases are driven primarily by increases in facilities management ($14.6 million) and information technology ($8.0 million). Facilities costs are increasing because of the completion of larger building projects and the expansion of leased space in New York. IT costs are increasing in support of cash and Treasury projects at several Reserve Banks. The staffing level is decreasing 21 ANP, primarily because of efficiency gains.

Five-Year Trend in Reserve Bank Expenses

Total expenses for the Reserve Banks have grown an average of 4.4 percent annually over the past five years.

Central Bank Services

Central bank services have grown an average of 9.2 percent annually over the past five years. The increase is primarily in the areas of monetary policy, public programs, and loans to depository institutions and others, where expenses have grown, on average, 12.5 percent annually; the Banks have increased resources dedicated to community outreach, financial literacy, regional economic research efforts, and lending activities. Expenses in the supervision and regulation function have grown an average of 9.0 percent annually over the past five years, reflecting the need for additional resources necessary to recruit and retain staff with specialized skills, and more recently, to address financial market turmoil and deteriorating banking and economic conditions. There have been ongoing efficiency improvements in the cash area over the past five years; however, expenses in cash operations have increased an average of 5.2 percent annually, reflecting increased costs to modernize the cash-processing and inventory-tracking infrastructure, along with higher support costs, particularly protection costs.

Treasury Services

Treasury services expenses have grown on average 3.4 percent annually since 2005. Efforts by the Treasury to limit expense growth and delays in some CCMM projects have resulted in modest growth in recent years. Growth from 2005 to 2007 was driven primarily by the expansion of the TWAI to host a growing number of Treasury applications.

Priced Services

Priced services expenses have declined an average of 7.8 percent annually over the past five years, driven by the check service. Efforts to reduce the size of the System's check operations, consistent with declining volumes, have resulted in an average annual decline of 12.9 percent in check-service costs since 2005. The downward trend in check expenses reflects staff reductions of 3,130 ANP since 2005.

2010 Personnel Expenses

Budgeted officer and employee salaries and other personnel expenses for 2010 total $1,678.0 million, an increase of $61.8 million, or 3.8 percent, compared with 2009 actual expenses. The increase reflects budgeted salary administration programs, including merit increases, market adjustments, promotions, and variable pay. Funding for officer and employee base salary administration programs is $47.1 million; merit pools for officers and employees total $33.2 million, and funding for market increases and promotions totals $13.8 million. The merit budget reflects an average increase of 2.5 percent for both officers and employees. Variable pay programs are increasing $9.5 million in 2010, with variable pay pools averaging 12.7 percent for officers and senior professionals and 4.8 percent for employees.

Although funding for merit increases decreased in 2010, merit continues to be the largest component of the total increase in salary administration costs. Growth in salary administration expenses continues to be driven by the cost of a more highly skilled workforce. Although ANP is budgeted to decrease 301 in 2010 when compared to 2009 actual staffing levels, the reduced positions are largely nonexempt, lower-salaried positions. The trend in staff additions have been toward more highly skilled, higher-salaried exempt and officer positions.

Risks in the 2010 Budget

There are a number of risks in the 2010 budget. Primary among these is the potential for legislative changes that could alter the Federal Reserve's authority. Additional staff may also be needed to manage the ongoing challenges facing banking supervision and regulation in the current economic climate. Treasury project changes and delays could also increase budgeted expenses. In connection with the CCMM initiative, the Treasury continues to refine its vision for collections and cash-management systems. If the Treasury changes its current direction, additional costs and resources may be required.

2010 Capital Plan

The 2010 capital budgets submitted by the Reserve Banks, FRIT, and OEB total $434.4 million, a $65.3 million, or 17.7 percent, increase from the 2009 actual level. The 2010 capital budgets include funding for projects to support strategies that improve operational efficiencies, enhance services to Reserve Bank customers, and ensure a safe and high-quality work environment. In support of these strategies, the 2010 budgets include seven categories of capital outlays: (1) building projects and facility improvements, (2) payment system improvements, (3) cash-services initiatives, (4) Treasury initiatives, (5) information technology infrastructure initiatives, (6) security enhancements, and (7) miscellaneous acquisitions.

The proposed capital budgets include $178.3 million for building-related projects and facility improvements. Of this total, $48.8 million is for major projects begun in previous years at the Federal Reserve Banks of Boston, New York, and St. Louis. The total also includes a major project for the Federal Reserve Bank of New York to accommodate increased staffing related to financial stability efforts. The remaining outlays in this category will fund various building renovation and refurbishment projects, as well as miscellaneous facility improvement projects.

Initiatives related to cash, payment systems, and Treasury initiatives represent $111.9 million of the capital budgets. Of this total, $54.6 million is for cash-services initiatives, including the CACHE development effort ($21.4 million) and the Systemwide upgrade of cash-processing machines ($25.1 million). The budgets also include $35.4 million for reimbursable Treasury initiatives, including support of the TWAI, Government-Wide Accounting, CCMM-related efforts, and various other initiatives, as well as $21.8 million for multiyear efforts to migrate System applications, including FedACH and Fedwire, off the mainframe to a distributed environment. The Reserve Banks and FRIT included $98.8 million in funding for major information technology initiatives. These initiatives do not include the automation components of building or payment systems initiatives discussed separately. Of the total automation-related outlays, FRIT projects and acquisitions account for $32.0 million and New York Reserve Bank projects account for $32.8 million. In addition, the budgets include $6.5 million in initial outlays for Systemwide server consolidation.

The proposed capital budgets include $40.9 million for security enhancements and $4.6 million for equipment and software not falling into the defined categories above. ■