

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 8465]
December 1, 1978

PRICING OF FEDERAL RESERVE SERVICES
Preliminary Schedule for Check and ACH Services

To All Banking Institutions
in the Second Federal Reserve District:

Following is the text of a statement issued by the Board of Governors of the Federal Reserve System:

The Federal Reserve Board today [November 17] approved for transmission to Congress a preliminary schedule of prices for Federal Reserve check and automated clearing house services.

The tentative schedule was developed by the Board and the 12 Federal Reserve Banks as part of a comprehensive plan to provide greater competitive equality among financial institutions. The prices will not be implemented until effective steps have been taken to alleviate the burden of membership in the Federal Reserve System.

Pricing schedules for other Federal Reserve services, such as the shipment of coin and currency, wire transfers of funds and the safekeeping of securities are under consideration.

The pricing of Federal Reserve services is part of an over-all effort to modernize the role of the Federal Reserve in the nation's financial system and the relationship of financial institutions in general to the Federal Reserve.

This program has been under active consideration by the Congress since July 1978 when the Board submitted its legislative proposals. These proposals included a statement of the guidelines that underlie the development by the Federal Reserve of a system of prices for its services.

The pricing of check collection services suggested in the attached schedule is based on the volume of check clearings by the Federal Reserve in the first half of 1978. The prices are meant to recoup direct and indirect costs of providing such services. In addition, adjustments totaling 11 percent of these costs have been added to reflect additional costs that would be borne in the private sector. These adjustments include capital costs, taxes, an allowance for dividends, and provision for reserve.

Prices for automated clearing and settlement services have been calculated to be competitive with check prices. Establishment of prices for automated clearing house services at this level is intended to encourage banks and their customers to take advantage of the potentially lower cost of electronic fund transfers as compared to the cost of payments by check, while still affording opportunity to develop competing automated clearing and settlement services in the private sector.

Before a final decision is made in pricing, the Federal Reserve will consider the advisability of establishing different prices for each zone in some Federal Reserve Districts.

Printed on the following pages is the text of the pricing proposal and a table showing a preliminary price schedule. We would be particularly interested in your views as to the competitiveness of the prices and your estimate of the effect of these prices on your institution. Your response may be sent to Thomas C. Sloane, Senior Vice President and Senior Adviser, at this Bank.

PAUL A. VOLCKER,
President.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Proposal For Pricing of Federal Reserve
Check Collection and Automated Clearing and Settlement Services

November 17, 1978

In connection with legislation to enhance competitive equity in banking, to improve monetary policy and to relieve the burden borne by Federal Reserve member banks, one of the issues under discussion during the recent session of Congress was pricing of Reserve Bank services. Service charges were one element of the comprehensive plan addressing these issues that the Board submitted to the Congress last summer. In addition, many of the bills under consideration by the Congress required the Federal Reserve to publish a price schedule for its services to financial institutions. At hearings on the bills, members of Congress and other interested parties commented that a price schedule for Reserve Bank services was needed in order to evaluate fully the effects of the proposed legislation.

In response to these comments, the System has prepared a preliminary proposal for charging for Reserve bank check collection and automated clearing and settlement services. A tentative price schedule is presented to elicit additional discussion. The System particularly hopes to receive indications of the competitiveness of the prices in relation to prices for comparable services (where available) in local markets. In addition, the System expects to receive analyses of the effects of implementing these prices on the banking industry and upon other users of payments services.

Attachment 1 to this proposal shows a tentative schedule of prices approximating those that would have been in effect in the first half of 1978 covering check collection and Automated Clearing House (ACH) clearing and settlement services. The payments mechanism services in this initial schedule account for about 60 per cent of the total expenses incurred by the Reserve Banks in providing services to financial institutions. Preliminary prices for the remaining services are in preparation and will be available later.

Implementation of Prices

Charges for Reserve Bank services could enhance the efficiency of the nation's payments mechanism. Such charges would promote both cost effective payments techniques and equity among institutions providing payments services to the public. However, the Federal Reserve System does not intend to implement service charges until effective steps have been taken to relieve the burden of membership in the Federal Reserve. Otherwise, the already very serious problem of withdrawals from the System would simply be exacerbated.

The Federal Reserve recognizes that these preliminary prices may have to be adjusted to reflect competitive realities and changing conditions in the industry and in the Reserve Banks. Furthermore, at the time of implementation, the System would monitor developments and could revise the prices to avoid disruption of existing clearing arrangements.

Objectives of Pricing

In constructing the tentative price schedule, the System has

been guided by the policies announced by the Board on July 10, 1978 in conjunction with its plan to resolve the membership problem. The Board stated that service charges should promote competitive equity among users of Federal Reserve services, encourage innovation and more efficient use of payments services, and enhance the opportunities of the private sector to compete with and improve upon Federal Reserve services. In addition, the Board announced that charges would be established with due regard to the need to assure continued efficient functioning of the payments mechanism, to avoid major disruption during the transition to a more competitive environment, and to maintain a satisfactory basic level of service nationwide.

Derivation of the Prices

The schedule in Attachment 1 shows prices approximating those that would have been in effect if service charges had been implemented in the first half of 1978. The check collection prices are based upon the cost accounting data recorded by the Planning and Control System (PACS) for the Reserve Banks. A markup of 11 per cent was applied to the total of direct and indirect PACS cost of providing the check collection service, after certain minor adjustments were made to refine the raw data.

The markup covers imputed costs similar to the capital costs and taxes that a private business firm providing the service would have borne. This markup or private-sector adjustment was calculated under the assumption that the Reserve Bank assets used in providing check collection services were financed one-half by debt and one-half by equity. The cost of servicing the debt

was assumed to be 9 per cent annually. The after tax cost of imputed equity was set at 7 per cent, equal to the 6 per cent statutory dividend that the System pays on Reserve Bank stocks held by member banks plus an added 1 per cent for reserve. The method used to construct the private-sector adjustment is described in Attachment 2.

No charge for Federal Reserve float is included in the check collection prices. There are alternative strategies for dealing with float that might be more desirable and should be considered. In addition there are uncertainties in measuring the value of float to society or to individual banks which cloud the issue of charging for float.

Tentative prices for ACH clearing and settlement services have been based upon projections of the estimated unit processing cost associated with probable future volumes of electronic payments items. Because of the inherent uncertainties, however, the preliminary ACH prices are set comfortably above the estimated long-run cost. The price for intra-ACH items equals the lowest District price for RCPC check items. These prices will permit banks, businesses, and consumers to reduce costs by converting to this new, highly efficient and secure electronic payments medium.

Level of Detail of Prices

The tentative price schedule presents the prices at the level of the Federal Reserve District. Service level differences, regional wage and transportation cost differentials, and other factors contribute to the differences among the District prices shown. Such differences may exist among offices within a District. Before a final decision is made on pricing, the System will consider the advisability of establishing different prices

for each zone in some Reserve Districts. For this reason, the System particularly hopes to receive indications of the competitiveness of the tentative price schedule compared with prices charged by others in those cases where comparable services are available in a local market. Disparities between the District average price and prices for comparable services in individual office zones could lead to inefficient volume shifts or have other undesirable effects on the payments mechanism. In such a case, adjustment of the prices may be necessary.

November 17, 1978

PRELIMINARY
 PRICE SCHEDULE
 FOR FEDERAL RESERVE CHECK COLLECTION AND ACH SERVICES
 (cents per item)

Federal Reserve District	<u>Cash Letters Deposited Directly at Processing Fed Office*</u>								<u>Cash Letters Consolidated with Shipments Sent from Other Fed Offices to Processing Fed Office</u>			<u>Automated Clearing and Settlement Services Items Deposited Directly at Processing Fed Office</u>	
	City	Country	RCPC	Mixed	Other Feds	Non-Mach.	Package Sort	Group Sort	City	Country	RCPC	Intra-ACH	Inter-ACH
Boston	1.5	--	1.5	1.9	3.7	3.9	.3	1.4	1.9	--	1.9	1.4	2.0
New York	2.2	2.4	2.0	2.0	4.5	5.6	.6	1.9	2.6	2.8	2.4	.3	1.5
Philadelphia	1.4	1.9	1.9	1.9	3.6	4.2	.6	1.5	1.8	2.3	2.3	1.4	2.0
Cleveland	1.3	--	1.9	2.0	3.5	4.1	--	--	1.7	--	2.3	1.4	2.0
Richmond	1.3	2.3	1.6	1.8	3.6	3.1	.2	--	1.7	2.7	2.0	1.4	2.0
Atlanta	1.3	--	1.5	1.6	3.4	3.9	.7	--	1.7	--	1.9	1.4	2.0
Chicago	1.5	2.3	1.6	--	4.0	3.4	.8	--	1.9	2.7	2.0	1.4	2.0
St. Louis	1.4	2.2	2.0	2.7	3.5	3.3	.5	--	1.8	2.6	2.4	1.4	2.0
Minneapolis	1.2	2.0	1.4	1.8	3.6	4.6	.6	1.2	1.6	2.4	1.8	1.4	2.0
Kansas City	1.2	1.9	1.4	2.2	3.4	3.5	--	--	1.6	2.3	1.8	1.4	2.0
Dallas	1.4	2.1	1.7	1.8	3.8	5.0	.7	1.6	1.8	2.5	2.1	1.4	2.0
San Francisco	1.3	--	1.4	--	3.6	4.2	.3	--	1.7	--	1.8	1.4	2.0
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)

* Includes Direct Send Cash Letters. Prices of other special deposit services will be available from each Federal Reserve office. Prices indicated are applicable at locations offering these services.

Attached to this schedule is a description of each of the services for which prices are shown in columns 1 through 13.

Description of Services

Cash Letters (Checks) Deposited Directly at the Processing Federal Reserve Office

The prices shown for the eight types of cash letters apply both to checks deposited by financial institutions located in the processing Federal Reserve office territory and to those checks sent directly by institutions located in other Federal Reserve office territories. (The latter institutions provide the required transportation to meet the deposit deadlines at the processing Federal Reserve office.)

The Federal Reserve intends to discontinue direct send transportation reimbursements with implementation of pricing.

City

City checks are drawn on financial institutions located in the same city as the processing Federal Reserve office. City check services are available at 43 Federal Reserve offices. Credit for city checks is available on the day of deposit at the processing Federal Reserve office if timely deposit is made (i.e., prior to the established cut-off hour. (Column 1)

Country

Country checks are drawn on banks that are geographically located outside a Federal Reserve office city and outside the area served by Regional Check Processing Center (RCPC) operations. Presentation of checks to country banks usually is made through the U.S. Postal Service. Country check services are available at 13 Federal Reserve offices. Credit for country checks is available one day after timely deposit at the processing Federal Reserve office. (Column 2)

RCPC

RCPC checks are drawn on financial institutions located in geographic areas designated as RCPC zones. Checks drawn on RCPC financial institutions are usually transported by courier for presentation. There are 44 Federal Reserve offices that offer RCPC check services. Credit for RCPC checks is available the same business day if the items are deposited by 12:01 a.m. (Column 3)

Mixed

Mixed cash letters contain checks drawn on financial institutions located in city, country, RCPC and in other Federal Reserve office territories. At present, only those member banks with less than 5,000 items to be cleared each day are eligible to deposit mixed cash letters. Mixed cash letter services are available at 27 Federal Reserve offices. Credit for checks deposited in mixed cash letters normally is available the day after deposit if the deposit is made before the processing Federal Reserve office "city check cut-off hour". (Column 4)

Other
Feds

Other Feds cash letters contain checks drawn on financial institutions located in all Federal Reserve office territories other than the processing Federal Reserve office territory. Prices for collecting these checks reflect the resources required to sort the checks at two Federal Reserve offices and to transport the items between these offices. All 46 Federal Reserve offices offer this service. Credit for Other Feds cash letters is available 1 or 2 days after timely deposit at the processing Federal Reserve office. Such credit is dependent on the availability of overnight transportation and the type of item (city, country or RCPC). (Column 5)

Non-
Machineable

Non-machineable cash letters contain checks which have rejected from the computer sorting equipment of the depositing financial institution, and those checks which are mutilated and cannot be computer processed. Prices for non-machineable checks reflect the additional manual handling required to process these exception items. Credit for non-machineable checks is deferred one day beyond normal for the same type check (e.g., credit for a city non-machineable check would be available the day after timely deposit to the processing Federal Reserve office). (Column 6)

Package
Sort

Package sort cash letters contain only checks that are drawn on one financial institution and are packaged for delivery. Federal Reserve service is limited to presentment and settlement. The package sort service is currently offered at 24 Federal Reserve offices. Later cut-off hours are applicable to package sort cash letters and credit is available on the same schedule as for city, country, and RCPC items. (Column 7)

Group
Sort

Group sort cash letters contain checks of a specific type (i.e., city, country or RCPC) which have been partially processed by the depositing financial institution. For example, the first pass through a check sorter of a multiple-pass sorting process would constitute a group sort. Seven Federal Reserve offices offer this service. Later cut-off hours are also applicable to group sort cash letters and credit is passed to depositing institutions on the same schedule as for city, country and RCPC items. (Column 8)

Cash Letters Consolidated with Shipments Sent from Other Federal Reserve
offices to the Processing Federal Reserve Office

The consolidated shipment service consists of consolidating direct send check shipments with regularly scheduled Federal Reserve inter-office check shipments. The cash letter types listed (city, country and RCPC) are the same as those described earlier. The price for these items reflects the costs associated with receiving, sorting, reconciling, settling, and presenting checks by the processing Federal Reserve Office, and the price

for transporting the checks between Federal Reserve offices. Those financial institutions authorized to use the consolidated shipment service are also authorized to direct send checks to processing Federal Reserve offices. (Columns 9, 10 and 11)

Automated Clearinghouse Services -- Items Deposited Directly at the Processing Federal Reserve Office

The prices shown, except at New York, are applicable at all Federal Reserve operated clearing and settlement facilities and include receiving, sorting, reconciling, settling and delivery of either debit or credit automated clearing house (ACH) transactions. New York prices reflect the provision of ACH clearing operations in the private sector and settlement by the Federal Reserve.

Intra ACH

Payment transactions received from local originating financial institutions for delivery to financial institutions located in the same ACH area. (Column 12)

Inter ACH

Payment transactions received from local originating financial institutions and from private sector ACH facilities for delivery to financial institutions in areas served by other ACHs. (Column 13)

BALLOT ENVELOPE

ELECTION OF DIRECTORS

of Federal Reserve Bank of New York

The marked preferential ballot should be placed in this envelope, and this envelope should then be sealed and placed in the certificate envelope.

**FEDERAL RESERVE BANK
OF NEW YORK**

Ballot

Group No. 3

December 4, 1978

This ballot and the certificate on the certificate envelope must be executed by an officer who has been authorized to cast the vote and whose designation has been duly certified to me.

The polls will open at 10 a.m. on December 5, 1978, and will close at 12 noon on Wednesday, December 20, 1978. This ballot must be returned so as to reach me before the latter time.

Failure to observe instructions will invalidate this ballot.

ROBERT H. KNIGHT,
Chairman of the Board.

VOTE FOR CLASS A DIRECTOR OF FEDERAL RESERVE BANK OF NEW YORK
for term of office from January 1, 1979 to December 31, 1981

(Section 4 of the Federal Reserve Act requires the officer casting a member bank's vote to indicate "first, second, and other choices." Where there are two candidates involved and only a first choice is made, the member bank will be deemed to have indicated the other candidate as its second choice.)

CANDIDATES		(Indicate choice by X below)	
		First Choice	Second Choice
NICHOLAS L. DEAK	President Deak National Bank Fleischmanns, N. Y.	<input type="radio"/>	<input type="radio"/>
JAMES WHELDEN	President Ballston Spa National Bank Ballston Spa, N. Y.	<input type="radio"/>	<input type="radio"/>

VOTE FOR CLASS B DIRECTOR OF FEDERAL RESERVE BANK OF NEW YORK
for term of office from January 1, 1979 to December 31, 1981

CANDIDATE	(Indicate by X below)	
JOHN R. MULHEARN	President New York Telephone Company New York, N. Y.	<input type="radio"/>

DIRECTIONS FOR RETURN OF BALLOT

1. Mark this ballot to indicate vote for each position.
2. Place marked ballot in the pink ballot envelope and seal that envelope.
3. Place sealed pink ballot envelope in certificate envelope and seal certificate envelope and execute certificate thereon.
4. Return sealed and executed certificate envelope (with sealed pink ballot envelope enclosed therein) in envelope addressed to Mr. Robert H. Knight, Chairman, Board of Directors, Federal Reserve Bank of New York, Federal Reserve P. O. Station, New York, N. Y. 10045.

CERTIFICATE ENVELOPE

**This Envelope Should Contain Only Ballot in Sealed Pink Envelope
It Will Not Be Opened Until Polls Close**

....., 1978

Group No. 3

TO MR. ROBERT H. KNIGHT,
Chairman of the Board,
Federal Reserve Bank of New York.

In accordance with section 4 of the Federal Reserve Act, as amended, I hereby certify that my votes for a class A director and a class B director of the Federal Reserve Bank of New York for terms of office from January 1, 1979 to December 31, 1981, are as indicated (by X) in the ballot sealed herein.

For

.....
(Name of Bank)

.....
(Location of Bank)

.....
(Signature of officer designated to vote. See list of member banks in Group 3 in accompanying circular.)

.....
(TITLE of Voting Officer)

MR. ROBERT H. KNIGHT,

Chairman, Board of Directors,

Federal Reserve Bank of New York,

Federal Reserve P. O. Station,

New York, N. Y. 10045

Room 1120