

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 9629]
[January 27, 1984]

WIRE TRANSFER AND NET SETTLEMENT FEES

— Increase in Off-Line Surcharges
— Proposed New On-Line Fee Structure

To All Depository Institutions, and Others Concerned,
in the Second Federal Reserve District:

The Board of Governors of the Federal Reserve System has approved a new fee schedule for the off-line funds transfer and net settlement service, which will become effective March 1, 1984. This new fee schedule represents the first change in funds transfer prices since April 29, 1982. In addition, public comment is requested on a proposal to change the fee structure for services that are provided to depository institutions with on-line connections to the Federal Reserve.

Concurrent with the announcement in March 1983 that existing fees for the funds transfer and net settlement service would remain unchanged through 1983, it was indicated that the Federal Reserve would be examining alternatives to charging only transaction fees. There are substantial fixed costs involved in operating a national telecommunications network, and these fixed costs do not vary, at least in the short-run, with changes in transaction volume. Moreover, the fixed costs are incurred to provide a basic level of service to all institutions, whether they use the capabilities of the network intensively by making many transfers or infrequently by making only a few transfers. Therefore, it appears reasonable to establish a fee structure that recognizes, at least to some extent, the fixed costs of providing on-line services.

The proposed fee schedule establishes a set of fixed monthly fees for on-line institutions by type of connection, i.e., dial-up, leased line, or computer interface. This would be a uniform national fixed fee and would be assessed once each month for each separately addressable on-line connection with the Federal Reserve. Only one fixed fee would be paid per connection, regardless of the number of services used.

An important feature of the fixed fee schedule is the associated proposal that the basic transaction fee for the funds transfer service would be reduced at least from \$0.65 to \$0.60, concurrent with implementation of the new schedule. This means that all depository institutions would benefit from lower transactions fees as fewer costs would need to be recovered from this fee component. While the proposal calls for an initial reduction in funds transfer transactions fees only, it is possible that similar reductions could apply to other services in the future. (In this connection, it should be noted that this Bank, as part of its ongoing cost control efforts, is reviewing its current policies regarding back-up communications arrangements for computer interfaces and leased-line (DART) terminals and may change the practice of absorbing redundant line and telephone connection charges.) The proposed implementation date for the new fee structure is June 28, 1984.

We believe that the proposed fixed fee structure for on-line access represents an orderly approach to offsetting, in part, the costs of providing the basic communications network required for such services. Your comments on the proposal are most welcome, and we would like to answer any questions you may have. Your comments must be submitted by March 17, 1984; comments on the proposal, or questions on the new surcharges or the proposal, may be directed to Henry F. Wiener, Assistant Vice President (Tel. No. 212-791-5079), or Robert W. Dabbs, Manager, Funds Transfer Department (Tel. No. 212-791-8475).

Printed on the reverse side is the text of the Board's press release. In addition, enclosed — for depository institutions in this District — are the Board's official notices in this matter; they will be published in the *Federal Register* and additional copies may be obtained from our Circulars Division (Tel. No. 212-791-5216).

ANTHONY M. SOLOMON,
President.

(Over)

Board Press Release on Wire Transfer and Net Settlement Fees

The Federal Reserve Board has published, for public comment, a proposed revision to the fee structure for the Federal Reserve's wire transfer of funds service. The proposal includes a reduction of the basic fee for originating or receiving a wire transfer of funds from \$0.65 to \$0.60 per transfer.

At the same time, the Board proposed a fixed monthly fee for all depository institutions that have an electronic connection with the Federal Reserve.

The fixed monthly fee charges would be:

<i>Type of Connection</i>	<i>Monthly Fees</i>	
	<i>All Priced Services, Except Dedicated ACH and Securities Transfer Connections¹</i>	<i>Dedicated ACH Connections²</i>
Computer Interface	\$1,400	\$840
Leased Line	\$ 350	\$210
Dial-up	\$ 75	\$ 45

Comment is requested by March 17, 1984.

Revisions to the off-line³ surcharges for the Reserve Bank's wire transfer of funds and net settlement services have been made, to become effective March 1. The new fee schedule is:

<i>Wire Transfer of Funds</i>		<i>Net Settlement</i>	
Off-Line Origination	\$5.50	Off-Line Settlement	\$8.00
Telephone Advice	\$3.00	Telephone Advice	\$3.00

Pending Board action, the basic transfer fee, currently \$0.65, will remain in effect for all on- and off-line funds transfers.

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- 1 Approximately 60 on-line connections are used by depository institutions solely for securities transfers. No fixed monthly fees will be assessed at this time for these dedicated connections, pending a review of the fee structure for securities transfers later this year.
 - 2 The automated clearing house (ACH) service is priced under an incentive pricing policy. The fees proposed for dedicated ACH connections reflect a 60 percent recovery rate for the service.
 - 3 Off-line institutions do not have an electronic connection with the Federal Reserve and, therefore, must originate their transactions and be advised of their settlement by phone.

FEDERAL RESERVE SYSTEM

Docket No. R-0504

FEE SCHEDULES FOR FEDERAL RESERVE BANK SERVICES

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Fee Schedules for Wire Transfer of Funds and Net Settlement Services.

SUMMARY: The Monetary Control Act of 1980 (Title I of Public Law 96-221) requires that schedules of fees be established for Federal Reserve Bank services. Revised fee schedules for the wire transfer of funds and net settlement services were implemented effective April 29, 1982, and continued through 1983. The Board has approved an increase in the off-line surcharges for the wire transfer of funds and net settlement services.

EFFECTIVE DATE: March 1, 1984.

FOR FURTHER INFORMATION CONTACT: Elliott C. McEntee, Associate Director (202/452-2231) or Florence M. Young, Program Manager (202/452-3955) Division of Federal Reserve Bank Operations; Gilbert T. Schwartz, Associate General Counsel (202/452-3625) or Elaine M. Boutilier, Attorney (202/452-2418), Legal Division, Board of Governors of the Federal Reserve System, Washington, D. C. 20551.

SUPPLEMENTARY INFORMATION: The Monetary Control Act of 1980 ("Act") requires that fee schedules be developed for Federal Reserve Bank services based on pricing principles established by the Board (12 U.S.C. § 248a). The current fee schedule for

[Enc. Cir. No. 9629]

the Federal Reserve's wire transfer of funds and net settlement services was implemented on April 29, 1982, and was reviewed by the Board on March 17, 1983. As indicated in the notice continuing the existing fee schedule (48 Fed. Reg. 12135), a comprehensive review was conducted during 1983 of the fee structure for the wire transfer of funds and net settlement services. These services include both on-line services--i.e., transfers made through electronic connections--and off-line services--i.e., transfers made upon the receipt of a telephone request.

This review concluded that the off-line services provided to depository institutions are labor intensive and that the current off-line surcharges are not fully recovering the costs incurred in providing the services. To enable the Reserve Banks to recover the costs of off-line services, the Board has determined that the following surcharges will apply for off-line services beginning March 1, 1984:

<u>Wire Transfer of Funds</u>		<u>Net Settlement</u>	
Off-line Origination	\$5.50	Off-line Settlement	\$8.00
Telephone Advice	\$3.00	Telephone Advice	\$3.00

The current fees are \$3.50 for an off-line origination of a funds transfer, \$5.00 for an off-line origination of a net settlement, and \$2.25 for a telephone advice of a funds transfer or net settlement entry. As a result of the changes, it is anticipated that annual off-line revenue will be approximately \$ 8 million. The current basic fee for transfers

originated and received (\$0.65 per transfer) and net settlement entries (\$1.30 per entry) will remain in effect until a new fee schedule is approved by the Board later this year. It is proposed that the basic transaction fee for transfers originated and received be reduced to \$0.60 and a new fixed monthly fee be assessed to on-line institutions based upon the type of electronic connection that is installed between the institution and the Federal Reserve Bank. (See Proposed Fee Schedules for Wire Transfer of Funds and Net Settlement Services, published simultaneously with this notice.)

By order of the Board of Governors of the Federal Reserve System, January 17, 1984.

(signed) William W. Wiles

William W. Wiles
Secretary of the Board

FEDERAL RESERVE SYSTEM

(Docket No. R-0505)

FEE SCHEDULES FOR FEDERAL RESERVE BANK SERVICES

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed 1984 Fee Schedules for Wire Transfer and Net Settlement Services.

SUMMARY: The Monetary Control Act of 1980 (Title I of Public Law 96-221) requires that schedules of fees be established for Federal Reserve Bank services. Revised fee schedules for the wire transfer of funds and net settlement services were implemented effective April 29, 1982, and continued through 1983. The Board now seeks comment on the following new fee structure and new prices for these services to be implemented in 1984:

<u>Type of Connection</u>	<u>Monthly Fees</u>	
	All Priced Services, Except Dedicated ACH and Securities Transfer Connections ^{1/}	Dedicated ACH Connections ^{2/}
Computer Interface	\$1,400	\$840
Leased Line	\$ 350	\$210
Dial Up	\$ 75	\$ 45

^{1/} A number of on-line connections are used by depository institutions solely for securities transfers. No fixed monthly fees will be assessed at this time for these dedicated connections, pending a review of the fee structure for the securities transfer service later this year.

^{2/} The ACH service is priced under an incentive pricing policy. The fees proposed for dedicated ACH connections reflect a 60-percent recovery rate for the service.

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In conjunction with implementing fixed monthly fees for electronic connections with the Federal Reserve, it is also proposed that:

- the fee for originating or receiving a wire transfer of funds be reduced from \$0.65 to \$0.60 per transfer; and
- the fee for originating a securities transfer be maintained at \$3.00 per transfer.

DATE: Comments must be received by March 17, 1984.

ADDRESS: Comments, which should refer to Docket No. R-0505, may be mailed to: William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N. W., Washington, D. C. 20551, or delivered to room B-2223 between 8:45 a.m. and 5:15 p.m.

Comments received may be inspected in room B-1122 between 8:45 a.m. and 5:15 p.m., except as provided in section 261.6(a) of the Board's Rules Regarding Availability of Information (12 C.F.R. § 261.6(a)).

FOR FURTHER INFORMATION CONTACT: Elliott C. McEntee, Associate Director (202/452-2231), or Florence M. Young, Program Manager (202/452-3955), Division of Federal Reserve Bank Operations; Gilbert T. Schwartz, Associate General Counsel (202/452-3625), or Elaine M. Boutilier, Attorney (202/452-2418), Legal Division, Board of Governors of the Federal Reserve System, Washington, D. C. 20551.

SUPPLEMENTARY INFORMATION: The Monetary Control Act of 1980 requires that fee schedules be developed for Federal Reserve Bank services based on pricing principles established by the Board (12 U.S.C. § 248a). The Board, in accordance with the requirements of the Act, has established fee schedules for the wire transfer of funds and net settlement services. The current fee schedule, implemented on April 29, 1982, was retained because estimates of the volume of funds transfers and the total costs, including the PSAF, indicated that revenues would cover the 1983 costs of providing the service. The Board noted, at that time, that a comprehensive review of the fee structure for these services had been undertaken and that if significant changes were determined to be necessary, public comment would be solicited (48 Fed. Reg. 12135, March 23, 1983). The results of that review indicate that it is appropriate to revise the existing fee structure for the wire transfer of funds service in order to recover anticipated costs for 1984. Accordingly, the Board is requesting public comment on a revised fee structure.

For the period January through November, 1983, total costs, including the PSAF, amounted to \$52.0 million and total revenues amounted to \$52.4 million, resulting in a modest net revenue surplus of approximately \$400 thousand. The volume of funds transfers originated amounted to 34.7 million during the eleven month period, an increase of 8 percent over the same period in 1982. Cost, volume and revenue data for December,

1983, are not yet available. However, it is expected that a modest net revenue surplus will be realized for the year 1983.

The total costs, including a 16 percent PSAF, of providing the wire transfer of funds and net settlement service are projected to be \$62.4 million in 1984. If the current fee schedule for these services were retained, projected annual revenues would amount to \$58.9 million, resulting in an estimated net revenue shortfall of \$3.5 million. Therefore, in order to match costs and revenues, the Board proposes to implement fixed monthly fees and lower basic transaction fees on June 28, 1984.^{3/} As a result of these changes, 1984 revenues of about \$62.9 million are anticipated for the wire transfer of funds and net settlement service, resulting in a net revenue surplus of \$500,000.

Cost Structure

The Reserve Banks provide electronic services to four classes of users: (1) institutions with computers linked directly to Federal Reserve computers, (2) institutions using terminals or micro-computers that are linked to the Federal Reserve via dedicated, leased lines, (3) institutions using terminals or micro-computers that are linked to the

^{3/} In this connection, the Board has approved, effective March 1, 1984, an increase in the off-line surcharges for the wire transfer of funds and net settlement services. (See Federal Register notice published simultaneously with this notice.)

Federal Reserve via public telephone lines or dial-up facilities, and (4) institutions without electronic connections that initiate and receive transfers of funds and securities over the telephone or, in the case of the automated clearing house ("ACH"), physically deliver and receive transactions. The following table indicates the approximate number of electronic links to the Federal Reserve as of December 31, 1983:

Number of Electronic Connections

<u>Type</u>	<u>Number</u>
Computer Interface	100
Leased Line	1,300
Dial-Up	2,700
ACH Data Link	200 ^{4/}

During 1983, on-line users of the Federal Reserve's electronic services originated about 98 percent of all funds transfers and about 99 percent of all securities transfers. In the case of the ACH service, on-line institutions originated less than 25 percent and received only 10 percent of commercial ACH transactions.^{5/}

The on-line electronic payments services offered to depository institutions by the Reserve Banks are capital

^{4/} Unlike other electronic connections, ACH data links are frequently shared. Approximately 2,000 depository institutions are currently served by the 200 data links that are installed.

^{5/} On September 23, 1983, a revised fee schedule for the ACH service was published for public comment. (48 F.R. 44650) The proposal to implement fixed monthly fees for electronic services will have a minor impact on the proposed ACH fee schedule since a relatively small percentage of ACH transactions are originated and received via on-line connections.

intensive services and fixed costs are high relative to total costs. The Federal Reserve has developed sophisticated intradistrict and interdistrict data communications networks, invested in state-of-the-art data communications and data processing equipment, and is developing enhanced automated systems for each of its electronic payments services.

Certain elements of the Federal Reserve's data communications and data processing costs would be incurred in order to offer electronic payments services even if no on-line connections with the Federal Reserve were offered. However, other costs, in particular the costs associated with intradistrict communications networks, would not be incurred if on-line connections were not offered. Intradistrict communications networks consist primarily of the lines, circuits, and modems used to link depository institutions to the Federal Reserve. During 1983, it is estimated that the costs of the local networks that were allocated to priced services amounted to \$6 to \$7 million.

Depository institutions that have computer-interface connections with the Federal Reserve originated and received more than 60 percent of the total number of funds and securities transfers during 1983. These institutions expend considerable resources to purchase and install computer-to-computer interfaces, and Federal Reserve staff devotes considerable time to testing the equipment. To ensure that the high transaction volumes are processed efficiently,

high speed, dedicated lines link these institutions to the Federal Reserve. In addition, the capacity of the Federal Reserve's data processing and data communications equipment is largely dictated by the volume of transactions originated and received by these high volume users.

Institutions using terminals or micro-computers that are linked via leased lines accounted for nearly 30 percent of all funds and securities transfers during 1983. Computer software necessary to interface with the Federal Reserve's applications software is provided by the Federal Reserve. However, Federal Reserve development and support costs are spread over a relatively broad base because the majority of institutions within a Federal Reserve District use the same equipment. In many cases, the lines leased from common carriers serving individual institutions feed into one circuit linked with the Federal Reserve and, generally, have less capacity than the lines used by institutions with computer interfaces.

During 1983, institutions using terminals or micro-computers linked via public telephone lines, that is, dial-up connections, accounted for about 8 percent of total transaction volume. The Federal Reserve provides the necessary software to support their use of electronic services. However, the lines connecting these institutions to the Federal Reserve are typically public telephone lines that require institutions to dial the Federal Reserve to originate or receive transactions.

In summary, the costs to the Federal Reserve of serving individual institutions with computer interfaces tend to be higher than for those with leased-line connections, which are higher than for those with dial-up connections. However, the three classes of on-line institutions use the Federal Reserve's electronic services with different intensities. When fixed costs, such as data communications costs, are spread over the high transaction volumes processed by computer-interface institutions, the per transaction impact of fixed costs tends to be lower. Conversely, for lower volume, leased-line or dial-up institutions, the per transaction impact of fixed costs tends to be higher.

Alternatives

At present, the fees assessed for the wire transfer of funds, securities transfer, and the ACH services are generally based on the average cost of processing a transaction.^{6/} Basing fees on average processing costs is an appropriate pricing methodology when a high proportion of total production costs are variable. In the case of the Federal Reserve's electronic services, a high proportion of costs are fixed relative to total costs. Thus, some modification to the

^{6/} On September 23, 1983, a revised ACH fee structure was published for public comment that proposed instituting fixed deposit and receiver handling fees reflecting fixed costs associated with these activities. (48 F.R. 44650)

current fee structures for electronic services could result in fee structures that more closely resembled the cost structure of the services.

To achieve this objective, the following alternatives were reviewed:

- assessing variable transaction fees for wire transfers of funds and securities services based on the type of on-line connection used by a depository institution;
- assessing on-line institutions the actual costs of the lines and modems that are installed to provide electronic payments services; and
- assessing fixed monthly fees that would vary by type of on-line connection and would, on average, recover the cost of intradistrict communications networks.

Based on the staff study, the first alternative, the use of variable transaction fees, would result in a range of transaction fees, with the highest being assessed to institutions using dial-up connections and the lowest fees being assessed to institutions with computer-interface connections, due to differences in transaction volumes among the three classes of on-line institutions. While the use of variable transaction fees would reflect the costs of providing electronic payments services more accurately than the current fee structures, it still would not fully reflect the fixed cost

structure of the Federal Reserve's electronic payments services. Moreover, variable transaction fees would also provide depository institutions an incentive to upgrade the type of connection linking them with the Federal Reserve in order to reduce the variable costs they incur in using Federal Reserve services. Since dedicated leased-line connections are more costly to the Federal Reserve than shared dial-up facilities and computer-interface connections are more costly than leased-line connections, moves to upgrade connections on the part of depository institutions would increase rather than reduce the overall costs of the Federal Reserve's electronic payments services.

The alternative of passing through actual line and modem costs to individual depository institutions would provide an objective means of assessing fees. It would also provide institutions with an incentive to select the most cost-effective, on-line connection based on the volume of transactions handled. However, telephone rates are frequently based on distance and may vary from region to region, resulting in disparate charges to institutions within the same class. Furthermore, the AT&T divestiture creates a great deal of uncertainty regarding the fees that would be assessed. Finally, determining the costs that would be assessed to institutions sharing leased lines or using dial-up networks would be complex. Therefore, this approach was regarded as unacceptable due to its complexity and the unpredictability of telephone rates.

The third alternative, assessing fixed monthly fees to on-line institutions that vary by type of connection, like passing through actual line and modem costs, would be based on clearly identifiable fixed costs and would result in a fee structure that reflects the fact that high fixed costs are incurred in providing electronic services. Setting fees that, on average, would recover the costs of intradistrict communications networks would generate revenues comparable to those generated under the second alternative. Although the effect of fixed monthly fees on institutions with on-line connections would vary within each connection category depending upon an institution's volume of transactions, variability in fees charged due to differences in telephone rates would not occur. Therefore, the use of fixed fees would remove the uncertainty regarding charges that would exist under the pass-through proposal. This alternative also should provide incentives for depository institutions to select cost-effective, on-line connections and, thereby, contribute to reductions in the overall costs of the Federal Reserve's electronic services. Accordingly, the Board believes that this alternative is the most reasonable basis for recovering fixed costs, and the following proposed fee structure incorporates this approach.

Monthly Fees

<u>Type of Connection</u>	<u>All Priced Services, Except Dedicated ACH and Securities Transfer Connections</u>	<u>Dedicated ACH Connections</u>
Computer Interface	\$1,400	\$840
Leased Line	\$ 350	\$210
Dial Up	\$ 75	\$ 45

Under the Board's proposal, a fixed monthly fee would be assessed for each separately addressed connection that is installed between a depository institution and the Federal Reserve. When an institution uses one connection to access the Federal Reserve for all types of electronic services, one fee would be assessed based on the type of connection. However, if a depository institution uses a computer-interface connection for funds transfer services and a dial-up connection for ACH services, and each connection is separately addressable, the institution would be assessed the monthly fee for each connection. It should be noted that fixed monthly fees would be assessed to all on-line institutions--those that use their own equipment to interface with the Federal Reserve and those that lease equipment from the Federal Reserve.

Because the ACH service is priced under an incentive pricing policy, it is proposed that the fixed monthly fees for communications links used solely for ACH transactions should be included under that policy. Specifically, the ACH fees recently published for public comment were set to recover 60 percent of the costs of providing commercial ACH services. That proposal also included fixed receiver handling fees for

both ground and electronic delivery. If fixed monthly fees for on-line connections with the Federal Reserve are implemented, it is proposed that the receiver handling fee for electronic delivery, if one is adopted, be eliminated in order to avoid double charging users of ACH services.

There are a number of on-line connections used by depository institutions solely for securities transfers. At this time, no fixed monthly fees are proposed for these dedicated connections, pending a review of the fee structure for the securities transfer service later this year.

Currently, some Federal Reserve Banks' terminal lease fees include a component that is intended to recover a portion of intradistrict communications and other costs. Some Reserve Banks also assess fixed monthly fees to on-line institutions that own their own terminals or micro-computers rather than leasing them from the Federal Reserve. If the proposed fixed monthly fees for on-line institutions are implemented, it is proposed that these Reserve Banks would discontinue assessing the fixed monthly fees that they now charge to on-line institutions.^{7/}

At this time, the Reserve Banks project that intradistrict communications costs will amount to approximately

^{7/} Existing fees assessed for terminals used exclusively for securities transfers will continue in effect pending a review of the fee structure for securities transfers later this year.

\$8.3 million during 1984, an increase of 20 to 40 percent over 1983 costs. The relatively substantial increase in costs is based on estimates of the effects of the AT&T divestiture, which are highly tentative at this time, as well as growth in the number of on-line connections with the Federal Reserve. Based on the projected number of each type of on-line connection with the Federal Reserve during 1984, it is estimated that the proposed fixed fees would generate annual revenues of approximately \$8.0 million.^{8/}

As a result of these changes, it is also proposed that the following transaction fees be implemented:

Basic Transfer Originated	\$0.60
Basic Transfer Received	\$0.60
Net Settlement Entries	\$1.30

This proposal would result in a \$0.05 reduction in the basic fee for originating or receiving a funds transfer. No change is proposed for the fee for net settlement entries. This new transaction fee would be implemented at the same time fixed monthly fees are implemented, which is proposed to be June 28, 1984.

By order of the Board of Governors of the Federal Reserve System, January 17, 1984.

(signed) William W. Wiles

William W. Wiles
Secretary of the Board

^{8/} Approximately 70 percent of the revenue generated through fixed monthly fees would be allocated to the wire transfer of funds and net settlement service.