

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 9834]
[April 17, 1985]

INTERTERRITORY CHECK FLOAT
Modification of Accounting Methodology

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

I am pleased to announce that the Federal Reserve System has modified its accounting methodology for interterritory check float recovered using the fixed availability option, and that the effect of this modification will be a reduction in float charges to depositors. This change became effective for float incurred beginning March 28, 1985. (The official notice of this action by the Board of Governors of the Federal Reserve System, which appears on pages 3 and 4 of our Circular No. 9830, dated April 4, 1985, is reprinted on the reverse side of this circular.)

Under previous fixed availability procedures, a depositing institution was given 100 percent credit for its interterritory check deposits according to local availability schedules. The amount of float later determined by actual collection performance was then fully recovered directly from the depositing institution. However, concern has been expressed that these procedures fail to take into consideration the effect of float on an institution's reserve requirements, and thus result in overcharging for float by the Federal Reserve. For example, when an institution using the fixed availability option sends checks to a Federal Reserve office, it receives full credit for the checks deposited, but its cash items in the process of collection (CIPC) balance is reduced by the amount of the credit. Since CIPC may be deducted from reservable transaction balances in calculating an institution's reserve requirement, this reduction tends to raise the institution's required reserves. When the institution is later charged for the float, no adjustment is made for the cost of the increased reserve requirement incurred by the depository institution. As a result, the charge for float may exceed the net benefit originally received from the float. This increased reserve requirement does not affect depositors using the fractional availability crediting option. Under fractional availability, credit for a fraction of the dollar value of each cash letter is deferred and therefore is reflected in its CIPC. The depositing institution may then deduct from its reservable liabilities the deferred portion of the cash letter.

In response to the concerns expressed by depository institutions, the Board of Governors has determined to modify the System's accounting procedures for float pricing purposes to take into account the effect that float would have on their reserve requirements if Reserve Banks were required to hold reserves. These procedures will result in the Federal Reserve accounting for float in a manner more closely conforming to the accounting practices of correspondent banks. Net check float will be deducted from the amount of clearing balances maintained with the Federal Reserve before the Federal Reserve's imputed required reserves are determined. *The effect of this action will be to permit a reduction of twelve percent in float charges to depositors, effective with float incurred beginning March 28, 1985.*

The Board has emphasized that, in spite of these reductions in float charges to depository institutions, the Federal Reserve's internal accounting procedures will continue to recognize as a cost to the Federal Reserve the full value of float at the Federal funds rate, as required by the Monetary Control Act.

Questions regarding this matter may be directed to Donald R. Anderson, Manager, Accounting Department (Tel. No. 212-791-5250) or Paul L. McEvily, Manager, Check Services Department (Tel. No. 212-791-6551).

E. GERALD CORRIGAN,
President.

(OVER)

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
Notice Regarding Accounting for Interterritory Check Float

[Docket No. R-0525]

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The Board has also approved several modifications to the procedures for accounting for Federal Reserve check float. Three of the commenters responding to the proposal to eliminate the fractional availability credit option commented that the remaining fixed availability crediting procedures do not take into consideration the effect of float recovery on required reserves, resulting in overcharging for float.

Depository institutions are permitted to deduct the amount of their cash items in the process of collection ("CIPC") from the amount of gross transaction accounts in computing required reserves. 12 CFR 204.3(f)(1). When a depository institution deposits a check with the Federal Reserve for collection, the amount of the check is included in the institution's gross transaction accounts subject to reserve requirements, and is offset by a corresponding CIPC deduction. The CIPC deduction is provided in recognition of the fact that the depository institution has not yet been given credit by the Federal Reserve for the check. When credit for the check is given, the institution loses the CIPC deduction and its reserve requirements

increase. If credit is given before the check is collected by the Federal Reserve, float is generated. When the institution is later charged by the Federal Reserve for the float, no adjustment is made for the cost of the increased reserve requirement, with the result that the float charge exceeds the benefit to the institution of the float.

In response to the concerns expressed by depository institutions, the Board has determined to modify the System's accounting procedures to take into account the effect of float on the reserve requirements to which Reserve Banks would be subject if they were required to hold reserves. Net check float will be deducted from the amount of clearing balances maintained with the Federal Reserve before the imputed required reserves are determined.

This procedure will result in the Federal Reserve accounting for float in a manner conforming more closely to the accounting practices of correspondent banks. The effect of this modification will be to reduce the Reserve Bank's imputed reserve requirement and increase their earning assets.¹ The interest on these additional earning assets will then offset part of the cost of

float that is to be charged back to depository institutions.

The Board wishes to emphasize that the Federal Reserve's accounting procedures as modified will continue to recognize as a cost to the Federal Reserve the full value of float at the federal funds rates, as required by the MCA. The accounting change approved by the Board will reduce explicit float charges to direct and consolidated sending institutions by 12 percent. Further, the float component of per-item fees will also be lowered by 12 percent. The modifications are expected to have a minimal impact on the Federal Reserve's per-item fees since the float component of the base used to calculate per-item fees is less than 3 percent of the total. A 12 percent reduction in this component will reduce the total to be recovered by only 0.25 percent. Federal Reserve income statements will be amended to reflect these accounting changes.

By order of the Board of Governors of the Federal Reserve System, March 20, 1985.
William W. Wiles,
Secretary of the Board.
[FR Doc. 85-7052 Filed 3-25-85; 8:45 am]

¹ In March 1984 the Board approved an adjustment to the balance on which earnings credits are paid on clearing balances to reflect the reserve requirements that would apply if the balances had been held with a correspondent bank. An imputed reserve burden was also imposed upon the Federal Reserves' revenues from clearing balances. 49 FR 11251 (March 26, 1984).

(Reprinted from Federal Register of March 26, 1985)