

Winter 1995  
News and Views  
for  
Eighth District Bankers

## Fed Realigns Financial Services

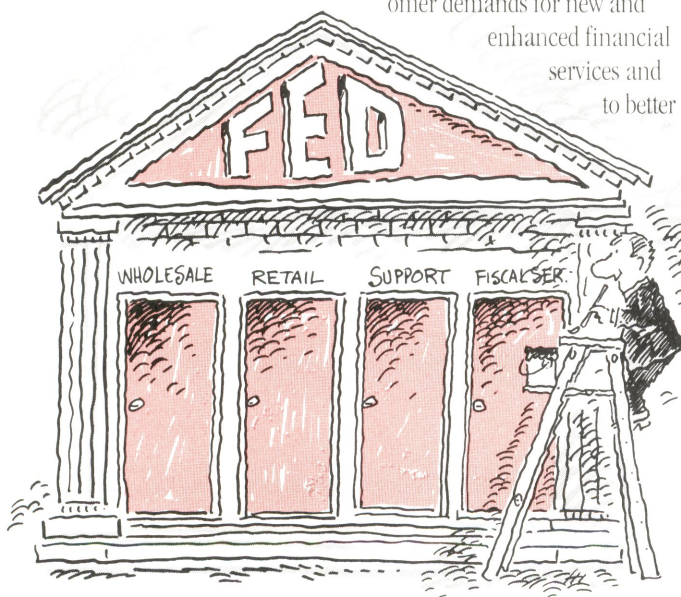
The Federal Reserve Bank of St. Louis, in concert with the Fed System, recently reorganized its financial services functions to respond more quickly to customer demands for new and enhanced financial services and to better

coordinate and integrate financial services across the Federal Reserve System.

With the exception of a few staff changes, business relationships established between Fed St. Louis and financial institutions in the Eighth District will remain the same.

At the national level, Fed financial services were realigned into four new product offices: retail, wholesale, cash/fiscal and support services (see sidebar for specific services).

Late last year, the St. Louis Fed implemented a new management structure to reflect, in part, this realignment (see organization chart on page 2). In addition, it consolidated all customer



### Service Lines Redefined

#### Wholesale Services

Fedwire, book entry

#### Retail Services

Check and automated clearing house (ACH)

#### Support Services

Accounting and automation (Fedline®, etc.)

#### Cash/Fiscal Services

Currency/coin, savings bonds, Treasury, Tax and Loan, noncash

support functions into a new Employee and Customer Relations Department.

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## Treasury Modernizes Tax Payment System

In October 1994, the Treasury's Financial Management Service and the Internal Revenue Service announced plans to start converting the current tax payment system to electronics in 1995.

The six-phase plan requires corporations with more than \$20,000 in employment taxes

to submit tax payments electronically through a financial institution or a Treasury financial agent.

Phase one of the conversion effort began on Jan. 1, when financial institutions, representing approximately 800 corporations, started processing tax payments through either

Fedwire or the Automated Clearinghouse. These corporations and their affiliates pay more than \$78 million annually in employment taxes.

*(continued on page three)*

# Feditorial

## Integrity and Accountability at the St. Louis Fed



Mary H. Karr

**T**he public's trust in our nation's banking system depends, in part, on its confidence in the ethics of bankers and bank regulators.

Recently, the St. Louis Fed revised its Code of Conduct for all employees.

As the new code affirms positions we've always held, it will be almost invisible to those with whom we do business.

Our code reflects a desire to be impartial and fair in our business dealings, whether we are acting as banking supervisors, as fiscal agents for the U. S. Treasury Department, as providers of payments services, or as buyers of goods and services for our own use.

The ethical principles we follow guide us in our daily dealings with the public to avoid

even the hint or appearance of bias. We ask all employees to think about, recognize and avoid even trivial situations that could raise any question about our impartiality. For example, we expect employees to refuse all but the most inexpensive items that may be offered by a financial institution or vendor.

In addition, we expect our staff to avoid outside activities that could conflict with the unbiased performance of their jobs. This may limit our investments, our part-time jobs, even our hobbies or political activities.

With this code we've renewed our resolve to continue a long tradition of independence and impartiality.

*Mary H. Karr is senior vice president of the Legal and Public Affairs Division and general counsel of the Federal Reserve Bank of St. Louis.*

### Services Realigned

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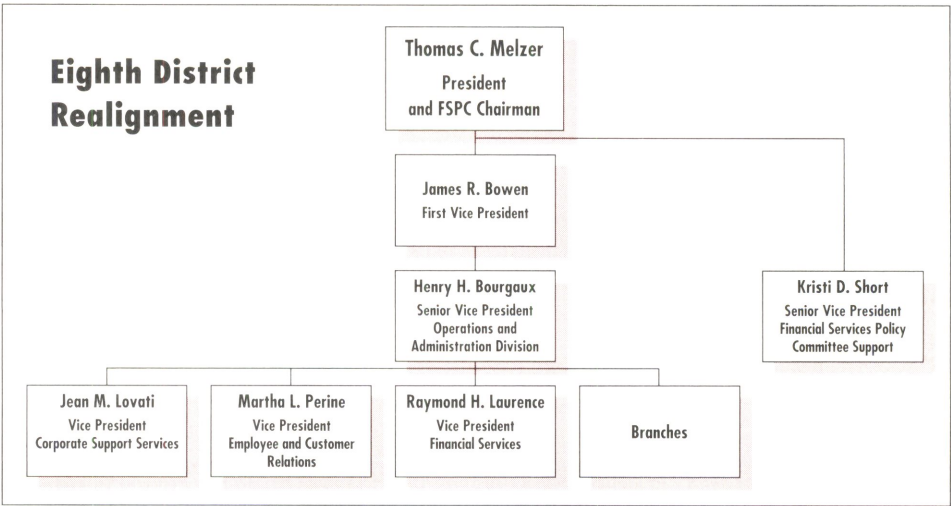
In conjunction with the financial services realignment, a new national-level Financial Services Policy Committee (FSPC) was created to establish strategic direction and policies for the Federal Reserve's financial services. St. Louis Fed President Tom Melzer was named chairman of this new committee, which oversees the product offices.

All Reserve Banks will continue to participate on System advisory groups, providing input on local issues and helping develop System-level plans.

Strategic planning will be the first order of business for the new FSPC and other man-

agement groups. The Fed intends to consult with depository institutions on issues

affecting the future shape of payments systems to ensure their needs are effectively met.







Mark D. Vaughn

## The Limited Value of Race and Gender Data in Small Business and Farm Loans

In September, the Federal Reserve Board solicited comments on a revised version of the interagency Community Reinvestment Act (CRA) proposal. The new version contains a provision requiring banks to request race and gender data from applicants for small business and small farm loans. In this unique market, however, such data are unlikely to help supervisors identify banks with lending records that suggest discrimination.

As our experience with Home Mortgage Disclosure Act (HMDA) data has demonstrated, the statistical analysis of race and gender data has drawbacks. Currently, supervisors use a three-stage statistical approach to look for evidence of discrimination in the mortgage-lending market. In the first stage, they analyze HMDA data for a given institution with a technique called regression analysis. This analysis uses three variables reported under HMDA—the race of the borrower, the income of the borrower and the loan amount requested by the borrower—to predict the probability that the institution will approve a mortgage loan.

If stage one reveals a strong statistical relationship between race and probability of loan acceptance, supervisors collect additional data on variables related to mortgage loan evaluation and conduct another regression analysis. If the second-stage regression still suggests possible discrimination, supervisors continue to a third stage. In the third stage, the regression model is used to match up pairs of applicants

with similar characteristics except for race; examiners then compare approval rates for these matched pairs.

The lack of a relationship between race and loan acceptance in stage one or stage two indicates that the institution probably does not discriminate and exempts it from further scrutiny. In this way, supervisors can concentrate their examiner resources on banks whose lending practices are most likely to result in discrimination.

**Collecting enough data to reduce false signals of discrimination would prove prohibitively expensive, if not impossible.**

Regression models can, however, falsely signal discrimination. False signals occur when the models exclude variables that are important in lending decisions. For instance, the stage-one regression on HMDA data excludes credit history. If minorities have weaker credit histories, on average, than other applicants, the regression model will signal racial discrimination when, upon closer examination, no difference in treatment actually exists.

In principle, supervisors could eliminate false signals completely by including all relevant explanatory variables in the second-stage regression. However, accounting properly for all the variables relevant to underwriting criteria is difficult and expensive—even for a relatively homogeneous market like the mortgage market.

False signals in the small business and small farm loan market are an even bigger problem than they are in the mortgage market. Compared with mortgage loans, small business and small farm loans are highly idiosyncratic. Small business loans, for example, vary widely in funding terms, payment structures and collateral arrangements. Given these characteristics, using only race, income and loan amount to predict loan acceptance in stage-one regressions will likely generate numerous false signals of discrimination. Moreover, collecting enough additional data to reduce false signals in the second-stage regressions would prove prohibitively expensive, if not impossible. The large number of false signals virtually eliminates the advantage of this approach to detecting discrimination.

Regression models aside, the regulation, as written, does not explicitly state how race and gender data are to be used in calculating an institution's CRA rating. This fact, combined with the data's extremely limited value in the small business and farm market, indicates that the additional burden imposed on institutions cannot be justified.

*Mark D. Vaughn is a senior manager and economist in the Banking Supervision and Regulation Division at the Federal Reserve Bank of St. Louis.*



# Regional Roundup

## OUT FOR

## COMMENT

The following are Federal Reserve System proposals currently out for comment:

■ **Proposed amendment to Regulation K (International Banking Operations). Comments due by February 13. (Docket No. R-0862)**

■ **Proposed revisions to the Federal Reserve Board's official staff commentary for Regulation B (Equal Credit Opportunity). Comments due by February 15. (Docket No. R-0865)**

■ **Additional comments on proposal to extend Fedwire hours, specifically, potential benefits, costs and market implications of early Fedwire opening. Comments also sought on new service capabilities and a firm closing time for Fedwire book-entry securities. Comments due by April 28. (Docket No. R-0866)**

*Direct all comments to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th St. and Constitution Ave., N.W., Washington, D.C. 20551.*

## Greenwood, Leslie Join St. Louis Bank

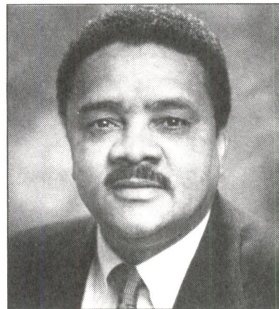
Lynn M. Greenwood and William C. Leslie both joined the official ranks of the St. Louis Fed in December 1994. Greenwood was appointed vice president of the Public Affairs Department. During her 20-year career in communications and public relations, Greenwood



served as director of corporate relations at the Federal Home Loan Mortgage Corp. and most recently, as public relations director for A.G. Edwards & Sons Inc., St. Louis.

Leslie was appointed vice president of the Bank's newly formed Retail Operations area, which includes check and ACH

processing. During Leslie's 20-plus years in banking, he



served as senior vice president of operations at Landmark Bank, and most recently at United Missouri Bank, both in St. Louis.

## New Community Profile Available

Later this month, the St. Louis Fed will release a new community profile of the lower Mississippi delta region.

The profile includes an analysis of census and other demographic data, along with information on community credit needs obtained through interviews with community organizations, government

officials and residents in the area.

Descriptions of organizations and programs that help address credit needs will also be provided.

Counties in the following areas are covered in the profile:

- 7 in northeast Arkansas
- 8 in southeast Arkansas
- 11 in western Kentucky
- 11 in southern Illinois
- 8 in northwest Tennessee
- 11 in northwest Mississippi
- 12 in southwest Mississippi
- 6 in northeast Missouri.

Copies of the profile will be mailed to CRA officers at all financial institutions in the Eighth District portion of the lower Mississippi delta region.

Stay tuned for additional profiles coming soon. A community profile of the Little Rock, Ark., MSA is being developed and will be available to banks in that area later this year.

## Renaissance in Rural America

**A**re you ready for the renaissance of rural America? The conference, that is.

On March 7-8, the Federal Reserve Banks of St. Louis, Atlanta, Dallas and Richmond are sponsoring a conference at the Peabody Hotel in Memphis, Tenn., that focuses on rural economic development.

The Renaissance Conference will cover a wide range of topics including: common themes in rural development, utilizing

secondary markets, strategic planning for rural community diversification and financing small businesses.

St. Louis Fed President Thomas C. Melzer and Lawrence Lindsey, a member of the Federal Reserve Board of Governors, will be featured speakers at the conference. Other speakers include Robert D. McTeer Jr., Dallas Fed president; J. Alfred Broadus Jr., Richmond Fed president; and representatives from HUD and the Rural Development Agency.

This is the first time four Fed districts have joined together to offer a conference of this size.

The conference is designed for financial institution officers, government officials, and business, community and nonprofit organization leaders interested in rural community and economic development lending.

If you would like more information, contact Diana Judge at (314) 444-8751 or toll-free at 1-800-333-0810, ext. 8751.



# Interstate Branching: States Begin Their Work

**T**hough interstate banking and branching are now “done deals” at the federal level, they remain

very much live issues at the state level. Over the next year or two, state legislatures will be asked to make several important decisions regarding the branching provisions of the

Because the law prohibits states from discriminating against *out-of-state* banks and bank holding companies, states need to review and possibly amend many of their existing banking laws. States also have to decide whether to allow banks *within their borders* to participate in interstate mergers or protect them from such activity.

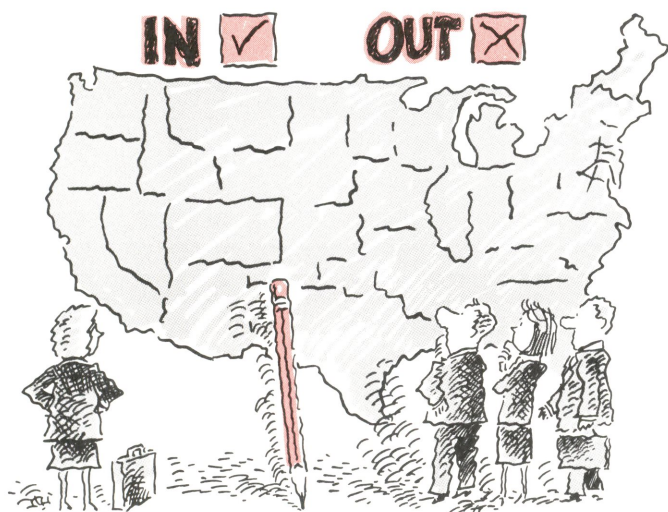
The big day for interstate branching is June 1, 1997. By this date, states must decide whether to:

- *Opt out*—enact laws that prohibit out-of-state banks from merging with in-state banks, which will also prevent in-state banks from making acquisitions out-of-state. If a state does not opt out, interstate mergers will be permitted after June 1, 1997.
- *Opt in early*—enact laws that permit mergers of in- and out-of-state banks before June 1, 1997.
- *Change concentration limits*—enact, repeal or amend limits on the proportion of deposits one banking organization may control in the state. A 30 percent limit will apply if states are silent.

If states already have a limit in place, that limit will apply.

- *Change age requirements*—enact, repeal or amend limits on how long a bank must exist before it can be acquired by another bank. No limit will apply if states are silent, and states cannot enact limits greater than five years.
- *Permit de novo branching*—enact laws that permit out-of-state banks to acquire a bank branch or establish a new branch in the state. Neither will be permitted if states are silent.

Despite the fanfare in Washington over the passage of this bill, it is these state decisions that will determine whether interstate branching is ushered in with a whimper or a roar.



new Reigle-Neal Interstate Banking and Branching Efficiency Act of 1994. Their decisions could have a tremendous effect on the branching activities of banks across the country.

## Tax Payment System

(continued from front page)

In April, two additional payment mechanisms will be offered. The first is a new “non-value” Fedwire message, which will replace the current typecode 1000 message.

The second option is a new software application for the Fed’s Fedline® or Computer Interface connections. This application, called the Electronic

Tax Application (ETA), will enable staff at the taxpayer’s financial institution to enter the tax information into pre-formatted screens.

By the year 2000, all financial institutions will send tax payments through a new system called the Electronic Federal Tax Processing System (EFTPS). EFTPS will increase the speed,

efficiency and accuracy of revenue collection and taxpayer account posting. It also will expedite the government’s funds availability, while providing critical investment decision-making information to the Treasury.

The Federal Reserve, acting as the fiscal agent for the government, will play a role in

the system by providing same-day reporting and payment mechanisms (e.g., Fedwire and ETA).

If you would like more detailed information about electronic tax payments, call Harriet Siering at (314) 444-8502.

# FedFacts

## 1995 Price Changes Announced

In November 1994, Fed St. Louis announced its 1995 prices for Eighth District check, electronic and securities services. While most prices remained the same, selected changes were made. Among the changes were increases in check return item fees and decreases in check deposit and wire transfer fees. The only ACH price change was an increase in paper government NOCs to \$10. If you have questions or would like additional copies of the price booklets, contact Customer Access Support at (314) 444-0869 or toll-free at 1-800-333-0869.

## Switch to Presentment MICR Under Way

Since November 1994, over 60 St. Louis Zone check customers have switched from Informational MICR to Presentment MICR, where the MICR transmission (rather than receipt of paper items)

constitutes legal presentment. Most of these customers said they made the switch to take advantage of a lower minimum daily fee of \$5. These customers will get an added bonus on Feb. 15, when all rejects will be included in their transmissions for free. If you'd like more information on either of these check services or would like to join the 315 institutions in the District that receive MICR transmissions, contact Customer Access Support at (314) 444-0869 or toll-free at 1-800-333-0869.

## Louisville Office Announces Check Price Changes

Effective Feb. 1, the Louisville Branch lowered the per-item fee for RCPC Regular deposits from 1.8 cents to 1.7 cents and increased fees for local items in mixed cash letters from 1.8 cents to 1.9 cents. These changes were made to encourage customers with sufficient volume to deposit their items

at the later RCPC deadline.

Also effective Feb. 1, the per-item fee for the truncation/CheckKeeper service was reduced from 1.3 cents to 1.1 cents.

## St. Louis Fed Seeks Efficiency With ACH

The St. Louis Fed is taking some of its own advice and converting its internal payments from check to ACH. The Fed initially targeted 450 of its vendors for the conversion, providing them with benefit information and educational materials on ACH.

The results of this initiative are noteworthy. To date, over 300 vendors have signed up to receive their payments via ACH. The St. Louis Fed is seeing tangible improvements as a result—its payments processing efficiency has improved, steps to complete payment transactions have been eliminated and payment reconciliation time has decreased.

# Calendar

## Upcoming Fed-sponsored Events for Eighth District Depository Institutions

### Renaissance in Rural America Conference

March 7-8 - Memphis, Tenn.

### 1995 District Dialogues

March 1 - Paducah, Ky.

March 22 - Quincy, Ill.

May 17 - Cape Girardeau, Mo.

October 2 - Evansville, Ind.

October 3 - Mt. Vernon, Ill.

### 1995 Economic Forums

April 25 - Greenville, Miss.

April 26 - Camden, Ark.

October 18 - Jackson, Tenn.

November 8 - Columbia, Mo.

For more information on the Rural America Conference call Diana Judge at (314) 444-8751 or toll-free at 1-800-333-0810 ext. 8751.

For more information on Economic Forums or District Dialogues, call Bernie Berns at (314) 444-8321 or toll-free at 1-800-333-0810 ext. 8321.



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