



Central Banker

FALL 2002

News and Views for Eighth District Bankers

St. Louis Fed's Web Site Gets a Makeover

In late summer, the Eighth District revamped its public web site. Our new address is much easier to remember, www.stlouisfed.org. We also have a brand new look and feel, and we've made substantial improvements—ones we hope bankers will come to appreciate.

All of our publications and economic data (FRED®) are still on the site. However, we have restructured many of our categories. Here's a brief summary of what you'll find:

- **New:** *Banking Information*—Includes several new topics, including regulations, applications and notices, bank data and much more.

- **New:** *News and Events*—Lists all news releases, speeches and Bank-sponsored conferences and events. Also includes a Press Room with Fed backgrounders, biographies and media FAQs.

- **New:** *Consumer Information*—Contains helpful links to various publications on credit, interest rates, savings bonds, personal finance and other topics.

- **Revised:** *Financial Services*—Provides four new online cash letter forms (under the Check Operations section). You'll also find a new and improved customer communications section.



- **New online tools:** Register online for most Bank-sponsored events.

When you have a moment, visit our new site. Then tell us what you think. You can access an online survey from our new home page. ■

ED to Replace Many Paper Mailings by October

In January, the St. Louis Fed launched an electronic distribution service to replace many of the paper mailings sent to depository institutions. This service, known as ED, provides Eighth District customers with a faster, easier and more efficient way to obtain and act on information from the Federal Reserve. And by Oct. 1, it will be the only way to receive many announcements and notices on changes to regulatory information and operating circulars from the Fed.

To subscribe to ED, simply go to www.stlouisfed.org and look for "E-Mail Alerts." There, you can sign up for the specific information you'd like to receive online. Some of the benefits of ED include: immediate notification, no limits on who can receive information, better-targeted mailings, the ability to change your subscription at any time, and no fees or charges.

To gauge customer satisfaction with ED, the Bank posted an online survey for subscribers in

July. The survey also measured the usability of the service and solicited suggestions for improvements. We're looking at the results now for ways to improve ED in the future.

If you have questions about ED or how to sign up, contact Tracie Mueller in St. Louis at (314) 444-8810 or 1-800-333-0810, ext. 44-8810. You can also reach her by e-mail at emailalert@stls.frb.org. ■



When Is a Check Not a Check?

By Hank Bourgaux, Senior Vice President at the Federal Reserve Bank of St. Louis

In a study released last November, the Federal Reserve showed that while the retail payment market continues to grow, the use of the check to pay for goods and services is shrinking. Many years into what some people call the “payments revolution,” the Fed and most financial institutions are starting to experience a drop in the number of physical checks we process. Where are they going? Our study documented that over the past 20 years, electronic payments had grown from about 15 percent of the retail payment market to about 40 percent. And the growth isn’t just from credit cards, debit cards, smart cards and the like. Today, we are seeing merchants—from mom-and-pop stores to the largest department stores—“electrifying” the check at the point-of-sale, lock-box collection services converting the check to an ACH item and more financial institutions providing only check images in bank statements. No wonder electronic check conversion can be confusing to some consumers.

Bankers can easily determine if the check is a check or if it has become an ACH item: If a check is collected and settled within the existing check processing system (even if it is done electronically), it is still a check. Even check images that replace paper

As the number of electronic payments continues to grow, it becomes the responsibility of the financial services industry to educate consumers.

checks are still considered checks. But it can get confusing for customers who hand over a check to merchants, who then use their check data to collect and settle through an electronic network. In this case, the check has been converted, and the electronic payment rules apply. Baffled consumers are given back a voided check and are left to wonder if any payment was actually made, and if so, what kind. Unfortunately, cash register clerks don’t always know how to respond to such confusion.

As the number of electronic payments continues to grow, it becomes the responsibility of the financial services industry to educate consumers about the differences between traditional paper checks and electronic payments, such as differences in processing times and legal rights.

To support financial institutions in their educational efforts, the Federal Reserve System offers several free resource materials about electronic check conversion and electronic payments, available online or in a format that can be downloaded. They are: <http://www.federalreserve.gov/pubs/checkconv/default.htm> and <http://www.chicagofed.org/publications/electronicmoney/>. I hope these help. ■

Electronic Access Support Consolidates at Minneapolis Fed

In July, the St. Louis Fed began efforts to consolidate customer support for electronic access services with the Federal Reserve Bank of Minneapolis. When the transition is complete, Eighth District customers will contact the help desk staff in Minneapolis with questions on FedLine®, Computer Interface, Frame Relay and other electronic access issues. We are implementing this consolidation gradually and plan to complete the transition in the fall.

Besides a change in contact and telephone numbers, the transition

to Minneapolis should be transparent to customers. The Minneapolis Fed has a solid background in electronic services customer support as well as an established customer service infrastructure. Customers can expect the same quality of service they were previously getting from customer support staff at the St. Louis Fed.

This latest effort follows closely on the heels of last year’s successful consolidation of our ACH, Book-Entry Securities and Wire Transfer services, and is part of an overall direction at the Fed.

“Consolidating the electronic access and customer support functions is a natural step in support of our District’s objective to make the Fed System more efficient,” said LeGrande Rives, first vice president of the St. Louis Fed. “This initiative further illustrates our long-term commitment to operational and cost efficiencies in electronic services.”

For updated EAS contact information please go to <http://www.stlouisfed.org/financial/> and look under the “features” section. ■

The Road to Check Modernization: Are We There Yet?

Several years ago, the Federal Reserve set out on its strategic journey as a payments provider when it decided to fundamentally redesign its infrastructure for providing both paper and electronic check services. A primary goal was for each Federal Reserve district to move to centralized systems and standard platforms while improving check services. The initiative—called Check Modernization—consists of four projects, each of which addresses a critical aspect of the check-clearing process. Here's a log of the St. Louis Fed's journey so far, as well as a vision of where we're headed next.

ENTERPRISE-WIDE ADJUSTMENTS Conversion complete!

October 2001—Following the St. Louis and Louisville offices' successful conversion in April 2000, the Memphis and Little Rock offices converted to the Enterprise-Wide Adjustment (EWA) system in October 2001. EWA, a standard software platform for streamlining adjustment research and resolution at the Fed, established a common platform for check adjustments with shared data across all Reserve banks.

The Fed can now benefit from automated workflow processes with minimal human intervention and is able to resolve adjustment requests without other Reserve bank assistance. For customers, this means quicker, more consistent service across the Fed System, greater accuracy and improved reference documentation.

FEDLINE FOR THE WEB—CHECK Now accepting customers.

February 2002—FedLine® for the Web—Check is the new web-based delivery channel for check services launched District-wide in February 2002. Compared with DOS-based FedLine, the web version offers a number of enhanced features and functions.

For one, FedLine services can now be accessed conveniently from most Internet-connected PCs, rather than a single designated FedLine terminal, making FedLine for the Web—Check an easy contingency option. Because it can be installed on PCs that communicate with a LAN, it also provides greater flexibility for downloading and uploading data (that is, MICR files) to back-end systems.

Web services also help the Fed develop and implement new or improved services faster, such as the FedImageSM Services, coming soon to the Eighth District (discussed later).

Another new web product, Large-Dollar Return Item Notification (LDRIN), will also be introduced this fall. The service will allow customers using the web service to send and receive notifications about large-dollar checks (over \$2,500) being returned to the bank of first deposit.

Another significant enhancement is the new check adjustments documents-to-follow (DTF) archive. This allows customers to electronically exchange

check adjustments supporting documentation with the Fed, dramatically improving the efficiency and timeliness of the adjustment process. This archive provides customers a 12-month history of adjustment activity—including advices, acknowledgement, check images and all other supporting documentation.

CHECK STANDARDIZATION Standardization complete!

July 2002—St. Louis became the final office in the Eighth District to convert to the standard check processing platform when it converted in July. The conversion follows those of Louisville in April, Little Rock in May and Memphis in June.

Known internally as the project with the largest scope and greatest impact on our operations, Check Standardization will bring standard hardware and software for check processing to all 45 Fed operating sites. Aside from testing with the Fed, participation in the cutover was minimal for customers. In fact, many won't notice much change in the new environment, except slight differences in the format of advices, cash letters and account statements.

Check Standardization will help the Fed roll out products more quickly, improve processing efficiency, eliminate redundant activities and reduce costs. Customers will benefit from more uniform and national services, as well as improved efficiency once all Fed districts convert to the new platform by the end of next year.

FEDIMAGE SERVICES Coming soon, to an office near you!

Upcoming—The Eighth District offices will soon also offer FedImage Services. When fully implemented across the Fed System, FedImage will establish a centrally managed platform and provide Reserve banks and customers alike the national archive to make images available within hours of capture. Customers will have web access to the archive and be able to retrieve images via FedLine for the Web.

You'll hear more about FedImage Services as your Fed office's conversion draws near.

Where We're Headed

Nearing the end of our multiyear journey into what the Fed has dubbed Check Modernization, the end of project planning and conversions is finally in sight. But the efforts to improve our services are not.

"Although the number of electronic payments is expected to grow and will displace paper checks over time, industry changes and technological advances continue to challenge us to retool our check processing environment," says LeGrande Rives, first vice president of the St. Louis Fed. "An ongoing goal at the Federal Reserve is to respond quickly to market needs and remain efficient and competitive."

FedLine® is a registered trademark of the Federal Reserve banks. FedImageSM Services is a service mark of the Federal Reserve banks.



Regional Roundup

Fed To Host Consumer Affairs Outreach Seminars

Invitations will soon be mailed for the Eighth District's annual Consumer Affairs Outreach seminars, to be held in October and November in St. Louis, Little Rock and Effingham, Ill. Sessions will run from 8:30 a.m. through 12:30 p.m., followed by a free luncheon.

Fed examiners will reveal tried-and-true practices for building strong compliance management programs and provide hands-on training to help assess the adequacy of current programs. Bankers will also learn risk-management techniques, which may improve the results of future compliance examinations. For information, contact Tim Stacy at (314) 444-8825 or Elizabeth Hayes at (314) 444-4251. They can also be reached at 1-800-333-0810, ext. 44-8825 or 44-4251, respectively. ■

National Customer Satisfaction Survey Wrapping Up

It has been three years since the Federal Reserve System conducted a customer satisfaction survey at the national level. That changed in mid-August, when Walker Information, the consulting firm retained by the Fed for the 1999 survey, initiated the second nationwide telephone survey of Fed customers.

Approximately 180 Eighth District institutions participated in the survey in 1999, providing insightful feedback about our products and services. In the wake of that survey, the St. Louis Fed re-emphasized its commitment to customer service by devoting staff to a District-wide improvement effort. In the current survey, we expect a similar audience, with representative samples from each of our District territories. The survey focuses not only on the

financial services provided by the Fed, but also customer relationships and customer service overall.

Results of the survey will be provided to each district later this year. We will share our results with you in publications and on our public web site. ■

2003 FOMC Meetings

The Federal Open Market Committee issued the following tentative meeting schedule for 2003:

- Jan. 28-29 (Tuesday-Wednesday)
- March 18 (Tuesday)
- May 6 (Tuesday)
- June 24-25 (Tuesday-Wednesday)
- Aug. 12 (Tuesday)
- Sept. 16 (Tuesday)
- Oct. 28 (Tuesday)
- Dec. 9 (Tuesday)

NexGen Notes Introduced As Next Phase of Redesigned Currency

The Federal Reserve and U.S. Treasury announced plans this summer to release the next generation of redesigned notes, with improved security features to deter counterfeiting. The new design, referred to as NexGen, affects the \$100, \$50 and \$20 notes. Circulation of the NexGen series could begin as early as fall 2003 with the introduction of the redesigned \$20 note. The \$100 and \$50 notes will follow in 12 to 18 months.

The NexGen designs will include the introduction of subtle background colors. While color is not in itself a security feature, the use of color provides the opportunity to add additional features that could assist in deterring counterfeiting. The introduction of additional colors will also help consumers to better identify the different denominations.

The new series will retain current security features, including watermarks similar to the portrait and visible when held up to a light, enhanced security threads that glow under ultraviolet light, microprinting, and color-shifting ink that changes color when the note is tilted.

To maintain the security of Federal Reserve notes, the Treasury aims to enhance the design of U.S. currency every seven to 10 years. The purpose is to stay ahead of advanced computer technologies used for some types of counterfeiting. According to the U.S. Secret Service, \$47.5 million in counterfeit money entered into circulation in fiscal year 2001.

The first initiative of the NexGen launch is already under way. The Bureau of Engraving and Printing is working with manufacturers of currency-accepting machinery to expedite the development of software and other devices, so vending machines and similar equipment accept NexGen notes. The cooperative effort allows a smooth transition for vending machine owners, mass transit agencies, the gaming industry and other proprietors that rely on currency-accepting machinery to conduct business transactions.

The redesign of the \$10 and \$5 notes is still under consideration, but a redesign of the \$2 and \$1 notes is not included in the plans for the NexGen series. ■



Cetus C. Coughlin is a vice president and economist at the Federal Reserve Bank of St. Louis. Additional discussion on this topic can be found in "Aviation Security and Terrorism: A Review of the Economic Issues," which Coughlin co-authored with **Jeffrey Cohen** and **Sarosh Khan**, and is scheduled for the September/October 2002 issue of the Bank's *Review*.

The Economics of Aviation Security

The terrorist attacks of Sept. 11 caused more than 3,000 deaths, property damage in the billions of dollars and a substantial decline in the public's confidence in the safety of air travel. Immediately, aviation security rose to paramount importance in the nation's policy agenda. Not surprisingly, conflicting views concerning how to improve aviation security were voiced. Which economic insights are relevant for understanding this vital issue?

Making the Skies Friendly

Prior to the events of Sept. 11, aviation security was provided by three main partners: airlines, airports and the Federal Aviation Administration (FAA). Generally speaking, air carriers and airports provided security, while the FAA performed a regulatory role. Indeed, studies prior to Sept. 11 had highlighted numerous aviation-security problems involving aviation computer security; access to aircraft, airfields and other facilities; as well as the detection of dangerous objects. With the passage of the Aviation and Transportation Security Act in late 2001, the role of the federal government in providing aviation security increased substantially.

A key feature of the airline industry is its transportation design. With its network structure, passengers from various remote nodes or spokes (different airports) often converge on a hub (a single airport), then depart for their final destinations. This hub-and-spoke system leads to interdepen-

dencies that give rise to what economists call an *externality*. An externality, also termed a spillover, exists when either the consumption or production activity of one consumer or firm affects directly either the well-being of other consumers or the production activities of other firms.

The events of Sept. 11 demonstrated vividly that aviation security—or lack thereof—in one location affected the movement of passengers and freight throughout the system. The existence of an externality provides an economic reason for governmental involvement in aviation security. Unregulated private markets are unlikely to provide sufficient aviation security because those making security decisions for one location may not account for the spillover benefits conferred upon others throughout the network. The role of government, however, might take various forms—regulating private providers, subsidizing private providers, or providing aviation security publicly. No one form of governmental involvement is necessarily superior to the other forms. Regardless of the form, too little or too much aviation security is possible.

A Boost in Resources

One result of the new legislation is a substantial increase in resources for aviation security. For example, the Congressional Budget Office estimates increased federal expenditures of roughly \$3.5 billion during both 2003 and 2004. These expenditures will fund large increases in the use of labor resources (passenger and baggage screeners, law enforcement officers in airports and airplanes, and administrators) and capital resources (passenger and baggage screening machines, access-control systems and reinforced cockpit doors). Because it is difficult to measure the effect of aviation security, the enhanced security produced by these additional resources is unclear. Thus, it is easy to foresee controversy about the benefits stemming from this increased commitment of resources. Nonetheless, during the legislative debates, any controversy about increasing resources was overshadowed by controversy surrounding the roles of airlines, airports and the federal government.

More Controversy

The federal government has assumed responsibility for the actual provision of aviation security. Especially contentious is the fact that federal employees will now be responsible for passenger and baggage screening. Proponents of this change argue that, as opposed to private provision, public provision reduces the incentives to increase profits by "cutting corners" on quality via cost reductions. On the other hand, a public agency might not provide security services efficiently because it can operate in a more-or-less monopolistic way. Furthermore, a public agency might provide excessive security and incur unnecessary expenses because it is likely to be judged on its security record and not on all the attributes encompassed by air transportation services for consumers. Unfortunately, economic theory alone does not provide a clear answer concerning the appropriate role of government. The bottom line is that policy-makers confronted tough decisions in terms of the amount of resources for, and the role of governmental involvement in, aviation security. Their choices will likely be scrutinized as the federal government assumes control of aviation security and as the war on terrorism continues. ■

Final Installment of Credit Scoring Series Out; Full Series Now Available

The fifth and final installment of the Fed's credit scoring series of articles, "Overrides and Second Review Process" is finished and in the mail. This installment completes the series Perspectives on Credit Scoring and Fair Mortgage Lending, developed by the Federal Reserve banks of Boston, Chicago, Cleveland, St. Louis and San Francisco, along with the Federal Reserve Board of Governors.

The articles gave the industry, concerned groups and individuals the opportunity to comment on issues surrounding the potential impact of credit scoring on mortgage applicants. In addition to an introduction and credit scoring overview, the series addresses credit scoring model development and maintenance, third-party broker issues, staff training, loan pricing, data accuracy, and the use of overrides and second reviews.

The complete series will soon be available online at www.stlouisfed.org. Simply go to

Community Development and look under "other publications." For a paper copy of the entire series, contact Linda Aubuchon at (314) 444-8646, or 1-800-333-0810, ext. 44-8646. You may also e-mail her at linda.a.aubuchon@stls.frb.org. ■

Two New Fed Governors Sworn In

Donald L. Kohn and Ben S. Bernanke took the oath of office Aug. 5 as members of the Board of Governors of the Federal Reserve System. The oath was administered by Fed Chairman Alan Greenspan.

Dr. Kohn was nominated to a vacant seat last held by Laurence H. Meyer, whose term expired Jan. 31, 2002. Dr. Kohn's term expires Jan. 31, 2016. Dr. Bernanke was nominated to the seat vacated by the resignation of Edward W. Kelley Jr. on Dec. 31, 2001. The term expires Jan. 31, 2004. ■

Mid-South Delta LISC Conference

SEPT. 18-20—TUNICA, MISS.
Conference will include a community development finance workshop presented by St. Louis Fed Community Affairs staff. For information, call David Jackson of Mid-South Delta LISC at (662) 335-3318.

Community Investment Forum on Affordable Housing

OCT. 1—JACKSON, TENN.
OCT. 2—COLUMBIA, TENN.
These half-day sessions are co-sponsored by the Federal Reserve banks of Atlanta and St. Louis. For information, call Ellen Eubank at (901) 579-2421.

Rays of Hope: A New Day for America's Distressed Urban Areas

OCT. 22-23—EAST ST. LOUIS, ILL.
Sponsored by the St. Louis Fed and the East St. Louis Action Research Project at the University of Illinois. For information, call Matt Ashby at (314) 444-8891.

A Shared Future—Part II: The Effects of City-County Mergers on Community Development

DEC. 10—LOUISVILLE
Sponsored by the Community Affairs department of the St. Louis Fed, the meeting will be held at the New Directions Housing Corp., 1000 E. Liberty St. For information, call Faith Weekly at (502) 568-9216.



P.O. Box 442
St. Louis, Mo. 63166

Editor: Alice C. Dames
(314) 444-8593
alice.c.dames@stls.frb.org

Central Banker is published quarterly by the Public Affairs Department of the Federal Reserve Bank of St. Louis. Views expressed are not necessarily official opinions of the Federal Reserve System or the Federal Reserve Bank of St. Louis.