



A Message from the First Vice President

Please, take us for granted.

It's fair to say that when you go to a movie theater, the dry cleaner, or a fast food restaurant, you assume the prices you pay will be about the same as they were, say, a month ago. When you go to your local bank to make a deposit, you assume your money is safe and the bank well managed. And when you return to your bank to cash a check or to withdraw money from your savings account, you assume the currency will be available.

You can take all of these things for granted because the Federal Reserve System—the nation's central bank—is doing its job.

The Federal Reserve's job comprises three important functions:

- *By conducting sound monetary policy, we keep inflation low and preserve the purchasing power of your money.*
- *By supervising and regulating banks, we make sure the bank you trust is operating in a safe and sound manner.*
- *By providing financial services to banking institutions and the U.S. government—such as clearing checks, providing cash, processing electronic payments, and providing Treasury services—we help the nation's payments system to work smoothly and efficiently.*

Each in its own way, these three functions contribute to the Federal Reserve's ultimate goal: to provide the nation with a safe, stable, and efficient monetary and financial system.

Maximizing the Efficiency of the Payments System

The Federal Reserve System has changed quite a bit since it was created by Congress in 1913. Some of the most visible changes have resulted from the Federal Reserve's ongoing efforts to keep the U.S. payments system safe, stable, and efficient.

For most of the Federal Reserve's history, maximizing efficiency has meant maintaining a large number of payments processing facilities throughout the United States. After World War II, the U.S. economy grew rapidly, and so did the public's demand for checks and cash. U.S. Treasury services—the sale and redemption of savings bonds and Treasury securities—were almost entirely paper based.

By 1980, the Federal Reserve System was operating 48 check processing facilities and providing cash and Treasury services at 35 of those locations. In the Fourth Federal Reserve District, three offices in Cleveland, Pittsburgh, and Cincinnati and a check processing facility in Columbus handled payments processing.

During the past two decades, technology, banking structure, and consumer preferences have reshaped the financial services industry. To keep pace, the Federal Reserve System has restructured its check, cash, and Treasury services to make them more efficient while assuring financial institutions equitable access, safety, and stability.

Banking Deregulation and Advances in Information Technology

Banking deregulation has allowed financial institutions to diversify their product offerings and to branch more freely within and across states, creating large national banking institutions. To serve these banks most effectively, the Federal Reserve System began to standardize its financial products and services, operating policies, data processing, and software application platforms.

These changes, together with advances in internet and electronic payments technology, have forced the Federal Reserve to rethink the way we deliver financial services—for instance, geographic proximity is no longer as important in the delivery of high-quality service to our customers. These shifts have transformed our relationships with the U.S. Treasury and with the nation's financial institutions—just as technology has changed our customers' relationships with their customers. The Federal Reserve has responded by adjusting our infrastructure, and the Federal Reserve Bank of Cleveland has been affected more than most districts.

Treasury Retail Securities

As the fiscal agent of the U.S. government, the Federal Reserve issues and redeems Treasury securities (bills, notes, and bonds) and U.S. savings bonds. These services were among the first to take advantage of the new economies of scale in the production and distribution of financial services. In the process, the number of savings bond processing sites was reduced from 22 to five during the early 1990s, and the sale of Treasury bills, notes, and bonds was centralized in three TreasuryDirect call centers. A second phase of consolidation occurred in 2004, with the remaining savings bond and TreasuryDirect operations consolidated into two Federal Reserve offices in Minneapolis and Pittsburgh.

The Federal Reserve Bank of Cleveland's Pittsburgh branch is responsible for the processing of Treasury retail securities. For instance, it prints and mails newly issued savings bonds, processes retired savings bonds, and staffs a TreasuryDirect call center. Employment at the Pittsburgh office increased throughout 2003 and 2004, and the office expects to add even more staff in 2005.

Check Operations

The Federal Reserve System's largest single operation is check clearing—that is, the means by which banks obtain payment for the checks they accept. Nationally, the Federal Reserve clears about 40 percent of the roughly 37 billion checks that consumers and business write each year. Though checks remain popular, a 2004 study found that electronic payments now exceed check payments. Declining check volumes, technological innovations such as check imaging and check-to-ACH conversion, and the recent Check 21 legislation have had a significant impact on the Federal Reserve's check clearing business.

As a result of these industry changes, the Federal Reserve System has begun to consolidate its check processing sites—from 45 in 2003 to 23 by mid-2006—and the Federal Reserve Bank of Cleveland is playing a key role in the effort. Our main office in Cleveland absorbed check operations from the Pittsburgh branch, boosting its average daily volume to 3.2 million checks. Over the next two years, the Cleveland office will take over the check operations of Federal Reserve offices in Detroit and Columbus. In addition, the Cleveland office now handles check adjustments for the entire Fourth District, as well as the Charleston, Louisville, and Indianapolis Federal Reserve offices, and maintains one of two large check image archives.

Consolidation of Federal Reserve Check Processing in the Fourth District



During 2004, the Bank's Cincinnati branch also took on work, absorbing check operations from Charleston, Indianapolis, and Louisville. Today, the Cincinnati office has nearly tripled its daily volume, processing more than 3.5 million checks each day and servicing about 800 financial institutions. These consolidation efforts have necessitated big changes in staff and job functions throughout the Federal Reserve; in the Fourth District, the volume of check business has increased significantly.

Cash Operations

The Federal Reserve System has a unique responsibility for the distribution, processing, and destruction of currency and the distribution of coin. Cash operations, of course, are paper based, and thus least conducive to consolidation. Nevertheless, the Federal Reserve has reduced its number of full-service cash operations from 35 to 31 sites. In the Fourth District, cash operations were relocated from the Pittsburgh branch to Cleveland in 1996, and from Louisville (a branch of the St. Louis Reserve Bank) to Cincinnati in 2004.

E-Government Operations

The Federal Reserve isn't the only organization working to make the payments system run better. The U.S. Treasury has also launched initiatives to make government operations more cost-effective and efficient through the use of electronic payments. As part of this effort, in 2000 the Federal Reserve Bank of Cleveland began work on a project, known as Paper Check Conversion, to help the Treasury convert checks written at government and military location into electronic debits, thereby speeding the collection of payments and improving financial control. Currently 99 agencies are using Paper Check Conversion, generating \$740 billion in transactions in 2004.

The Bank has also partnered with the Treasury on Pay.gov, an internet payment portal that allows businesses and consumers to make payments and submit forms to the government online, reducing the time and cost of completing paperwork manually. In 2004, Pay.gov processed \$4.1 billion in transactions for government agencies.

Ensuring the Efficiency of Payments in the Future

Throughout the Federal Reserve's history, external and internal forces have influenced the way the central bank formulates and implements monetary policy and supervises and regulates banking institutions. The largest and most visible changes have taken place in the way the Federal Reserve provides services to the U.S. government and to banking institutions.

Where once investors could visit a Federal Reserve office to purchase savings bonds or Treasury notes, today those transactions take place much more quickly by mail, by telephone, or online. In the future, the millions of checks that cross the country each day may be a thing of the past. We're confident those changes—like the changes that have already taken place—will occur seamlessly. We're also confident those changes will reflect and reaffirm the Federal Reserve's overarching goal: to maintain the safety, stability, and efficiency of our nation's payments system.