

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Date: December 12, 2001
To: Board of Governors
From: Edward W. Kelley, Jr.
Subject: 2002 Final Reserve Bank Budgets

The Committee on Federal Reserve Bank Affairs has reviewed staff's recommendation that the Board approve the Reserve Bank budgets for 2002. In aggregate, the 2002 Reserve Bank budgets total \$2,580.2 million, an increase of \$118.4 million or 4.8 percent over 2001 estimated expenses. This includes Reserve Bank operating budgets totaling \$2,567.8 million and a special project budget totaling \$12.4 million. The staff memorandum is attached.

Attachment

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

DIVISION OF RESERVE BANK OPERATIONS AND PAYMENT SYSTEMS

Date: December 12, 2001

To: Board of Governors

From: Elizabeth Perez, Stuart Sperry, Cathie Austin, Dorothy Lachapelle, Tillena Clark, and Paul Bettge

Subject: 2002 Final Reserve Bank Budgets

ACTION REQUESTED

Staff requests Board approval of the 2002 Reserve Bank budgets totaling \$2,580.2 million, an increase of \$118.4 million or 4.8 percent over 2001 estimated expenses.¹ This includes Reserve Bank operating budgets totaling \$2,567.8 million and a special project budget totaling \$12.4 million.²

Staff also requests Board approval of the 2002 Reserve Bank, Federal Reserve Information Technology (FRIT), and the Office of Employee Benefits (OEB) capital budgets totaling \$375.1 million. The capital budgets are approved with the understanding that approval for actual capital outlays will be in accordance with the Board's Policies and Guidelines Concerning Reserve Bank Operations (S-2602).

¹ These expenses include those budgeted by FRIT and the OEB. Expenses from these entities have been charged to the Reserve Banks, as appropriate, and included in their budgets.

² Unless otherwise noted, expenses also include costs associated with the check standardization special project. Special projects are major efforts having Systemwide significance that are outside the budgets of the individual Reserve Banks.

TOTAL EXPENSE AND EMPLOYMENT SUMMARY

The Reserve Banks' 2002 total budget of \$2,580.2 million is \$118.4 million or 4.8 percent above estimated 2001 expenses. Approximately half of Reserve Bank expenses in the 2002 budget are offset by priced service revenues (37 percent) and reimbursable claims for services provided to the U. S. Treasury and other government agencies (12 percent). Priced service revenues are budgeted to increase 0.3 percent as a result of projected

Table 1
Change in Net Expenses
(dollars in millions)

Expenses	2001 Budget	2001 Estimate	2002 Budget	Percent Change	
				01B-02B	01E-02B
Reserve Banks	2,442.2	2,461.8	2,580.2	5.7%	4.8%
Less:					
Priced service revenue	977.8	953.6	956.2	-2.2%	0.3%
Reimbursable claims	290.1	291.9	307.5	6.0%	5.3%
Net expense	\$1,174.3	\$1,216.3	\$1,316.5	12.1%	8.2%

price increases and modest volume growth in the check service. Declining revenue in other services moderates this increase. ACH revenue reductions reflect some erosion of commercial origination volume due to increased competition, as well as priced reductions. Declining revenue is also attributed to price reductions in the Fedwire funds transfers and book-entry securities services. Reimbursable claims will increase 5.3 percent, as the System continues to provide and expand Treasury-related services.

Individual Reserve Bank 2002 budget changes from 2001 estimated expenses vary from an increase of 0.3 percent to an increase of 8.7 percent, as depicted in Table 1 in Appendix A. The Reserve Bank budget increase of \$118.4 million provides funding for each District's salary administration and benefit program, nationally-provided support service (NPSS) initiatives, consolidated operations, and local Reserve Bank initiatives.

Total 2002 projected employment for the Reserve Banks, FRIT, and OEB is 23,550 average number of personnel (ANP), an increase of 282 ANP or 1.2 percent from 2001 estimated staff

**Table 2
Employment**

levels.³ Reserve Bank employment is expected to increase 228 ANP or 1.0 percent, largely due to plans to increase security staff. Tables 1 through 4 in Appendix A provide more detail on expense and ANP changes by District and service line.

	2001 Estimate	2002 Budget	Change	
			ANP	Percent
Reserve Banks	22,525	22,753	228	1.0%
FRIT	712	763	51	7.2%
OEB	31	34	3	9.7%
Total	23,268	23,550	282	1.2%

2001 BUDGET PERFORMANCE

The Reserve Banks estimate that 2001 expenses will be \$2,461.8 million, which represents an increase of \$19.6 million or 0.8 percent from the approved 2001 budget of \$2,442.2 million. Reserve Bank, FRIT, and OEB employment is estimated at 23,268 ANP, a decrease of 218 ANP from approved 2001 levels.

Eight Reserve Banks are experiencing cost overruns in 2001 ranging from 0.1 percent in Dallas to 6.8 percent in Kansas City. The remaining four Banks are below their approved 2001 budgets, ranging from 0.7 percent in Philadelphia to 4.5 percent in Atlanta. Tables 5 through 8 in Appendix A provide more detail on 2001 expense and ANP estimates by District and service line.

³ The term average number of personnel describes levels and changes in employment at the Reserve Banks. ANP is the average number of employees in terms of full-time positions for the period. For instance, a full-time employee who starts work on July 1 counts as 0.5 ANP for that calendar year; two, half-time employees who start on January 1 count as 1 ANP.

Higher-than-budgeted contract staff expenses add about \$9.5 million to the overrun. These fees include consultants involved in national project management and development support for the check standardization project (\$3.8 million), technical positions hired to support local IT initiatives, temporary staff in New York's check operation, and several major Systemwide initiatives, including Lotus Notes implementation and *PeopleSoft* conversion (\$5.7 million).

The 2001 estimate includes \$6.8 million in unbudgeted costs related to the recent terrorist acts.⁴ This cost is primarily due to a significant increase in overtime expenses largely for protection staff, alternative check shipping arrangements, and the costs associated with shipping currency to alternative storage locations. Offsetting a portion of these expenses are lower-than-planned travel expenses (\$1.0 million).

The 2001 estimate includes a net increase of \$4.7 million and 14 ANP associated with the System's revamped financial services product office structure. The Reserve Banks created the product office structure in the early 1990s to centralize leadership of the System's major financial services business lines. The structure is designed to draw on leadership from Reserve Bank offices that possess specialized expertise in a particular business area. As business requirements change and Reserve Banks develop new projects and initiatives, leadership of a product office may shift from one Reserve Bank to another, and responsibilities may be redefined. In 2001, the Reserve Banks redefined several areas of responsibility and shifted leadership among several Banks. Because final plans for these changes had not been approved when the

⁴ These costs have been isolated from the other sources of the 2001 overrun discussed in subsequent paragraphs.

Banks developed their 2001 budgets, the associated costs were unbudgeted. Most of the increase is the result of expanded product office responsibilities.

Higher costs associated with fully-reimbursable Treasury projects account for \$2.9 million of the 2001 overrun. This increase reflects higher communications costs for Treasury Direct consolidation, additional enhancements requested by the Treasury for continued development of the ASAP.gov application and the new Pay.gov and Government Point-of-sale Check Conversion (GPCC) projects. Appendix B provides a description of each of these projects, as well as other projects referenced later in this memorandum.

In addition, a variety of factors at a few Reserve Banks contribute to the overrun in 2001. The RPO in Atlanta experienced higher-than-budgeted costs associated with the Check Relay air transportation function (\$2.1 million) due to higher fuel costs. Several Banks experienced higher-than-planned medical costs (\$5.9 million) and one-time transition costs associated with the Systemwide consolidation of ACH operations (\$1.5 million). Chicago also increased its supervision staff by 17 ANP to enhance the quality of that function (\$1.2 million). Severance payments associated with restructuring, centralization, and efficiency initiatives in Richmond and Dallas also added to the overrun (\$4.2 million).

Partially offsetting these increases are lower costs related to the check imaging services system (ISS) project as a result of delays in its implementation schedule (\$3.6 million), an underrun in San Francisco due to revised year-end spending forecasts (\$3.0 million), and cost reduction programs in Atlanta (\$8.1 million and 157 ANP) and Richmond (\$1.1 million and 72 ANP). The Atlanta Reserve Bank's lower ANP

projection primarily is the result of not filling planned positions through restructuring, consolidation, and centralization efforts. The majority of Richmond's ANP reduction is the actual separation of staff.

THE 2002 BUDGET

2002 SALARY ADMINISTRATION

Reserve Bank, FRIT, and OEB budgets include \$108.9 million to fund salary administration programs for officers and employees.⁵ The budgets include average merit increases of 4.5 percent for officers and

4.3 percent for employees, totaling \$52.0

million, or 48 percent of the total salary

administration budget. Variable pay programs,

which include cash awards and incentive

payments for officers and employees, represent

\$33.2 million and are within the thresholds

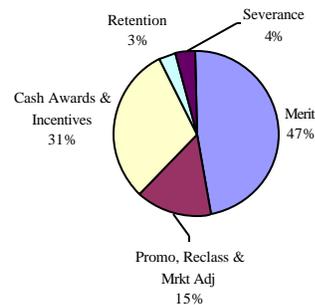
established by the Board.⁶ Promotions,

reclassifications, and market adjustments represent \$16.4 million, retention payments

represent \$4.1 million, and severance payments represent \$3.2 million. Merit and other

salary-related expenses are in line with public and private sector trends.

Figure 1
Salary Administration Components



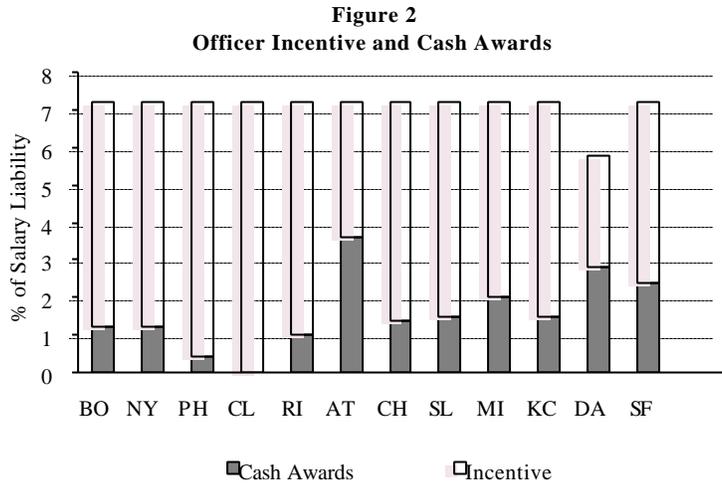
⁵ Salary administration, as shown in Table 9 of Appendix A, represents the budgeted funds that are available to increase compensation to officers and employees in the upcoming year. It does not include adjustments for changes in staffing levels, turnover and lag in hiring, and overtime.

⁶ Cash awards are payments for exceptional achievements during the year. Incentive payments represent awards for the accomplishment of pre-defined objectives related to specific projects and initiatives.

Officer incentive payments and cash awards total \$10.2 million or 7.0

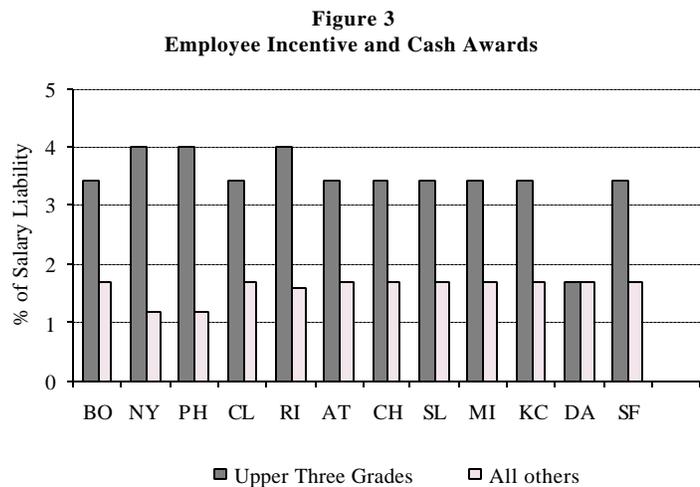
percent of officer salary liability.

As shown in Figure 2, officer variable pay continues to show increased funding for incentive-type awards, with one District using the entire variable pay pool for incentive awards. One Bank did not fund the officer incentive/cash award program to the maximum.



Employee incentive payments and cash award funds total \$22.8 million or 2.2 percent of employee salary liability (Figure 3). Consistent with the variable pay

guidelines, three Banks opted to apportion a higher percent of the award funds to the top three grades, with a commensurate reduction in other grade pools. One Bank did not fund the full amount of employee variable pay. The mix between incentive and cash awards



in the employee category continues to be heavily weighted toward cash awards.

Officer turnover in 2002, including retirements, is projected to decrease from an estimate of 5.9 percent in 2001 to 4.0 percent in 2002, ranging from no turnover

(Boston and Kansas City) to 12.3 percent (San Francisco). Employee turnover is projected to increase slightly from 10.9 percent in 2001 to 11.1 percent in 2002, ranging from 8.1 percent (Richmond) to 15.0 percent (Kansas City). Banks are reporting higher turnover in check operations and some professional and technical areas. To assist in retaining employees with critical skills, Reserve Banks plan to maximize variable pay, retention incentives, and other monetary and non-monetary rewards for key officers and employees.

Retirement and other benefit expenses, which account for 15 percent of Reserve Bank budgets, are anticipated to increase by \$31.0 million or 8.9 percent in 2002. Salary-related benefits, such as Social Security and Thrift Plan contributions, will increase 9.7 percent. The increase is primarily related to the combined effect of higher salaries and a change in 2002 to the employer matching component of the System's Thrift Plan (increasing the employer match from 80 percent to 100 percent for employees with at least five years of service). Other factors include higher postretirement and postemployment valuations, which are directly related to changes in actuarial assumptions. Non-salary-related benefits will increase 10.7 percent, primarily due to increases in employer contributions for health benefits (10.2 percent for non-HMO plans, 14.0 percent for HMOs, and 6.2 percent for dental plans). These increases are partially offset by projected savings from the new System prescription drug program.

INITIATIVES AFFECTING THE 2002 BUDGET

The 2002 budget provides funding for several initiatives associated with System and local Reserve Bank efforts. These initiatives and budgeted resources are described below and are organized by the operational area benefiting from the initiatives.

Initiatives Affecting Fee-Based Services to Financial Institutions

Check Modernization: In 1999, the Federal Reserve Banks, under the leadership of the RPO, initiated four major projects, collectively referred to as check modernization. The four projects – check standardization, enterprise wide adjustments, image services system, and electronic access and delivery – will standardize the check function's operating platform, enable new products to be introduced into the market more quickly, reduce the ongoing costs of operations, and facilitate the move to electronic payments. A brief description of the projects is included in Appendix B, page 35. The 2002 budget for the Reserve Banks includes a total of \$82.4 million in national costs for the check modernization projects and \$23.8 million in local Reserve Bank costs. The budgetary effect of each of the check modernization projects is described below.

Check Standardization: Reserve Banks and FRIT have identified NPSS costs associated with the project totaling \$39.7 million, local Reserve Bank implementation costs of \$22.5 million, and special project costs of \$12.4 million.⁷ Local implementation costs vary significantly by District and are determined by the timing of each office's conversion in the forty-five-month implementation schedule.

⁷ The check standardization special project includes only the portion of the check standardization project that relates to redundant operational costs and severance and retention payments for staff affected by each Bank's transition to the new check operating environment.

Enterprise Wide Adjustments (EWA) System: The 2002 budget includes \$7.7 million in NPSS costs for this project. An additional \$0.5 million has been included by the Banks for local costs associated with the project. San Francisco has responsibility for the development and Systemwide implementation of EWA. Twenty-five offices had converted to EWA by the end of 2000. Today, thirty-seven adjustment offices are relying on EWA for check adjustments processing and the remaining offices are scheduled to convert during 2002. In late 2002 and early 2003, the servers that support EWA are scheduled to migrate to FRIT.

Imaging Services System (ISS): The 2002 budget includes NPSS costs of \$15.5 million and local Reserve Bank costs of \$0.4 million for this project. Boston provides management for the ISS project, which will convert the Federal Reserve's currently diverse and decentralized commercial image archive systems to a standard, centrally-managed national image archive. As the project management site, Boston began staffing an ISS centralized business administration function (CBAF) in 2001 that will support ongoing operations after ISS implementation. Three Reserve Bank offices – Cleveland, Minneapolis, and Philadelphia – will serve as regional archive sites for the System. The Cleveland archive is scheduled to be ready for production by year-end 2001; almost a year later than originally planned due to software vendor delays.

Check Electronic Access and Delivery (CEAD): The 2002 budget includes NPSS costs of \$7.0 million and local Reserve Bank costs of \$0.4 million for the project. The Dallas Bank has been assigned responsibility for development of this application. The System began converting customers to CEAD under a controlled rollout in July 2001.

Wholesale Payments Consolidations: The 2002 budget includes net cost reductions of \$4.9 million in the funds transfer area and nearly \$1.4 million in the book-entry securities service related to the Wholesale Payment Product Office's (WPPO) continued consolidation efforts. This consolidation effort also is expected to result in a 16 ANP reduction in 2002. In 1999, off-line transfer services were consolidated to Boston and Kansas City. In the fourth quarter of 2001, the WPPO began consolidating the on-line support and related administrative functions for the funds transfer and book-entry securities transfer services to these two sites. In addition, computer interface customer testing is being consolidated in New York, where the majority of customers that use this service are located. These consolidations will reduce costs across the System by standardizing the provision of the service while improving service quality. Consolidations are scheduled for completion in the third quarter of 2002.

ACH Consolidation: Early in 2001, the RPO announced the consolidation of ACH operations resulting in 2002 budget savings of \$8.8 million and 37 ANP. The Atlanta and Minneapolis Banks, sites of the RPO and the ACH CBAF, respectively, were designated as the System's two processing sites. Atlanta is responsible for seven Districts, and Minneapolis will process work for five Districts.

Initiatives Affecting Services Provided to the Treasury And Government Agencies

Treasury Initiatives: Five Districts identified projects for the Treasury that in the aggregate are projected to increase by \$9.1 million and add 5 ANP. The Treasury reimburses Reserve Banks for project development costs. These projects include the Treasury Check Information System (TCIS), Pay.gov, GPCC, Intra-

government Payment and Collection System, Automated Standard Application for Payment (ASAP), and Treasury Web Application Infrastructure (TWAI).

Initiatives Affecting Central Bank Services⁸

Cash Initiatives: Three Districts identified cash initiatives, resulting in an increase in costs of \$5.7 million and 10 ANP. The increased costs are primarily the result of the full-year effect of opening the new Phoenix operations center in September 2001. To a lesser degree, the addition of processing shifts at the Atlanta and Dallas Banks and costs associated with volume increases in the Atlanta and San Francisco Districts are contributing to growth in this area.

Supervision and Regulation: Initiatives affecting the supervision and regulation function are projected to add \$5.1 million and 37 ANP in 2002. Additional resources are needed to address the growth in state member banks, increased responsibilities to supervise Large Complex Banking Organizations, and the full-year effect of 2001 staff increases. These initiatives are concentrated in the Richmond, Chicago, Kansas City, and San Francisco Districts.

Initiatives Affecting Cross-Functional Areas

Targeted Staff Reductions: Ten Districts identified savings totaling \$66.0 million and staff reductions of 392 ANP associated with ongoing or planned initiatives to improve productivity, streamline operations, and reduce discretionary expenditures. The

⁸ Central Bank Services is composed of Monetary & Economic Policy, Services to Financial Institutions and the Public, and Supervision and Regulation.

majority of the staff reductions are in Reserve Bank support and overhead areas, including information technology, financial management, administrative services, personnel services, and business development. Targeted reductions in discretionary expenditures include areas such as equipment, travel, training and education, and food service operations.

Security Enhancements: The budgets include \$50.3 million to enhance security at the Reserve Banks, an increase of \$11.4 million from estimated 2001 expenses. About half of the increase is associated with salary-related expenses for additional staff. Also included in this increase are expenses for security screening equipment and depreciation from various security-related building projects.

RISKS IN THE 2002 BUDGET

Reserve Banks have noted several common risks associated with the 2002 budgets. A number of Banks believe that cost reduction initiatives, necessary to meet System business owner guidance, may pose some risk to the budget. During the 2002 Reserve Bank Budget Outlook (RBBO) process, System business leaders, such as the product offices and oversight committees, provided spending targets for their respective areas. Because this was the first year this approach was used in the RBBO process, targets provided varying levels of detail. The need to tighten spending, however, is reflected in most Reserve Bank budgets, and many Districts outline efficiency initiatives to achieve spending targets. Many of the efficiency initiatives include staff reductions through attrition. If attrition is not sufficient to address the staff reductions, there is a risk that a limited amount of unbudgeted severance may be required.

The check modernization projects continue to present budget risks.

Delays associated with the ISS project have resulted in shifts in resources from 2001 to 2002. Similar pressures exist with the check standardization project. In addition to potential resource diversions, delays in project schedules could result in higher-than-projected staffing, equipment, and software costs. The expense associated with this risk varies by Bank and is dependent upon each Bank's position in the transition schedule. Following conversion, unforeseen problems, such as the inability to stabilize operations, could present additional risk.

There is also some risk in the supervision and regulation function. Most prevalent are concerns that additional resources could be needed if examination requirements exceed those already factored into the budgets. Tight labor markets have presented challenges for Reserve Banks to fill these positions. With the exception of highly-specialized positions, however, Banks recently have reported greater success in hiring examiners primarily due to softening labor markets. In addition, the supervision function is sharing more resources and specialized skills across Districts.

The Reserve Banks currently are in the process of conducting a post-September 11 assessment, with a focus on further improving the robustness and resiliency of critical Federal Reserve functions. Funding needed to implement recommendations that may arise from this assessment has not been included in the budgets. In addition, the Reserve Banks' 2002 budgets include early estimates of the expense and capital funding that will be required to enhance the overall physical security of the Banks. As Reserve Banks finalize these plans, additional resources may be required.

CAPITAL PLAN

The 2002 capital budget submitted by the Reserve Banks, FRIT, and OEB totals \$375.1 million. The budget includes \$338.3 million for the Banks, \$33.5 million for FRIT, and \$3.3 million for the OEB. Tables 10 and 11 in Appendix A provide detail of capital expenditures by District and asset classification.

As in previous years, the 2002 capital budgets include funding for projects that support the strategic direction outlined in the plans of the Reserve Banks, FRIT, and OEB. These strategic goals include improving operational efficiency and effectiveness, improving services to Bank customers, and providing a safe, quality work environment. In support of these strategies, the 2002 budget contains four major categories of capital outlays: building and facility improvements, including security enhancements; automation and communications-related initiatives; payment service improvements; and cash services initiatives.

The proposed capital budget includes an estimated \$220.7 million for **building-related projects and facility improvements**. These projects are geared toward renovation, modernization or replacement of physical facilities, and replacement or upgrading of critical systems. Building initiatives include several building projects in New York, including the continuation of the multi-year, floor-by-floor modernization of the Head Office building, and various other building and leasehold improvements. Budgets also include funding for the Houston Branch new building project in the Eleventh District, major floor renovations in Chicago, and remodeling of the San Francisco office lobby. In addition to the larger projects described, funding is also

provided for security enhancements, replacement of routine building-related equipment, and furniture and fixture replacements.

The proposed capital budget includes \$75.9 million in funding for major **automation and communications initiatives**. These initiatives do not include the automation components of building, payment systems, or cash services initiatives that are discussed separately. The strategic directions outlined in the individual Bank budgets include enhanced technological capabilities, the continued implementation of LAN technology, and the development of common office environments and web-based applications.

Of the total automation-related outlays, FRIT projects and acquisitions account for \$27.8 million. FRIT's 2002 capital plan includes outlays for FEDNET modernization, a CPU replacement project, and various software and hardware upgrades and enhancements. Aside from FRIT, major automation-related projects include \$10.3 million for server equipment primarily in New York and Atlanta, \$5.1 million for additional phases of the Transaction Processing System and the Foreign Processing System projects in New York, \$2.1 million for telecommunication equipment upgrades and internet gateway/directory services in Boston, and \$1.5 million for local area network upgrades in Philadelphia.

The automation total also includes \$11.9 million in capital for reimbursable Treasury initiatives, including the TWAI project, TCIS, and the Savings Bond Architecture Project (SnAP). The largest share of the remaining funds supports the Districts' distributed technology strategies.

The 2002 capital budget includes \$43.8 million for **initiatives related to payment system improvement**. These initiatives include \$5.7 million in FRIT's budget for hardware, software, and network components for the ISS and check standardization projects. The remaining funds support other national and local initiatives associated with the check modernization projects, the acquisition and installation of high-speed check imaging equipment and software, and check reader/sorter and endorser replacements. Many aspects of these initiatives are underway in a majority of the Districts.

Outlays of \$34.7 million have been included in the capital budget for **cash services initiatives**. In 2002, Bank budgets include \$27.1 million for the Board-approved cash project that includes installation of new sensors and scanners on all currency processing machines. In addition, San Francisco has included \$4.1 million for an inventory management system.

TO THE PRESIDENT OF EACH FEDERAL RESERVE BANK

Dear _____:

The Board of Governors has approved the Federal Reserve Bank of _____ 2002 expense budget of \$_____. The Board has also approved your District's 2002 capital budget of \$_____ with the understanding that approval of actual outlays for building and equipment purchases will be in accordance with the Board's Policies and Guidelines Concerning Reserve Bank Operations (S-2602).

The Board approved a 2002 budget for all Reserve Banks totaling \$2,580.2 million, a 4.8 percent increase over 2001 estimated expenses. The budget includes \$12.4 million for the check standardization special project.

The Board recognizes the difficult decisions that each Reserve Bank has made this year. The Board also recognizes that each Reserve Bank has been challenged to make trade-offs so that continued improvements in productivity can be achieved in 2002 and beyond.

As in the past, you are asked to keep the Board informed of any major changes anticipated in the spending plans for 2002 in accordance with S-2602. Please notify us as soon as possible should any major changes occur that affect your resource needs.

Very truly yours,

Jennifer J. Johnson

Secretary

TO THE DIRECTOR OF FEDERAL RESERVE INFORMATION TECHNOLOGY

Dear Mr. Summers:

The Board of Governors has approved the FRIT 2002 expense budget of \$195.1 million and special project budget totaling \$5.3 million. The Board has also approved your 2002 capital budget of \$33.5 million, with the understanding that approval of actual outlays for building and equipment purchases will be in accordance with the Board's Policies and Guidelines Concerning Reserve Bank Operations (S-2602).

The Board approved a 2002 budget for all Reserve Banks totaling \$2,580.2 million, a 4.8 percent increase over 2001 estimated expenses. The budget includes \$12.4 million for the check standardization special project.

As in the past, you are asked to keep the Board informed of any major changes anticipated in the spending plans for 2002 in accordance with S-2602. Please notify us as soon as possible should any major changes occur that affect your resource needs.

Very truly yours,

Jennifer J. Johnson

Secretary

TO THE EXECUTIVE DIRECTOR OF THE OFFICE OF EMPLOYEE BENEFITS

Dear Mr. Donovan:

The Board of Governors has approved the Office of Employee Benefits' 2002 expense budget of \$36.2 million. The Board has also approved your 2002 capital budget of \$3.3 million, with the understanding that approval of actual outlays for building and equipment purchases will be in accordance with the Board's Policies and Guidelines Concerning Reserve Bank Operations (S-2602). The Board approved a 2002 budget for all Reserve Banks totaling \$2,580.2 million, a 4.8 percent increase over 2001 estimated expenses.

As in the past, you are asked to keep the Board informed of any major changes anticipated in the spending plans for 2002 in accordance with S-2602. Please notify us as soon as possible should any major changes occur that affect your resource needs.

Very truly yours,

Jennifer J. Johnson
Secretary

APPENDIX A
Statistical Supplement

Table 1	Total Expenses of the FR Banks, by District
Table 2	Total Employment of the FR Banks, FRIT, and OEB by District
Table 3	Total Expenses of the FR Banks, by Service Line
Table 4	Total Employment of the FR Banks, by Service Line
Table 5	Total Expenses of the FR Banks, by District (Current Year Performance)
Table 6	Total Employment of the FR Banks, FRIT, and OEB by District (Current Year Performance)
Table 7	Total Expense of FR Banks, by Service Line (Current Year Performance)
Table 8	Total Employment of FR Banks, by Service Line (Current Year Performance)
Table 9	Salary Administration Expenses of the FR Banks, FRIT, and OEB Officers and Employees
Table 9	Capital Outlays of the FR Banks, FRIT, and OEB by District
Table 10	Capital Outlays of the FR Banks, FRIT, and OEB by Asset Classification

Note: In the following tables, components may not add to totals because of rounding. Table-to-table comparisons may also differ due to rounding.

2002 Final Budget

TOTAL EXPENSES OF THE FEDERAL RESERVE BANKS
by District, 2001 and 2002
(Dollars in Thousands)

District	2001 Estimate	2002 Budget	Change	
			Amount	Percent
Boston	145,356	155,701	10,345	7.1%
New York	490,179	508,994	18,816	3.8%
Philadelphia	120,743	125,751	5,008	4.1%
Cleveland	129,413	138,766	9,353	7.2%
Richmond	194,906	198,829	3,924	2.0%
Atlanta	284,111	298,857	14,746	5.2%
Chicago	236,690	244,842	8,152	3.4%
St. Louis	128,164	139,348	11,184	8.7%
Minneapolis	144,707	145,083	375	0.3%
Kansas City	160,993	170,040	9,047	5.6%
Dallas	144,777	151,614	6,837	4.7%
San Francisco	267,970	290,009	22,039	8.2%
Subtotal	2,448,008	2,567,835	119,827	4.9%
Special Project	13,803	12,387	-1,416	-10.3%
Total	2,461,811	2,580,221	118,411	4.8%

2002 Final Budget

**TOTAL EMPLOYMENT OF THE FEDERAL RESERVE BANKS,
FRIT, and OEB
by District, 2001 and 2002**

District	2001 Estimate	2002 Budget	Change	
			Amount	Percent
Boston	1,316	1,341	26	2.0%
New York	3,428	3,383	-45	-1.3%
Philadelphia	1,290	1,298	8	0.6%
Cleveland	1,344	1,402	58	4.3%
Richmond	2,139	2,173	34	1.6%
Atlanta	2,504	2,463	-42	-1.7%
Chicago	2,145	2,160	14	0.7%
St. Louis	1,305	1,355	50	3.8%
Minneapolis	1,296	1,306	9	0.7%
Kansas City	1,717	1,769	52	3.0%
Dallas	1,561	1,531	-30	-1.9%
San Francisco	2,479	2,572	93	3.7%
Subtotal	22,525	22,753	228	1.0%
FRIT	712	763	51	7.2%
OEB	31	34	3	9.7%
Total	23,268	23,550	282	1.2%

2002 Final Budget

TOTAL EXPENSES OF THE FEDERAL RESERVE BANKS
by Service Line¹
(Dollars in Thousands)

Service Line	2001 Estimate	2002 Budget	Change	
			Amount	Percent
Monetary and Economic Policy	234,043	242,938	8,895	3.8%
Services to U.S. Treasury and Gov't Agencies	265,617	284,116	18,500	7.0%
Services to Financial Institutions and the Public	578,826	626,782	47,957	8.3%
Supervision and Regulation	444,752	474,993	30,241	6.8%
Fee-Based Services to Financial Institutions	924,769	939,004	14,235	1.5%
Total	2,448,008	2,567,835	119,827	4.9%

¹ Service line expenses exclude special project costs.

2002 Final Budget

TOTAL EMPLOYMENT OF THE FEDERAL RESERVE BANKS
by Service Line¹
(Average Number of Personnel)

Service Line	2001 Estimate	2002 Budget	Change	
			Amount	Percent
Monetary and Economic Policy	886	850	-36	-4.1%
Services to U.S. Treasury and Gov't Agencies	1,387	1,334	-53	-3.8%
Services to Financial Institutions and the Public	2,818	2,916	98	3.5%
Supervision and Regulation	2,572	2,607	35	1.4%
Fee-Based Services to Financial Institutions	5,436	5,402	-34	-0.6%
Support and Overhead	9,426	9,644	218	2.3%
Total	22,525	22,753	228	1.0%

¹ Service line employment excludes FRIT, OEB, and special project Average Number of Personnel.

2002 Final Budget

TOTAL EXPENSES OF THE FEDERAL RESERVE BANKS
by District, 2001 Budget and 2001 Estimate
(Dollars in Thousands)

District	2001 Budget	2001 Estimate	Change	
			Amount	Percent
Boston	144,041	145,356	1,315	0.9%
New York	484,358	490,179	5,821	1.2%
Philadelphia	121,597	120,743	-855	-0.7%
Cleveland	131,778	129,413	-2,364	-1.8%
Richmond	188,288	194,906	6,617	3.5%
Atlanta	297,629	284,111	-13,518	-4.5%
Chicago	226,869	236,690	9,821	4.3%
St. Louis	123,780	128,164	4,384	3.5%
Minneapolis	138,828	144,707	5,879	4.2%
Kansas City	150,806	160,993	10,187	6.8%
Dallas	144,597	144,777	180	0.1%
San Francisco	273,246	267,970	-5,277	-1.9%
Subtotal	2,425,817	2,448,008	22,191	0.9%
Special Project	16,392	13,803	-2,589	-15.8%
Total	2,442,209	2,461,811	19,602	0.8%

2002 Final Budget

**TOTAL EMPLOYMENT OF THE FEDERAL RESERVE BANKS,
FRIT, and OEB
by District, 2001 Budget and 2001 Estimate**

District	2001 Budget	2001 Estimate	Change	
			Amount	Percent
Boston	1,285	1,316	31	2.4%
New York	3,431	3,428	-2	-0.1%
Philadelphia	1,287	1,290	3	0.3%
Cleveland	1,392	1,344	-47	-3.4%
Richmond	2,205	2,139	-66	-3.0%
Atlanta	2,666	2,504	-162	-6.1%
Chicago	2,111	2,145	34	1.6%
St. Louis	1,318	1,305	-13	-1.0%
Minneapolis	1,289	1,296	7	0.6%
Kansas City	1,678	1,717	39	2.3%
Dallas	1,600	1,561	-39	-2.5%
San Francisco	2,499	2,479	-20	-0.8%
Subtotal	22,760	22,525	-234	-1.0%
FRIT	698	712	15	2.1%
OEB	29	31	2	7.8%
Total	23,486	23,268	-218	-0.9%

2002 Final Budget

TOTAL EXPENSES OF THE FEDERAL RESERVE BANKS
by Service Line¹
(Dollars in Thousands)

Service Line	2001 Budget	2001 Estimate	Change	
			Amount	Percent
Monetary and Economic Policy	229,340	234,043	4,703	2.1%
Services to U.S. Treasury and Gov't Agencies	264,406	265,617	1,211	0.5%
Services to Financial Institutions and the Public	574,360	578,826	4,466	0.8%
Supervision and Regulation	445,165	444,752	-412	-0.1%
Fee-Based Services to Financial Institutions	912,547	924,769	12,223	1.3%
Total	2,425,817	2,448,008	22,191	0.9%

¹ Service line expenses exclude special project costs.

2002 Final Budget

TOTAL EMPLOYMENT OF THE FEDERAL RESERVE BANKS
by Service Line¹
(Average Number of Personnel)

Service Line	2001 Budget	2001 Estimate	Change	
			Amount	Percent
Monetary and Economic Policy	890	886	-4	-0.4%
Services to U.S. Treasury and Gov't Agencies	1,422	1,387	-35	-2.5%
Services to Financial Institutions and the Public	2,834	2,818	-16	-0.6%
Supervision and Regulation	2,575	2,572	-3	-0.1%
Fee-Based Services to Financial Institutions	5,396	5,436	39	0.7%
Support and Overhead	9,643	9,426	-216	-2.2%
Total	22,760	22,525	-234	-1.0%

¹ Service line employment excludes FRIT, OEB, and special project Average Number of Personnel.

2002 Final Budget

**SALARY ADMINISTRATION EXPENSES OF THE
FEDERAL RESERVE BANKS, FRIT, and OEB
Officers and Employees by District, 2002
(Dollars in Thousands)**

District	Merit	Promo & Reclass	Market Adjustment	Cash Awards	Incentive Payments	Retention Payments	Severance	Total	Percent ¹
Boston	3,086	525	63	460	1,365	-	-	5,499	7.0%
New York	10,244	1,687	950	4,688	2,303	398	1,499	21,769	8.5%
Philadelphia	2,349	407	281	1,057	650	66	125	4,935	7.2%
Cleveland	2,180	370	381	1,096	514	145	-	4,686	6.8%
Richmond	4,116	1,334	734	1,812	849	-	-	8,844	8.2%
Atlanta	5,302	1,914	267	2,132	940	229	203	10,987	8.9%
Chicago	4,822	1,650	600	1,586	1,669	200	403	10,930	8.7%
St. Louis	2,552	325	15	704	1,006	190	-	4,792	7.3%
Minneapolis	2,531	328	125	775	727	1,361	-	5,846	9.0%
Kansas City	3,612	1,394	797	1,080	970	277	74	8,205	8.9%
Dallas	2,815	355	70	1,102	352	81	60	4,834	6.4%
San Francisco	6,013	1,016	431	2,092	1,424	540	824	12,340	7.9%
Subtotal	49,621	11,304	4,713	18,583	12,769	3,488	3,188	103,666	8.1%
FRIT	2,239	420	-	526	1,154	625	-	4,963	8.2%
OEB	129	-	11	48	101	-	-	290	8.3%
Total	51,989	11,724	4,724	19,158	14,024	4,112	3,188	108,920	8.1%

Merit: the amount of budgeted salary expense that reflects the cumulative impact of planned salary increases based on performance.

Promo & Reclass: the amount of budgeted salary expense that reflects the cumulative impact of salary increases for individuals as a result of grade promotions and reclassifications resulting from a job evaluation.

Market Adjustment: the amount of budgeted salary expense to bring individual salaries to the minimum of a grade range or to better align salaries with the market.

Cash Awards: the amount of other personnel expense that represents payments for awards in recognition of exceptional achievements.

Incentive Payments: the amount of other personnel expense that represent payments for the achievement of pre-determined goals.

Retention Payments: the amount of other personnel expense that represent payments to employees based upon contractual agreements with the Bank. Generally used to retain staff in "hot market" jobs, or positions critical to the success of the Bank.

Severance: the amount of other personnel expense that represent payments to employees upon separation from the Bank.

¹ Percent represents the total of the stated payments as a percentage of total salary and other personnel expense.

2002 Final Budget

**CAPITAL OUTLAYS OF THE FEDERAL RESERVE BANKS,
FRIT, and OEB
by District, 2001 and 2002
(Dollars in Thousands)**

District	2001 Estimate	2002 Budget	Change	
			Amount	Percent
Boston	13,262	19,282	6,021	45.4%
New York	46,476	66,718	20,242	43.6%
Philadelphia	9,953	19,513	9,560	96.1%
Cleveland	22,746	22,781	35	0.2%
Richmond	23,935	27,284	3,349	14.0%
Atlanta	88,202	26,877	-61,325	-69.5%
Chicago	32,957	54,634	21,677	65.8%
St. Louis	20,635	19,312	-1,322	-6.4%
Minneapolis	7,237	7,374	137	1.9%
Kansas City	16,031	19,264	3,232	20.2%
Dallas	9,339	18,579	9,239	98.9%
San Francisco	19,810	36,673	16,863	85.1%
Subtotal	310,583	338,291	27,708	8.9%
FRIT	42,035	33,511	-8,524	-20.3%
OEB	1,475	3,300	1,825	123.7%
Total	354,093	375,102	21,009	5.9%

2002 Final Budget

**CAPITAL OUTLAYS OF THE FEDERAL RESERVE BANKS,
FRIT, and OEB**

by Asset Classification, 2001 Estimate and 2002 Budget¹

(Dollars in Thousands)

Asset Classification	2001 Estimate	2002 Budget	Change	
			Amount	Percent
Equipment	127,316	137,083	9,767	7.7%
Furniture & Fixtures	27,914	17,496	-10,418	-37.3%
Land & Other Real Estate	1,772	15,403	13,631	769.4%
Buildings	127,062	122,899	-4,163	-3.3%
Building Machinery & Equipment	19,564	35,984	16,420	83.9%
Leashold Improvements	6,761	5,402	-1,359	-20.1%
Software	43,704	40,835	-2,870	-6.6%
Total	354,093	375,102	21,009	5.9%

APPENDIX B

Glossary of Projects

Treasury Projects

Automated Standard Application for Payment (ASAP) and ASAP.gov – As the host Bank for the ASAP CBAF and development teams, the Federal Reserve Bank of Richmond is closely involved in supporting the Treasury's strategic goal to consolidate Federal proprietary grant payment systems through the use of the ASAP system. To meet this goal, the Treasury requires that the ASAP system be re-engineered and that an internet connection be offered to meet the needs of new agencies and recipient organizations that will be migrating to ASAP during 2000 to 2002. Additionally, to meet the increased need for timely and effective training, the Treasury requested a web-based training application be offered in conjunction with the ASAP.gov, Release I (Authorizations). ASAP.gov, Release I was implemented in September 2001 in the trusted zone of the existing FRB infrastructure using FRB certificates. The Automated Enrollment software was implemented mid-2001. Implementation of the remaining releases of ASAP.gov, II through VI, is projected to occur by year-end 2002.

Government Point-of-Sale Check Conversion (GPCC) – FRB Cleveland also has been asked by the Financial Management Service (FMS) to provide the Government Point-of-Sale Check Conversion service. This project supports the electronic conversion of a check received at the point-of-sale at government locations. Checks received at these locations will be imaged and immediately handed back to the customer. The transaction will be authorized on-line and the payment will be processed electronically. Beginning in September 2001, the operation was implemented in four U.S. Army bases in Germany. It will be expanded to other Army bases in Europe and then to other government locations worldwide.

Intra-government Payment and Collection System (IPAC) – FRB Richmond is working as the host site with FMS to enhance and re-deploy the current Online Payments and Collections (OPAC) application family. Renamed Intra-governmental Payments and Collection (IPAC), the new system will be implemented as a web-based, three-tier client server application written in Java. IPAC was successfully implemented in late 2001. Multiple releases are planned for 2002.

Pay.gov – FRB Cleveland has been asked by FMS to provide the Pay.gov ACH payment service. Pay.gov will provide organizations and individuals with the ability to make payments to the government for services and fees by logging onto the Pay.gov web site to initiate an ACH transaction. The Treasury has indicated that the potential volume of collections made by Pay.gov could reach 80 million payments annually with a total value of \$125 billion.

Savings Bond Architecture (SnAP) – This project will convert the current mainframe-based savings bond processing software to a client-server-based platform

Treasury Check Information System (TCIS) – In support of the Treasury's strategic goal to provide timely and accurate Federal payments, the Treasury's FMS has requested FRB Philadelphia to develop, deploy, and maintain an application to replace its existing Check Payments and Reconciliation System currently housed at its Hyattsville headquarters. The replacement system will be a commercially-available reconciliation and claims package customized to meet FMS business requirements. The new application will manage the Federal government's checkbook and related inquiries, claims, and adjustments. Philadelphia will perform all necessary activities including developing interfaces, user training, and data conversion to meet the fourth quarter 2002 target date to begin the implementation effort for this application. Philadelphia also will provide long-term technical support and operations management of the system, including provision for appropriate contingency backup and recovery.

Treasury Web Applications Infrastructure (TWAI) – FRIT is leading this project to build a network to support Treasury applications, connecting Treasury's customers and other business partners by using web and internet-based technologies.

Check Modernization Projects

Check Electronic Access and Delivery (CEAD) – CEAD eliminates the check service's dependency upon the DOS FedLine platform by migrating current and future products to FedLine for the Web.

Check Standardization – Check standardization will standardize Reserve Bank check processing on a single platform and software suite. Data processing support for this platform will be provided by FRIT. Support for application software will be centralized.

Enterprise Wide Adjustments (EWA) System – EWA is intended to provide a common, standard platform for check adjustments processing throughout the System. With the entire System on a single processing platform, the Reserve Banks will gain case resolution efficiencies. Additionally, the Reserve Banks will be able to resolve cases remotely, making remote assistance more practical when one office begins to have backlog difficulties. In the long term, EWA will improve internal efficiency and eliminate duplicate support requirements. In 2002, the Reserve Banks will enhance EWA functionality, complete migration, and begin to transition support responsibility to FRIT.

Imaging Services System (ISS) – This project will convert the Federal Reserve's currently diverse and unconnected commercial image processing platforms to a standard, centrally-managed national image archive.