



# F I N A N C I A L

## S e r v i c e s

### Teaming up with the banking industry to enhance the retail payments system

**F**or years now, the checkless society has seemed just around the corner. Today, we have a growing variety of electronic tools to pay our bills, quickly and efficiently, without having to write a single check – yet about three-fourths of all non-cash U.S. transactions are still made by check.

This reality presents a special challenge to the Federal Reserve. The paper-based system of check collection relies on a mature technology that is unlikely to see significant gains in efficiency. One of our vital goals has always been to enhance payments efficiency – both in our own operations and those of our banking customers and society.

#### The Rivlin Report

In January, the Federal Reserve's Rivlin Report concluded that we should enhance the efficiency, effectiveness, and convenience of check collection and automated clearing-house (ACH) services. The report recommended that Federal Reserve Banks work closely with private industry to help evolve strategies for electrifying the payments system.

With an electronic infrastructure well in place in 1998, the Kansas City Fed was well positioned

to bring the Rivlin Report's recommendations to life. At the beginning of the year, more financial institutions were receiving electronic check presentations in the Tenth District than in any other Federal Reserve district.

#### Check imaging for banking customers

One way to increase the efficiency of clearing

paper checks is truncation, a process that substitutes electronic information for the paper check during the collection process.

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Some banks have been reluctant to adopt truncation, however, because customers want quick and easy access to physical copies of their checks.

The Kansas City Bank was the first in the nation to offer banks access to digital images of checks over the Internet during the truncation process. Check imaging enables banks to take advantage of truncation and still offer their customers copies of checks, electronically or on paper.

#### Removing barriers to ACH use

ACH allows institutions, firms, and consumers to make a variety of direct deposits and payments, with no need to transport, process, and store billions

## *The Automated Payments Partnership helped heighten public awareness of the advantages of ACH.*

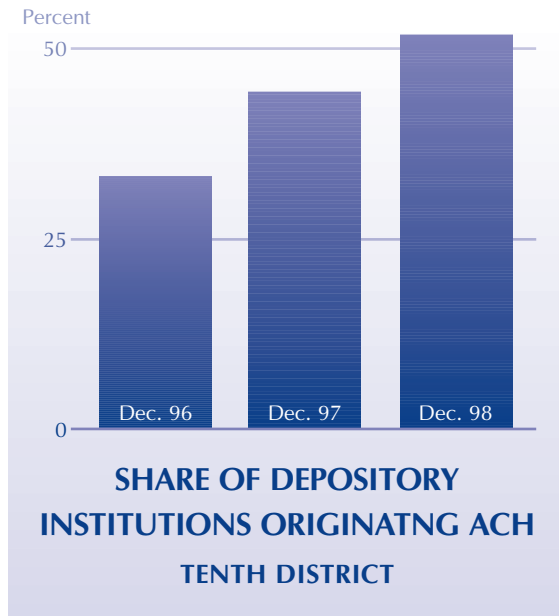
of pieces of paper. Despite its advantages, ACH accounts for only about 5 percent of all noncash U.S. transactions.

With such enormous potential, why hasn't ACH caught on, especially in business-to-business transactions? One answer is that many banks simply lack the software to translate a transaction's accompanying invoice information into plain English for their corporate customers.

A Federal Reserve project team, headed by Tenth District staff, worked closely with industry experts and ACH users in 1998 to help solve this problem. Together, we developed a software package, FedEDI, which can translate this information. We began distributing FedEDI nationally and held training programs for users. ACH is now an attractive payments option for a much broader spectrum of banking customers.

### **Collaborating with private industry**

A key to creating a more effective payments system is forging partnerships. The private sector has always provided technical innovation. As their partner, we have helped establish the basic



conditions needed for fostering innovation.

In addition to FedEDI, another joint effort with private industry in 1998 was making sure our payments system would operate smoothly

through the century date change. A majority of our on-line customers have already worked with us to test their use of our electronic payments services.

We also worked with other Federal Reserve Banks and private industry to heighten public awareness of ACH, a vital task given the federal government's EFT99 initiative to electronify most government payments in 1999. As the Automated Payments Partnership gathered steam, over 1,300 financial institutions and corporate partners helped us inform potential customers about the benefits of ACH. By yearend, 52 percent of our district's depository institutions were originating ACH payments.

By forging active partnerships with private industry, we can help foster a competitive, productive environment for the birth of new products and ideas. In doing so, we can help satisfy two of our primary goals – a wider range of payments choices for consumers and businesses, and enhanced efficiency in all facets of the retail payments system. ■

# Profiles

## ALICE DITTMAN

Alice Dittman's banking career spans almost five decades, starting in the early 1950s with a check-filing job for 50 cents an hour. Since then, she and her late husband, Mark, have started two new banks, brought the total assets of the Cornhusker Bank in Lincoln, Nebraska, from \$10.5 to \$170 million, and received nearly every honor and award possible.

A member of the Kansas City Fed's Financial Services Customer Advisory Council, Alice is a strong proponent of technology. "We were the first Nebraska bank to go fully to an imaging format for our check operation," she says. She values the Federal Reserve's efforts to improve the efficiency



Nearly 400 Midwest banks receive Fed Services through correspondent relationships with MIB.



Cornhusker Bank's chairman is an advocate of technology in her drive for banking efficiency.

of the payments system.

"The Federal Reserve continually strives to shorten presentment times, working hard to help all banks become more efficient in delivering services. Day to day, we as bankers rely on the Fed to clear the largest percentage of our checks in the most efficient manner possible. It's a great team. I'm excited about the Fed's entrance into imaging and look forward to the day we can receive our cash letter in this efficient format." ■

## CAM FINE

Like bankers and business people around the world, Cam Fine, president and CEO of Midwest Independent Bank, is making sure his systems are year 2000 compliant.

## *Bankers give valued advice regarding Financial Services issues.*

“It’s the largest single issue there is,” Cam says from his Jefferson City, Missouri office. “People are delaying other projects to make sure they’re ready. We are testing our internal systems and the systems that interact with our correspondents through FedLine.”

Taking care of their correspondent banks is the order of business for MIB, a banker’s bank owned and directed by independent community banks. MIB provides these kinds of banks a wide range of technical and traditional correspondent banking services.

As one of the Kansas City Fed’s largest customers and a member of the Customer Advisory Council, Cam meets frequently with the Bank’s operations staff. This relationship has resulted in a number of innovative strategies for meeting the service needs of banks throughout the district. ■

## BRUCE MORGAN

**A**t Valley State Bank in Atchison, Kansas, community spirit is a given, and president and CEO Bruce Morgan wouldn’t have it any other way. He believes it’s important to keep the Federal Reserve user-friendly for the small community bank. “The Fed is an important correspondent banking partner,” he says. His bank maintains a Fed account and subscribes to nearly all the Kansas City

Fed’s operations-related services.

Bruce has worked closely with the Kansas City Fed on several initiatives, serving on the Customer Advisory Council and in focus groups on electronic check presentment. He has served as a speaker and trainer at Federal Reserve Banks in Chicago and Atlanta, training senior-level bank examiners on the future of community banking.

Through his partnership with the Fed, Bruce hopes to ensure the viability of community banks. “The banking system reminds me of roads



**Programs that focus on the future of community banking are important to Valley State Bank.**

on a map,” he says. “Despite all the merger mania, there will always be red highway banks and blue highway banks. I’m a blue highway banker.” ■