

Consumers Union

Publisher of Consumer Reports

West Coast Regional Office
1535 Mission St.
San Francisco, CA 94103
415-431-6747

March 5, 2004

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

By overnight delivery

Docket # R-1176, Check 21

These comments are filed by Consumers Union, the nonprofit publisher of *Consumer Reports*,¹ the Consumer Federation of America, U.S. PIRG, the National Consumer Law Center, and Consumer Action.

Check 21 treats an electronic transfer of **funds** initiated by check under check law, but at the same time provides **some** new consumer rights to accompany this fundamental change in how checks are processed. These consumer groups seek changes in the proposed rule and commentary to make the new consumer rights accessible. Although Check 21 fails to assure consumers a minimum package of rights that **apply** to *any* check that has been processed electronically, Check **21** does **take** an important first step **toward** consistency for consumers in payments **law** by including a consumer right of recredit with respect to **substitute** checks which is similar to the consumer's right of recredit under the Electronic Funds Transfer Act.

Check **21** **provides** consumers three important **new** rights. First, consumers whose checks are processed using a substitute **check** receive a special substitute check warranty. Second, consumers **who** receive a substitute check are indemnified from **harm** caused by not receiving the original **check**. Third, consumers receive **a** right to claim **an** expedited recredit for erroneous payment of a substitute check or for a **warranty** claim on a substitute check.

¹ Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide consumers with information, education and counsel about goods, services, **health**, and **personal finance**; and to initiate and cooperate with individual and **group** efforts to maintain and enhance the quality of **life** of consumers. Consumers Union's income is solely derived from the sale of Consumer Reports, its other publications and from noncommercial contributions, grants and fees. In **addition** to reports on Consumers Union's **own** product testing, Consumer Reports with approximately 4 million paid circulation, regularly carries articles on **health**, product safety, marketplace economics and legislative, judicial and regulatory actions which **affect** consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support. The other organizations signing **this** letter are described in Attachment 2.

We seek changes in the proposed rule and draft commentary to make these rights work for consumers. Check 21 is ambiguous about whether the right of recredit applies whenever a substitute check has been used, or only when the substitute check has also been provided to the consumer. The proposed rule narrows the Scope of the recredit right by imposing an obligation that the substitute check be provided to the consumer before the right of recredit is triggered, and also by interpreting “was provided” to mean provided only an paper and not provided in electronic form. These two policy choices in the proposed rule should be reversed, so that the right of recredit will do the job contemplated by Congress of protecting consumers. Similarly, to the degree that the statute is read to require that the consumer be provided a substitute check in order to exercise the right of recredit, it is crucial that the regulation expressly recognize a consumer right to receive a substitute check on request. If a bank can simply deny the consumer’s request for a substitute check, it could avoid all application of the key consumer right of recredit. In addition, the proposed rule omits a key statutory requirement for bank denial of a recredit to a consumer—that the bank demonstrate that the substitute check was properly charged to the consumer’s account.

Consumers Union, the Consumer Federation of America, U.S. PIRG, the National Consumer Law Center, and Consumer Action seek these key changes in the text of the proposed rule:

- The rule should be changed to delete the requirement that the substitute check “was provided” to the consumer in order to trigger the right of recredit. This would resolve a statutory ambiguity in favor of more consumer protection through wider access to the right of recredit.
- The rule should be changed to treat the provision of an image of a substitute check, and the right to request a substitute check, as satisfying any precondition on the right of recredit that a substitute check “was provided” to the consumer.
- The rule must expressly require a bank to provide a substitute check to a consumer who requests a substitute check, an original check, or a copy of an original check. This is needed to prevent circumvention or evasion of Check 21.
- The rule should be changed to incorporate a key statutory precondition on a bank’s denial of a recredit—that the bank has “demonstrated to the consumer that the substitute check was properly charged to the consumer account.”
- The rule should direct banks to reverse NSF fees and other adverse consequences to the consumer after an error in processing a substitute check.
- The rule should disallow or place a strict time limit on reversal of a recredit after the bank has notified the consumer it has determined the claim to be valid.
- The substitute check notice should be sent to all consumers.
- The model consumer notice should be made more accurate, and the notice should be augmented to inform the consumer of shorter float and to answer this consumer question: “Where is my original check?”

- The Board should provide the model notices in both English and Spanish.
- The rule must require banks to accurately respond to consumer inquiries about how a particular check was processed and what rights and obligations attach to that check.
- The rule should prohibit non-bank creation of substitute checks.

Importance of these rules

The Check 21 rules are important because the non-return of an original paper check may be caused by one of several different ways in which the payment was processed, each with different consequences for the check writing consumer. Three identical checks written by one consumer can be processed differently, leading to three very different sets of rights and protections. These widely varying sets of consumer rights are: 1) Regulation E protection (electronic check conversion); 2) dollar-capped Regulation E-style Check 21 recredit protection (substitute checks); or 3) no recredit right (voluntary truncation by bank agreement).

These three very different sets of legal rights and remedies apply when the circumstances appear largely identical to the consumer, who simply wrote a check and did not receive the original check back.² This is already causing, and will continue to cause, significant consumer confusion. The Federal Reserve Board should reduce the opportunities for that confusion by interpreting the Check 21 right of recredit broadly, thus bringing at least the substitute check rule into closer alignment with the treatment of electronically converted checks covered by Regulation E.

The right of recredit is of high practical importance to consumers. Under traditional check law, a consumer's only remedies if a check is improperly paid are to persuade the bank to return the funds or sue the bank to enforce state law Uniform Commercial Code provisions. The Electronic Funds Transfer Act and Regulation E created a new, efficient, non-litigation remedy for consumers. That remedy is the right of recredit. With recredit, the consumer can get disputed funds put back into the account promptly. Recredit allows the consumer to avoid the harmful consequences of a dispute in the amount of a payment from the consumer's account, by getting the funds restored before a rent check bounces, a car insurance policy is cancelled due to an NSF check, or a late charge is incurred on a bill that would have been paid on time if not for the disputed funds being missing from the consumer's account. Recredit is easy and simple to invoke. A consumer can use recredit without a lawyer. Recredit avoids the expense and delay of litigation for all parties to the dispute. Congress chose to give consumers whose check processing is changed by Check 21 a right of recredit which strongly parallels the EFTA right. The changes we seek in the proposed rule and draft commentary are essential to making that right of recredit truly available to consumers.

The undersigned national consumer groups ask the Federal Reserve Board to use this rulemaking to bring the application and implementation of Check 21 closer to what Congress intended—that Check 21 would protect consumers while introducing more efficiency into the banking system. Because the right of recredit is crucial to protecting consumers, we ask the Federal Reserve

² While electronic check conversion of periodic payments requires consumer authorization, major billers are beginning to condition acceptance of checks on this authorization, placing a notice in the fine print that submission of a check constitutes authorization for electronic check conversion. Consumers Union is receiving calls from consumers who had no awareness that they had "consented" to electronic check conversion.

Board to **make** the right of recredit available to all consumers whose payments are processed using substitute checks or who have a substitute check returned to them. This interpretation of the scope of the right of recredit **will** reduce the practical differences between the rights available to consumers whose checks are processed in whole or in part **as** substitute checks as compared to consumers whose checks are subject to electronic check conversion.

Three **key** changes in the rule are needed to provide sufficient access to the right of recredit. First, the Board should resolve the ambiguity in the statute about whether or not a substitute check must have been provided to the consumer to trigger the right of recredit. ~~The~~ Board should resolve that ambiguity in favor of broader access to recredit. Second, if the rule does impose a requirement that the substitute check “was provided” to the consumer, then the Board should change the rule to allow the provision of an image of a substitute check provided pursuant to **an** agreement to satisfy any such “**was** provided” precondition on the right of recredit. Third, the rule must expressly require that a bank give the consumer a substitute check upon request for a substitute check, **an** original check, or a copy of the original check. **As** presently drafted, the rule makes the right of recredit wholly illusory because it ties that right to whether the consumer was provided a paper substitute check, but does not require that a bank ever provide that piece of paper, even on request of the consumer.

A fourth key change **we** seek is for the regulation to impose on banks a requirement already imposed by the statute: that **an** otherwise proper application for recredit cannot be denied unless the **bank** demonstrates to the consumer that the substitute check **was** properly charged to the consumer’s account.

Our comments are organized as follows:

- Recredit issues
- Warranty issues
- Consumer notice issues
- Other substitute check issues
- Specific requests by the Board for comment
- Specific suggested changes to model notices.. Attachment One
- Description of groups joining comments. Attachment: Two

Recredit issues

The legislative history shows that Congress intended expedited recredit to be available to consumers when a substitute check was erroneously charged to the consumer’s account.

The extensive statements in the legislative history that Check 21 was intended to protect consumers require that ambiguities in the statutory language be construed in favor of greater, not lesser, consumer protection. The legislative history indicates that Check 21 was intended to increase consumer protection. Congress Member Bachus, referring to an amendment offered by Congress Member Watt, stated: “Part of that language clarifies that nothing in this act shall diminish in any **way** and everything in this act shall preserve all consumer protections. In fact, we have added consumer protections in this act.” 149 Cong. Rec. H 4987, June 5, 2003.

The right of recredit, in particular, **was** intended by Congress to enhance consumer rights, allowing consumers to get their money back without navigating the intricacies of the UCC. Thus, Congress Member Davis (**AL**) stated to the House in the Committee of the whole:

I want to dwell for a minute on an act of simplification that this bill creates with respect to consumers. Right now, a good many of the people who are watching this or **who are** part of our districts have had the experience of looking at their bank ledgers and finding out that they have been credited [sic] for something that they did not think they wrote. **A** lot of people regularly run into these kinds of very small issues with the banking community, and those of us who went to law school can recall the portions of our bar books that summarize the UCC and the various protections, and they have been something of an imponderable maze.

This bill **improves** that. The **expedited** recredit provision has a number of very simple but *very important* features.

The first one is that if it is determined that a bank has falsely credited [sic] someone's account, within 1 day of that determination the bank must recredit the account. And there is a very specific **window** of time that is set to resolve a dispute. If a bank has not determined that a claim is valid within 10 business days, the bank has two options: either recrediting the lesser of the amount charged or \$25 [sic: \$2,500] with interest being recredited and any remaining amount with 45 calendar days. That is an important act of simplification.

149 Cong. Rec. H 4999-5000, June 5, 2003.

The first three items discussed below **must** be changed in order for the proposed **rule** to serve Congress' goal of offering recredit as a simple, accessible remedy when a substitute check was erroneously charged to a consumer's account.

The rule should not restrict recredit to a consumer who was provided with a substitute check.

Congress' intent should be honored by resolving a significant ambiguity in the statutory **language of the** recredit section in **favor** of more access to recredit. The first subsection of the recredit section of Check 21 talks about the claim existing **when** a substitute check "was provided" to the consumer; **but the two** more specific subsections on the procedures for claims **and on when** a bank must recredit a consumer account both omit any restriction on the right of recredit only to substitute checks that were provided to the consumer. Each of these two more specific subsections focus not on what was provided to consumer, but on what was charged against the consumer's account.

Section 7(a)(1)(A) of Check 21 states that, in general, **a** consumer **may** make a claim for expedited recredit if the consumer asserts **in** good faith that the bank charged the consumer's account for a substitute check that **was** provided to the consumer. However, the more specific "procedures for **claims**" provisions of subsection 7(b) do not require a consumer to allege or prove that he or she was provided with a substitute check. Even more importantly, subsection

7(c), states when “the bank **shall** recredit” a consumer’s account without conditioning recredit upon the consumer **having** been provided with a substitute check. Under subsections (b) and (c), the availability of recredit depends upon whether a substitute check was properly charged to a consumer account, and whether the bank has both provided the consumer **with** the original check or an accurate copy of the original check and demonstrated to the consumer that the substitute check **was** properly charged to the consumer account.

Subsection 7(b) requires that the consumer give the bank a description of the claim, including an explanation of why the substitute check was not properly charged to the consumer’s account or an explanation of the warranty claim with respect to such check. The consumer must also state that he or she suffered a loss, give an estimate of the amount of the loss, and give the reason why production of the original check or a better copy of the original check is necessary to determine the validity of the charge to the consumer’s account or of the warranty claim. Finally, the consumer must give sufficient information to identify the substitute check and to investigate the claim. There is *no* requirement in subsection 7(b) that the consumer provide a copy of the substitute check, and *no* requirement that the consumer allege that she was provided with a substitute check. Instead, the claim procedure is focused on showing that a substitute check was erroneously charged to the consumer’s account, and **how** that erroneous charge harmed the consumer.

Subsection 7(c) plainly states a bank’s obligation to recredit a consumer account without limiting that obligation to those occasions when a substitute check **was** provided to the consumer. Subsection (c) requires that a bank “shall recredit a consumer account...for the amount of a substitute check that **was** charged against the consumer account” if the consumer submits a claim that meets the requirements of subsection (b) and the bank has not provided to the consumer the original check or a better copy of the original check and also demonstrated to the consumer that the substitute check **was** properly charged to the consumer account.

The availability of expedited recredit for a breach of a warranty claim is additional evidence that Congress did not intend to restrict the right of recredit solely to circumstances where a substitute check was provided to a consumer. Subsection 7(a) and 7(b) both refer to the availability of recredit for a check upon which the consumer has a warranty claim. The warranty, however, as defined in Section 5 of Check 21, **is** triggered by the transfer, presentment or return of a substitute check for consideration “regardless of whether the warrantee receives the substitute check or another **paper** or electronic form of the substitute check or original check.” This language in Section 5 expressly defines the warranty claim to be available when a substitute check was charged to the account, regardless of **what** was provided to the consumer.

The substitute check warranty **is** a key warranty, protecting consumers against the risk of double payment when a substitute check has been used. It would make very little sense to structure the recredit right as a remedy for this “no double debit” warranty but then restrict recredit to when the consumer was provided a substitute check. The warranty explicitly runs to the consumer regardless of **what** the consumer has received, including a paper or electronic form or the substitute or the original check.

The legislative history strongly suggests that Congress intended the remedy of expedited recredit to be available to all consumers with a dispute about whether a substitute check was properly charged. The principal sponsor of the measure, Congress Member Ford, told the House

Subcommittee on Financial Institutions and Consumer Credit of the Committee on Financial Services:

Finally, Check 21 establishes a new consumer right—an expedited re-credit for contested substitute checks. If a substitute check is not properly charged to a consumer's account, banks must re-credit the consumer for the amount of the check, up to \$2,500, within 10 business days. This is a new and important consumer protection established by this bill.

Transcript of hearing on H.R. 1474—Check Clearing for the 21st Century Act, Committee on Financial Institutions and Consumer Credit, Committee on Financial Services, April 8, 2003, p. 7.

Congress Member Ford similarly described the bill to the full House at the reading of the conference report: “Check 21 is a strongly pro-consumer bill.” He described for the full House four areas in which Check 21 is pro-consumer, including:

Fourth, Check 21 establishes a new and important consumer protection - an expedited *recredit for contested substitute checks*. A consumer **who** raises a dispute because a check that *has been rendered into a substitute has been improperly charged* to his account will, receive a recredit within 10 business days, for amounts **up** to \$2,500. This ‘right of recredit’ is an important part of this bill.

149 Cong. Rec. H 9290-9291 (Oct. 8, 2003) (italics added).

The bill's principal legislative sponsor described the right of recredit as a right which *is* available “*for contested substitute checks*” which have “*been improperly charged.*” The scope of the right of recredit under the proposed rule is significantly narrower than this. The Congressional discussion ties the availability of the right of recredit to whether a substitute check has been improperly charged to a consumer's account, not to whether a substitute check was provided to the consumer. The bill's principal sponsor Congress Member Ford goes on to note that where there were differences in the House and Senate bills, “in each case, the conference adopted the pro-consumer position.” He went on to point out that the conference report retains an amendment: “which stipulated that the consumer need not currently be in possession of the substitute check to enjoy the right of expedited recredit.” 149 Cong. Rec. H 9291. (Oct. 8, 2003).

The Congressional intent that recredit be **available** to remedy a contested substitute check which has been improperly charged to a consumer's account can only be honored by resolving the statutory ambiguity between subsection 7(a), which refers to a substitute check having been provided, and subsections 7(b) and 7(c), which confer a right of recredit irrespective of whether a substitute check was provided, in favor of subsections 7(b) and 7(c). To do this, proposed Section 229.54(a) and the associated commentary must be changed to eliminate any “was provided” precondition to recredit.

If a “was provided” requirement is retained in the rule, then the rule and commentary should be changed to indicate that a consumer who receives an image of a substitute check was provided with a substitute check.

Under both Section 7(a) of the statute and Section 229.54(a) of the proposed rule, a consumer is entitled to **make** a claim for recredit “for a substitute check that **was** provided to the consumer.” As discussed above, other parts of Section 7, including the subsection 7(c) that requires a bank to

make the recredit, do not make “was provided” a precondition to the right of recredit. If, however, this is retained as a precondition in the rule, then the scope of the recredit right will be significantly affected by **how** the triggering condition of “was provided” can be satisfied. This is not addressed in the statute. The commentary takes a too narrow approach, concluding that a substitute check cannot be provided to the consumer electronically. Comment 1 to Section 229.54(a) states that “a consumer that received only **an** image statement conining an image of a substitute check would not be entitled to make an expedited recredit claim.. .”

As banks enter into image statement agreements **with** their customers, it is more and more likely that the substitute check **will** be “provided” as an electronic image, rather than as a paper copy. The definitions state that a substitute check is a paper item but those definitions do not address the effect of providing that paper item electronically, in the same fashion that other documents required by **law** to **be** in writing can be provided electronically.

The rule permits a bank to discharge its obligation to a consumer to provide an original check or a sufficient copy by providing **an** electronic image, where tlc consumer has agreed to receive that informarion electronically. Sections 229.54(e)(2)(i), 229.58. At the same time, the commentary treats the provision of an electronic image of a substitute check to a consumer pursuant to an agreement as *not* qualifying as the provision of a substitute check sufficient to trigger the recredit right. Comment 1 to Section 229.54(a). Thus, the commentary allows a bank to satisfy its obligations to a consumer electronically, but does iiot allow a substitute check that **was** provided electronically to trigger a consumer’s recredit rights. This makes no sense.

The commentary overstates the requirements of the statute when it says that a consumer may make a claim for expedited recredit only for a substitute check that lie or **she** “has received.” “Received” is not a requirement found in any part of Section 7 of Check 21. Section 7(a) discusses a substitute check that “was provided” to the consumer. Paper documents can be *provided* electronically, when the consumer has agreed to receive them electronically. This is the heart of the federal Electronic Signatures in Global and National Commerce Act (E-Sign).’ 12 U.S.C. § 7001.

As discussed above, **we** question whether, in fact, the statute restricts recredit to when a substitute check “was provided” to the consumer, and urge that the conflicting statements in subsection 7(a) as compared to subsections 7(b) and (c) be resolved in favor of the language of subsections 7(b) **and** (c) and the absence of **any** “was provided” requirement. However, the structure of Section 7 provides strong support for the conclusion that, *if* a substitute check must be provided to trigger the recredit right, it could be provided by making the substitute check available in electronic form or by making it available on request, as well as by including it with the statement. For example, subsection 7(a)(2) provides a rule for starting the consumer’s **time** to make a claim. It does not tie that **time** period to the date that a substitute check **was** provided to the consumer. Instead, subsection 7(a)(2) triggers the time period for action by the consumer from the later of the date that the financial institution mails or delivers a periodic Statement of account which contains the information concerning the transaction, or the date on which a substitute check is “made available” to the consumer. This suggests that making the substitute check available *in* electronic form, or available upon request, should be sufficient to satisfy any “was provided” precondition.

Subsection 7(h) also supports the interpretation that the consumer need not have been provided with a physical paper substitute check in order to exercise the right of recredit. This subsectionii

clarifies that a consumer who **was** provided a substitute check may make a claim for expedited recredit under Section 7 “whether or not the consumer is in possession of the substitute check.” There are several reasons **why** a consumer would not be in possession of a substitute check which **was** provided to the consumer, including that the substitute **check was** lost, the substitute check **was** provided electronically, or that the provision of the substitute check occurred by giving the consumer a right to request the substitute check rather than by sending a physical paper document.

The author of this amendment, Congress Member Davis (AL), engaged in an extensive discussion with witnesses from Consumers Union and from the banks, expressing the view that consumer should be able to access the recredit right without a physical substitute check.
Congress Member **Davis**:

Let me **ask** you a fairly basic question. Do you or Mr. Cloutier or **anybody** else on the panel think that the substitute check is **an important** instrument in resolving a dispute between a consumer and the bank, **or** resolving some issue as to the amount of how much a check was written for? Do any of you think that **a** substitute check is a necessary part or even **a very** helpful part **in** getting to the bottom of that kind of a question?

Mr. Cole;

Only to **the** extent that that is **what is** presented to our bank—if that is the evidence that we have. Now, **we** will also have **that** on microfilm, so it **is** very unimportant, actually. **We** will be using **the** records.

Congress Member Davis:

So presumably what Ms. Duncan is saying is that obviously if someone walks in with a substitute check, that is a very strong argument **in** their quiver. But if **they** do **not** walk in with **a** substitute check, there are any number of other means for determining a dispute. That is presumably **what she is** saying. Now, given that, why isn't she correct? If the substitute check is **not** necessary to get to the bottom of a dispute between a consumer or customer and the bank, why should **we** differentiate between people who have a substitute check and those who do not with respect to the re-credit provisions?

Transcript of hearing on H.R. 1474—Check Clearing for the 21st Century **Act**, Committee of Financial Institutions, **April 8, 2003, p. 53.**

The rule and the commentary should be changed so that any precondition to recredit that a substitute check **was** provided is satisfied **if** the consumer was provided with either: 1) an image of a substitute check; or 2) another form of check image accompanied by a right to request a substitute check.

If the rule retains any “was provided” precondition on recredit, **then** the issue of whether that provision could be through an image significantly affects the scope of the right to recredit. The narrow interpretation in the draft commentary will restrict the right of recredit far more than necessary; is inconsistent with the principles of electronic provision of consumer information authorized by E-Sign; and will require consumers to learn about and engage in the extra step of requesting a paper substitute check in order to invoke the legal rights provided by the statute.

The extra step of requiring a paper form of the substitute check is inconsistent with the legislative history about the purpose of the recredit right. At the second House Subcommittee hearing on Check 21, Chairman Oxley stated that “there is little need for paper checks in today’s payment system,” then **went** on to say “This bill protects consumers by ensuring that they have *the ability to retrieve improperly debited funds* and are given information on the operation of this new system.” Transcript of hearing on H.R. 1474—Check Clearing for the 21st Century Act, U.S. House of Representatives, Committee on Financial Institutions and Consumer Credit, Committee on Financial Services, April 8, 2003, p. 5 (italics added). Congress Member Hart, also a principal legislative sponsor of Check 21, told the House Subcommittee: “Consumers will benefit from a new expedited right of re-credit for amounts **up** to \$2,500.” Transcript of hearing on H.R. 1474—Check Clearing for the 21st Century Act, U.S. House of Representatives, Committee on Financial Institutions and Consumer Credit, Committee on Financial Services, April 8, 2003, p. 9.

It makes no sense to treat a consumer who receives a statement containing an image of a substitute check differently from a consumer who receives a paper substitute check. If there is a dispute about the payment of the check, that dispute is highly likely to be about the amount paid, the person to whom the check **was** paid, or the number of times the check was paid. None of these are any less of an issue because the consumer **was** given an image of a substitute check rather than a hard copy of the substitute check.³

The commentary’s conclusion that a substitute check is insufficient to satisfy any “**was provided**” precondition on the recredit right also **is** inconsistent with principles of efficiency and economy in the banking system. Banks may wish to encourage consumers to accept image statements because they are cheaper to provide. Some consumers may want image statements, **because** they can more readily manipulate the information on a home computer, if the consumer feels that computer is sufficiently secure. However, if substitute check rights attach only when a physical paper substitute check is provided, and not when the substitute check is provided via an electronic image, then consumers can maximize their consumer rights only by behaving in the least efficient fashion for the banks—by insisting on paper substitute checks. Since image accounts are likely to permit the consumer to request a copy of an image received, it seems particularly illogical for the rule to deprive consumers who received an image form of a substitute check of the opportunity for recredit. The effect will either be to add delay while consumers seek physical paper substitute checks, or the loss of consumer rights due to lack of knowledge that the consumer’s rights would improve if he or she requested a paper substitute check.

If the Federal Reserve Board resolves the ambiguity in the statute against consumer protection and retains the proposed rule’s approach that recredit requires that a substitute check “**was provided,**” **then** the Board should treat that requirement as satisfied by provision of an image of the substitute check, **and** by provision of another **kind** of image accompanied **by** the right to request a substitute check. This requires a change in Comment 1 to Section 229.54(a).

³ The comments suggest **that a consumer who receives an image of a substitute check will** have the warranty, but not the recredit. Having the substitute check **warranty without** the recredit right is inadequate. The recredit right **was added** precisely because the remedies for check warranty generally available under *the UCC* are not practical for most consumers. Indeed, in describing the need for **the right** of recredit, **as a more simple and usable right than any** offered by the UCC, Congress Member Davis (AL) described the UCC as “something of an imponderable maze.” 149 Cong. Rec. H 4999, June 5, 2003.

The rule must require a bank to provide the consumer with a substitute check in response to a request for a substitute check, an original check, or a copy of an original check.

The rule must be changed to expressly confer on consumers a right to receive a substitute check on request. If the right of recredit is to depend upon provision of a substitute check, and a bank can defeat that right simply by refusing to provide a substitute check when requested, then the right is truly illusory.

The legislative history does not suggest that Congress intended the Check 21 right of recredit to be an illusion or a sham. The bill's principal sponsor, Congress Member Ford, referred to the right of recredit as "a new protection for consumers." 149 Cong. Rec. H 4999, June 5, 2003.

Congress Member Bachus described the conference committee's action on Check 21, thus: "we have also added new consumer protections that go beyond present law." 149 Cong. Rec. H 9292 (Oct. 8, 2003). Congress Member Frank also referred to the fact that in the bill: "We add new protections for consumers." He referred to the right of recredit, as already described by Mr. Ford, as one of those protections. 149 Cong. Rec. H 9292 (Oct. 8, 2003).

The legislative history also reveals Congress' expectation that Consumers would in fact be able to get substitute checks under Check 21. Chairman Oxley told the full House, in introducing the conference report on H.R. 1474: "businesses and consumers continue to have the option of accepting checks in paper form." 149 Cong. Rec. H 9290, Oct. 8, 2003. Congress Member Bachus stated that consumers will have a right to get a substitute check under Check 21. In response to a question by Congress Member Sanders about how many people in fact would be getting substitute checks, Congress Member Bachus stated: "*And she will have a right to get those, so she will have that right if she wants it. She can request it.*" Transcript of hearing on H.R. 1474—Check Clearing for the 21st Century Act, U.S. House of Representatives, Committee on Financial Institutions and Consumer Credit, Committee on Financial Services, April 8, 2003, p. 11 (italics added). Congress Member Frank told the full House that the Act promotes efficiency "while protecting consumers," stating: "This bill, as I said, does do that with regard to your *ability to get the check if you actually need it.*" 149 Cong. Rec. H 4996 (italics added). Referring to a consumer's access to a substitute check, the Federal Reserve Board's Dr. Ferguson assured the House Subcommittee that consumers "*simply have to request one.*" Transcript of hearing on H.R. 1474—Check Clearing for the 21st Century Act, U.S. House of Representatives, Committee on Financial Institutions and Consumer Credit, Committee on Financial Services, April 8, 2003, p. 23 (italics added).

The Board's Vice Chairman also told Senators that consumers have a right under Check 21 to receive a paper substitute check on request. He stated to the Committee on Banking, Housing and Urban Affairs of the U.S. Senate:

I have been privileged to work with this committee on one such initiative, the Check Truncation Act, or Check 21. This legislation removes a legal impediment and should, over time, foster greater use of electronics in the check clearing process *while also preserving the rights of consumers and banks to receive paper checks.*

Testimony of Vice Chairman Roger W. Ferguson, Jr., statement on his renomination as Vice Chairman of the Board, to the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, Oct. 14, 2003, p. 3.

If a bank can simply refuse to provide a consumer with a substitute check even on request, then the right of recredit will be easily evaded. Congress gave the Board the authority to prescribe regulations “as may be necessary to implement, prevent circumvention or evasion of, or facilitate compliance with the provisions of this Act.” Check 21, Section 15. The Board should prevent evasion of the recredit right by requiring depository and payee banks to provide a **consumer** with a substitute check on request. Since consumers **may** not know exactly what to ask for, the obligation to provide a substitute check should **apply** when the consumer requests a substitute check, an original check, or a copy of an original check.

The rule does not adequately set forth the standards a bank must meet to find a recredit claim invalid. It omits the key statutory requirement that the recredit must be given if the bank has not “demonstrated to the consumer that the substitute check was properly charged to the consumer account.”

Section 7(c) of **Check 21** requires that a bank must recredit the consumer’s account, when the consumer submits a claim meeting the procedural requirements of Section 7(b), if the bank has not both provided the original check or an accurate copy of the original check and “demonstrated to the consumer that the substitute check was properly charged to the consumer account.” Section 7(c)(1)(B)(i)(II). The proposed rule, by contrast, entirely omits the obligation of a bank, **which** denies a claim to demonstrate that the substitute check **was** properly charged to the consumer account. The proposed rule simply tells a bank what to do if it determines a claim to be **valid** or invalid, but the rule is silent on how a bank is to **make** that determination. Section 229.54(c)(1) and (2). This silence suggests a degree of discretion in the **bank** which is wholly inconsistent with the statute, and which omits a key consumer protection adopted by Congress—that a bank shall recredit the consumer’s account if the bank has not “demonstrated to the consumer that the substitute check **was** properly charged to the consumer account.” Section 229.54(c) of the proposed rule must be revised to incorporate this requirement of Section 7(c)(1)(B)(i)(II) of the Act.

The rule should make it clear that the consumer, not the bank, determines whether a copy is sufficient to resolve the dispute.

The statute refers to the original check or a better copy of the original check. The rule replaces “better copy” with “sufficient copy,” but does not state in Section 229.54 on recredit or in the definition of “sufficient copy” in Section 229.2(aaa) who decides whether a copy is sufficient. The concept of “sufficient copy” should not replace the statutory requirement for a “**better copy**,” unless the rule also requires that, for a copy to be sufficient, it is either a better copy than **what** has previously been provided to the consumer, or it is a copy which otherwise resolves the dispute to the customer’s satisfaction; that is, a copy that the consumer deems to be sufficient.

If a bank can make a unilateral decision that a copy is sufficient, the **consumer** will not be put in the same place by Check 21 as if the original check had been provided. Allowing the **consumer**, rather than a bank, to determine a sufficiency of the copy is one way to ensure that a bank does

not attempt to satisfy the statutory obligation to provide a better copy with a copy that is not adequate to resolve the dispute. This change will also prevent a bank from simply re-providing to the consumer the same document which the consumer has already found to be inadequate. Giving the consumer another copy of what he or she has already found to be insufficient, and about which a claim has been filed, cannot meet the statutory requirement for production of either the “original check or a better copy” of the original check. The proposed rule’s use of the term “sufficient copy” should not change that result.

The rule should be changed to clarify that an oral claim is timely even if information is required in writing.

Comments 7 and 9 to Section 229.54(b) say that a bank may insist on a written claim, rather than on written information in support of a timely oral claim. This is inconsistent with the statute, which permits an oral claim. We do not object to the portion of Section 229.54(b) that starts the time clock for bank action from the submission of the information which the bank is permitted to require in writing. However, the commentary errs when it characterizes the written submission as the actual claim when there has been a prior oral claim. This makes a difference in determining whether a claim is timely.

Section 7(a)(1) of Check 21 defines a claim without requiring that it be in writing. A bank’s exercise of its discretion to require that the information be provided in writing does not prevent the initial oral claim from satisfying the time period requirement. Section 7(b)(2) refers to the discretion of the bank to require the consumer to submit “the information” in writing, not to any discretion in the bank to require that the claim *itself* be submitted in writing. The claim exists when it is made orally, even if the bank subsequently exercises its right to require that information be provided in writing. The oral claim should satisfy the time period for action by the consumer. The rule should be augmented, and comments 7 and 9 to Section 229.54(b) changed, to make this clear.

The rule should be augmented to obligate the bank to inform the consumer of an incomplete claim.

Comment 10 to Section 229.54(b) states that an incomplete claim is “not a claim for purposes of § 229.54.” If an incomplete claim is not a claim, then there will be no obligation under the statute or rule to tell the consumer that the claim has been denied, or even that it is incomplete. This could lead to abuse. The rule and commentary should either include an incomplete claim as a claim for purposes of notice of denial of the claim, or the Federal Reserve Board, acting under the general implementing power conferred by Section 15 of the Act, should augment the rule to require that a bank give the consumer notice; 1) that the claim is incomplete and does not qualify as a claim, and 2) what additional information would have to be provided to complete the claim. This is particularly important when the incompleteness could be remedied before expiration of the time to make a claim. If the consumer receives no notice that the claim is incomplete, the time to submit a proper claim could expire while the consumer waits for the bank to act on the incomplete claim. The rule should not permit a bank to simply ignore a claim which the consumer has no reason to know is incomplete.

The rule should direct banks to reverse NSF fees and other adverse consequences to the consumer after an error in processing a substitute check.

The rule should be augmented to require that a bank reverse NSF fees and other adverse actions caused by wrongful payment of a substitute check once the bank has determined that a substitute check was **paid** in error, such as for the wrong amount, to the wrong person, paid twice, or another error. The statute and proposed rule are silent about the handling of an NSF fee which was imposed on a substitute check that is later the subject of a dispute, **and** about NSF fees that were imposed on other checks which would have cleared if not for the payment of the disputed check which is subsequently reversed. The commentary does recognize that NSF fees caused by an erroneous debit are proximately caused losses covered by the substitute check warranty. Comment 2, example a, to Section 229.53(b)(indemnity). However, there is no discussion of an obligation to reverse these charges when a recredit is given, or to reverse other adverse actions stemming from the erroneous payment, such as a report to ChexSystems or a similar entity, an overdraft fee, **or** an internal “account overdrawn” counter which affects future funds availability.

The rule, or at least the commentary, should remind banks of the general obligation not to charge or retain fees from consumers that are not owed, and not to take or maintain an action that adversely affects the consumer which is not grounded in contract and in fact. For this reason, after a bank determines that a claim for recredit is valid, the rule should require that the bank reverse associated NSF and overdraft fees, withdraw or correct reports to ChexSystems or other account history databases, and reverse any other adverse actions **by** the bank against the **consumer** flowing from what the bank has determined was an error. If such corrections are not required to be automatic, then the consumer and the bank would have to engage in the economically wasteful activity of a separate warranty claim solely to address these additional proximately caused losses after the main issue has been resolved through the recredit process. Less sophisticated consumers are unlikely to pursue that claim, and thus will be the ones who suffer the continuation of unjustified adverse consequences.

The rule should disallow or place a strict time limit on reversal of a recredit after the bank has notified the consumer it has determined the claim to be valid.

Section 229.54(c)(4) allows a bank to reverse a recredit given under (c)(1) or (c)(3). The rule places **no** time limit on **how** long after the recredit the bank **may** reverse, and the rule permits a reversal **even** after the bank has notified the consumer that the bank determined the consumer’s claim to be valid. Comment 2 to Section 229.54(c) says that the reversal may be “at any time later.”

Although the statute permits reversal after a finding of a valid claim, the Federal Reserve Board should use its Section 15 implementing authority to prohibit or at least strictly limit the time period for reversal after the bank determines that a claim is valid. An open-ended time for reversal is unfair and impractical for the consumer. Consumers **need** to know how much money they have available for family expenses. A long-delayed reversal of a recredit, or indeed any reversal, after the bank has notified the consumer that the bank has found the claim to be valid, will interfere with certainty and household budgeting. Once a bank has notified a consumer that a claim is valid, there should be no opportunity for reversal. If this cannot be done, then a time a period of no more than 10 days should be provided for a reversal of a recredit after the bank notifies the consumer that the claim has been granted. We do not suggest, of course, that the

time period for reversing a provisional recredit be changed, but only that there should be enhanced certainty for consumers once a bank determines that a claim is valid.

The rule or commentary should prohibit a bank from charging any fees in connection with a request for recredit.

The rule or the commentary should remind banks that they may not charge the consumer a fee for copies of the documents relied upon in denying or reversing a recredit; nor a fee for an investigation into a claim for recredit.

The commentary should not refer to the bank's "belief" that the check was properly charged,

Comment 2 to Section 229.54(e) directs a bank denying a recredit claim to explain the reason for the denial, "such as the reason the bank *believes* the substitute check was proper..." (italics added). This language should be changed. Check 21 allows a bank to deny a claim for recredit when the bank has "*demonstrated* to the consumer that the substitute check was properly charged to the consumer account." Section 7(c)(i)(B)(i)(II). (italics added). The commentary should not suggest a lesser standard.

Examples in the commentary of the application of recredit for a double debit would be useful.

An additional area of the concern at the time Congress considered Check 21 was double debit. This issue is well-covered in the comments on Section 229.52(a) on the content of the substitute check warranty, but the commentary on recredit does not explain how warranty and recredit fit together. The recredit commentary should include examples of how the recredit would be used in seeking to rectify a double debit. It should include examples where: 1) both the original and a substitute check were charged, 2) two substitute checks were created and charged, and 3) a substitute check was charged and there was also an ACH charge arising from the same information. These examples should make it clear that the recredit right applies regardless of the order in which the erroneous charges occurred.

Comment 5 to Section 229.52(a) implies, but does not state, that whether the substitute check was the first or second item to be charged does not affect the validity of the warranty claim. It would be helpful to make this clear. Comment 5 to Section 229.52(a) on warranty is also helpful in that it makes clear that the double debit claim is in no way dependent on fault. It clarifies that the warranty applies even where the demand for duplicate payment arises from a fraud which has been perpetrated on both the bank and the consumer.

Warranty issues

Substitute check warranty coverage for an ACH payment is appropriate only if it does not disturb application of Regulation E.

If one of two payments stemming from the same check was an ACH payment, then that transaction will involve both the substitute check warranty **against** double payment and Regulation E. The proposal asks whether information from a check used to create an ACH data entry should be a payment request covered by ~~the~~ substitute check warranty. **We** believe that it should, but only if this characterization will not interfere with application of Regulation E as well to that payment transaction. If only one legal scheme can **apply** to an ACH payment originating from a substitute check, then the Board should choose Regulation E, which is more protective of consumers.

Comment 1 to Section 229.53(b) and its examples are useful.

This comment gives very useful examples of how damages are measured in a warranty claim, including the treatment of NSF fees and attorneys fees. The example on the effect of the absence of a legal equivalence legend also is helpful.

Consumer notice issues

All consumers need the substitute check notice.

The statute directly requires notice about the nature and rights attaching to substitute checks only for consumers who receive **original** checks or substitute checks. Check 21, Section 12. Section 229.57(b) thus describes the distribution of notices only for consumers who receive paid checks with periodic statements or who receive a substitute check. The Board should use its Section 15 authority to require that the notice be given to **all** consumers whose accounts include a checking feature, not later than the first scheduled communication after October 28, 2004. While it is useful for the notice to accompany a substitute check sent in response to a request for an original check, receipt of the substitute check should **not** be the only trigger for that notice for consumers not otherwise receiving original or substitute checks.

How will the consumer even **know** to request a substitute check without the notice? **A** consumer who is not currently receiving original paid checks, **and** may not **even** know what a substitute check is, ~~has the~~ same need to understand the nature of substitute checks and to know about the warranty, indemnity, and recredit rights as **any** other consumer. Further, because the substitute check warranty applies **whenever** a substitute check has been *used*, all consumers should be given **a** notice explaining the concept of substitute checks, **how** they may be used, and what rights **apply**.

We urge the Board to exercise its implementing authority under Section 15 of the Check 21 Act to require that the consumer notice be given to all consumer checking account customers, not merely to those **who** request or receive original or substitute checks.

The key model consumer notice inaccurately tells consumers that recredit is limited to losses “because you received a substitute check.”

Notice C5-A, Substitute Check Policy Disclosure, is inaccurate. This notice states in the second paragraph: “If you lose money *because you received* a substitute check, you have the right to file a claim for an expedited refund.” Later, the text of the notice more accurately states that federal law gives consumers the right to an expedited refund if the substitute check **was** incorrectly charged to the consumer’s account, there was a loss to the consumer, and the original check or a better copy is issued. However, the earlier statement—that the loss must be “because” of receipt of the substitute check—is inaccurate. In fact, the basis for a right of recredit is that a substitute check **was** either not properly charged to the consumer’s account or the consumer has a warranty claim, and the consumer suffered a loss. Check 21, Section 7. The statute does not restrict recredit to circumstances where the loss was “because” of receipt of a substitute check. The “because” statement in the draft notice is misleading and should be eliminated.

The notice should tell the consumer that he or she may also have a warranty right.

The notice says it describes “the rights that you **will** have when you *receive* substitute checks.” There is a strong implication in this language that a consumer has rights with respect to substitute checks **only** when the consumer receives a substitute check. Whether or not recredit requires that the consumer was provided with a substitute check, the **warranty** right is independent of provision to the consumer of a substitute check. Describing the consumer’s new substitute check rights as if they are triggered only by receipt of a substitute check is likely to mislead consumers. In general, the notice is not designed to inform consumers about the warranty right, which attaches to use of a substitute check regardless of what is or is not returned to the consumer. However, consumers need this information.

The use of the term “send” in the notice implies that oral claims not permitted.

The text under “expedited refund” says “you must send us a claim.” Because Section 7 of Check 21 allows for an oral claim, the phrase “you must send” is inaccurate. Even if the bank insists upon supplemental written information, the consumer **is not** required by statute to send a written claim, **but** rather to follow **up** the oral claim with certain requested written information. It would be more accurate to say “you must make a claim.”

The notice should directly answer the question: “Where is my original check?”

The notice should answer a key question that will be on consumers’ minds—“What happened to my original check?” The notice should tell the consumers that **if** the consumer wants his or her original check, or a copy of it, to **ask** for a substitute check. It should also tell consumers that they have the right to receive a substitute check on request.

The notice should inform consumers of a key consequence of Check 21—shorter float,

A key consequence for consumers of Check 21 is that checks written by consumers will clear faster. Consumers who may have an expectation about float on the checks they write are likely to find more checks bouncing. While the statute does not require that the notice inform consumers about reduced float, failing to do so will lead to more bounced checks, more NSF fee revenue for banks, and more financial headaches for consumers. The basic notice about substitute checks should be modified to tell consumers that the statute will speed up check clearing so that the checks which consumers write are likely to be presented against their accounts sooner. Sample language for this and several other suggested changes is provided in the attachment following these comments. Some of the items we suggest adding to the model notice are not required by the statute, but the Board could require them under its Section 15 implementing authority.

The Board should provide the model notices in plain language.

We strongly suggest that the Federal Reserve Board seek input on the model forms from a plain language expert and make them as simple as possible, so that they will be more useful to consumers. There is always a tension between high levels of technical accuracy and plain language. However, an extremely accurate notice is of no use to consumers if most consumers do not understand it.

The Board should provide the model notices in both English and Spanish.

The Board should publish the model notice forms in both English and Spanish. While the commentary points out that a bank may provide the disclosures in Spanish, so long as the English-language disclosures are available upon request, it would be much more helpful for the Board to provide a set of the actual model forms in Spanish. This could increase the number of banks who choose to provide the disclosure in both languages, thus helping to educate more consumers about their rights and obligations under Check 21.

The rule must require banks to accurately respond to consumer inquiries about how a particular check was processed and what rights and obligations attach to that check;

Since the passage of Check 21, Consumers Union has been receiving questions from consumers and the media. These questions are posed as questions about Check 21, but they are coming mostly from persons who have experienced non-return of a paper check due to electronic check conversion. The nature of these questions suggests that consumers, members of the media, and possibly even some bank employees may be mixing up check conversion, which is fully covered by Regulation E, with Check 21-check imaging, which is not. A Chicago journalist who called several local banks in February 2004 told Consumers Union that the bank employees he spoke to could not explain to him what had happened to his paper check, or why his paper check was unavailable. Some of the consumers who have contacted Consumers Union contacted their banks first, and formed an impression that Check 21 was the reason that they did not receive back an original check. Conversations between Consumers Union and those consumers revealed that their original checks were non-returned for a different reason—the checks were subject to

electronic check conversion by non-bank payees. 'Telling consumers that a check **was** processed under Check 21 when it in fact was processed under electronic check conversion would be misleading and deceptive, because consumers have recredit rights for electronic check conversion transactions with no dollar cap under Regulation E.

If these kinds of questions and confusion are arising now, before Check 21 is effective, they can be expected to be more widespread once Check 21 goes into effect. The Federal Reserve Board should add to the proposed rule an obligation on banks to clearly and *accurately* respond to consumer inquiries about why the consumer **has** not received an original check, and about how a check **was** processed. 'These responses should include accurate information to the consumer about what set of rights and responsibilities apply to **my** particular check.

Banks might argue that it is difficult to tell how a check **has** been processed and what legal rights **apply**, but if even the bank can't tell, how is a consumer to determine what has happened to her check, and to identify **her** rights and obligations when something **has** gone wrong? As with several of the other notice issues, the Federal Reserve Board could impose such a requirement in the rule under its Section 15 implementing authority.

The rule should require banks to tell consumers when they request an original check or a copy of an original check that they may request a substitute check which is legally equivalent to the original check.

A key purpose of the substitute check is to put consumers in the **same** place as if they have received the original check. This purpose cannot be served if a consumer who contacts his or her bank and **asks** for the original check is told: "We don't **have** the original check," without **also** being told about the existence and availability of the substitute check. The rule should expressly require banks to tell consumers about the availability of a legally equivalent copy of the original check **when** a consumer asks for the original check or for a copy of the original check.

The rule should expressly require compliance with E-Sign for notices to consumers.

Section 229.58 allows delivery of notices or other information by mail **or** by any other means agreed to by the consumer. **The** rule should be clarified to ensure that it authorizes delivery to a consumer by electronic means only **when** the requirements of E-Sign, including a consumer consent meeting the standards of E-Sign, have been met.

Because E-Sign addresses requirements that would otherwise be required **by law** to be in writing, a simple rule authorizing electronic delivery "if agreed" could be read to remove the notice covered by that standard from E-Sign, by removing the threshold requirement in the underlying statute or rule that the notice or information be provided in writing. The commentary suggests that there **was** no intent to undermine application of E-Sign, at least **with** respect to a bank's communications with **its** consumers.

Section 229.58 should be altered to condition the authorization for electronic delivery to consumers on compliance with E-Sign, closing off **an** assertion that a generalized "agreement" not complying with E-Sign's consent standards would be sufficient. The handling of this issue in the commentary is not sufficient to resolve this problem. Comments 37 and 38 to Section

229.2(d) say that compliance with E-Sign satisfies the requirement for written notice to a bank's consumer, but they do not say that compliance with E-Sign is necessary to give the notice in electronic form. The rule and commentary should require E-Sign compliance for communications with the bank's consumers.

Other substitute check issues

Non-bank creation of substitute checks will increase consumer confusion and should be prohibited.

We appreciate the acknowledgement in the commentary at Comment 2 to Section 229.51(a) that if a non-bank can create a substitute check, then the bank of first deposit must accept responsibility for, and make warranties about, that substitute check. However, we are concerned that permitting a non-bank to create a substitute check will make it extremely difficult for consumers to determine whether an electronically processed check is covered by Check 21 (as a substitute check) or by Regulation E (as an electronic check conversion). It is confusing enough for consumers that merchants convert checks under Regulation E, while banks may create either substitute checks with similar but more limited rights, or images of original checks that lack even substitute check rights. However, if a non-bank payee can take a single check and either create a substitute check or perform an electronic check conversion, the consumer's ability to find out what happened, and thus what consumer rights apply, may be hopelessly muddled.

Now, consumers are often able to learn that it was the payee who transformed a check for electronic processing. The consumer should not also have to determine what the payee called that transformation. A bank that permits its customers to both use electronic check conversion and to create Check 21 substitute checks will violate Regulation E in handling a dispute if it gives the consumer erroneous information about which method was used, since the right of expedited recredit under Regulation E is broader; for example, it has no dollar cap.

The only solution we see to this maze is for the Federal Reserve Board to draw a clean line between electronic check conversion and substitute checks by using its Section 15 implementing authority under Check 21 to restrict the creation of substitute checks to banks. Non-bank payees who wish to transform checks for electronic processing can continue to do so through electronic check conversion, with all the protections of Regulation E for the consumer. Banks will be able to inform consumers quite simply what scheme applies — Regulation E if the payee converted the check; Check 21 if a bank created a substitute check.

The treatment of a purported substitute check with a MICR error as a substitute check is appropriate, but the concept should also apply to other types of errors on paid substitute checks.

We favor the special rule in section 229.51(c) of the proposed rule on purported substitute checks, but it may be too narrow. We agree that it is necessary to treat as a substitute check, for the purposes of warranty, indemnity, and recredit, an item that would be a substitute check if not for a MICR line error. Any other result would put a significant loophole in the substitute check protections. However, we question why only a MICR line error should qualify a purported

substitute check for treatment as a substitute check, and for attachment of the substitute check warranty if that purported substitute check has been paid.

Once a purported substitute check has been paid, the consumer has the same need for the warranties, indemnity, expedited recredit, and liability provisions for that defective, but paid, substitute check as for a defective substitute check with a MICR line error. We do not suggest that a defective substitute check must be paid, but rather that *if* a defective substitute check has been paid, then it should be subject to the **same** consumer rights, perhaps other than legal equivalence, which attach to a non-defective substitute check. We suggest that this section of the rule be augmented to state that paid items which would be substitute checks if not for defects other than a MICR line error are **also** substitute checks for purposes of Sections 229.52- 229.57.

The rule also should clarify that if the reason that the substitute check is defective is the absence of the “legal equivalence” legend, but the defective substitute check has been paid, then state law consumer rights and remedies apply to the same extent as if the check **were** a substitute check, at least for all purposes except legal equivalence. Without such a rule, consumers could be in the odd position of having substitute check rights with respect to a **paid** but defective substitute check, but **not** ordinary state law check warranties with respect to that same paid check. This conundrum is created because state law uses the term “check” and since a defective substitute check is not legally equivalent to a check, state **law** rights can’t attach to it even though it has been paid.

There should be a copy of both the original check and the original source document for creation of a substitute check somewhere in the banking system.

State **law** requires that a copy of the original check be retained for seven years. Because a substitute check can be created either from an original check or from a previously truncated check, it seems that there will be instances where there will be no one in the payments system who has an obligation to retain a **copy** of the source document from which the substitute check **was** created. There **will** be some instances where the substitute check or a better copy of the substitute check is insufficient to resolve a dispute. Consumers might well ask for a **copy** of the document from which the substitute check **was** first created. When that document is the original check, state law already provides that at least a copy be retained, but when that source document *is* not the original check, the proposed rule includes no requirement that anyone retain a copy of that source document.

Under electronic **check** conversion, one of the most common consumer questions Consumers Union has received is: “How could the merchant destroy my check? How do I prove the amount of my check after they have destroyed it?”

It appears that neither Check 21 nor state law would require anyone in the chain of payment to retain a copy of a source document, other than **an** original check, from which the substitute check is created. State Uniform Commercial Code law requires retention only of a legible copy of the original paper check. Under the “legal equivalence” rule in Check 21, that requirement would be satisfied by retaining a copy of the substitute check. However, there appears to be **no** obligation in current state law, and no obligation stated directly in Check 21, for any bank in the chain to retain a copy of **any** other kind of source document for a substitute check.

Consumers are highly likely to find this result unsatisfactory. It is one thing to tell consumers that they **will** no longer get the original checks back as a matter of course, it is quite another to tell consumers that the document from which the substitute check **was** created has been destroyed and no one in the payment chain has a copy of it.

Disclosures are not in a form the consumer may keep if they can be downloaded but not printed,

Comment 38 to section 229.2(ddd) states that a notice is in a form the customer may keep if “it can be downloaded *or* printed.” A printable notice is in a form that the consumer may keep. A form which is both downloadable and printable also should qualify. However, Comment 38 also defines a document as being in a form that the consumer **may** keep even that document can only be downloaded, but not printed, by the consumer. To avoid this problem, the commentary should be changed to refer to the notice in a form which “can be printed, or can be downloaded *and printed.*”

Specific requests by the Board for comment

Issue A: Treatment of generally applicable industry standards,

To the **maximum** extent possible, the commentary should identify the relevant industry standards. If several standards are appropriate, each should be mentioned. Members of the industry may be familiar with these, but the commentary should also be useful to consumers and their lawyers, who may attempt to determine whether the appropriate standard has been followed. Referencing the appropriate standard in the commentary may also **help** to reduce disputes about whether the proper standard has been used.

There *is* an important related issue. Generally applicable industry standards are used to determine the **size** of a substitute check. The commentary to Section 229.2(zz) should be augmented to point out that if industry standards develop in a way that makes a substitute check difficult for recipients to read or use, continued deference to those standards will defeat the purpose of the substitute check, which is supposed to be as usable to the consumer **as** the original paper check. The commentary should remind the banking industry that if industry standards develop in such a way that the substitute check **is** too small or otherwise lacks usability for individuals, the Board could exercise its regulatory power under Section 15 of the Act to determine that those standards are no longer the proper measure for the adequacy of a substitute check.

Issue B: Relation of Check 21 to other law.

The commentary should describe the various **ways** that a check can be processed electronically which are not Check 21 transactions at all, but instead are fully covered by federal Regulation E. This is **necessary** because how the check is processed electronically after leaving the consumer’s hands determines what **law** applies. Persons who know only that an original check **was** not returned may look to the Check 21 rule when they should be looking to the Regulation E

material on electronic check conversion. The commentary should describe and distinguish between these different types of transactions, and cross reference the electronic check conversion material.

The commentary should also describe the practical effect of legal equivalence for a person who has written a check and now needs proof of payment. The commentary should give examples where persons to whom the check was written must accept the substitute check as proof of payment, including such common examples as landlords, creditors, debt collectors and the Internal Revenue Service.

Issue C: Remotely-created consumer demand drafts.

The Board asks for comment on whether the UCC revisions addressing remotely-created consumer checks should be incorporated into Regulation CC. In general, we believe that this is a good idea. However, any incorporation of those rules into Regulation CC should make it clear that the effect of those rules is to shift the relative rights and responsibilities between the depository bank and the payor bank, not to reduce the rights of the consumer against the payor bank. While a depository bank may have a better ability than a paying bank to prevent certain kinds of fraudulent deposit items, the consumer must continue to have a remedy directly against his or her own bank for payment of any item not authorized by the consumer.

Conclusion

The Check 21 Act was adopted by Congress under the principle that enhanced efficiency could be introduced into the banking system in a way that protects consumers. The substitute check and the associated rights of recredit, warranty, and indemnity are supposed to provide this protection. The proposed rule, draft commentary, and draft model notices need significant changes and additions to fulfill Congress' goal that the introduction of substitute checks be good for both banks and consumers.

Very truly yours,



Gail Hillebrand
Senior Attorney
Consumers Union
West Coast Regional Office
1535 Mission St.
San Francisco, CA 94103
415-431-6747 (phone)
415-431-0906 (fax)
hillga@consumer.org

Consumer Federation of America
1424 16th Street, NW Suite 604
Washington, DC 20036

U.S. PIRG
218 D Street, SE
Washington, DC 20003

National Consumer Law Center
1001 Connecticut Avenue, N.W., Suite 510
Washington, DC 20036

Consumer Action
717 Market St. Suite 310
San Francisco, CA 04103

Attachment One: Suggested changes to model notices

C-5A--Substitute Check Policy Disclosure Substitute Checks and Your Rights

Some or all of the checks that you receive **with** your account statement or by request may look different than the check you wrote. To make check processing easier, a federal law permits banks to replace original checks with "substitute checks." This notice describes substitute checks and the rights that you will have ~~when you receive~~ concerning substitute checks,

Where is My Original Check?

Under a new federal law effective October 28, 2004, your bank may not get your original check. The new law creates special kind of copy of your check, called a substitute check, that you can use just like you would use the original check. If you want a specific original check back, ask your bank for a substitute check. If you like getting all your original checks back, ask your bank to send substitute checks with your account statement. If you suffer a loss because you didn't get your original check back, you have a claim against your bank. You have other new rights which are described in this notice.

What Is a Substitute Check?

A substitute check is a copy of an original check that is the same as the original check for all purposes, including proving that you made a payment, if it includes an accurate copy of the front and back of the original check and contains the words; "This is a legal copy of your check, You can use it the same way you would use the original check." A substitute check that meets these requirements is generally subject to federal and state laws that apply to an original check. If you lose money because because a substitute check was charged to your account ~~you received a substitute check,~~ you have the right to ~~file a claim for~~ an expedited refund.

Your Right To File a Claim for an Expedited Refund

Federal law gives you the right to file a claim for an expedited refund if you ~~receive a substitute check and~~ believe that all of the statements below are true—

(1) The substitute check was incorrectly charged to your account (for example, this may be true if **we** charged your account for the wrong amount or if **we** charged your account more than once for the same check);

(2) You lost money **as** a result of the substitute check charge to your account; **and**

(3) You need the original check or a better copy of the original check to demonstrate that we incorrectly charged your account (for example, **this may be true if** you think that we charged your account for the wrong amount and the substitute check does not clearly show the amount).

Expedited Refunds

To obtain an expedited refund, **you must send us** make a claim. You may make an oral claim, but we can require that you submit certain information in writing after you make your claim. We cannot charge you a fee for your claim. Federal law limits an expedited refund to the amount of your loss, up to the amount of the substitute check, plus interest if your account earns interest. You should be aware that **you** could be entitled to additional amounts under other state or federal law, including this law.

How To Make a Claim for an Expedited Refund

Please **make** your claim [by calling (phone number), by writing to us at (address), or by e-mailing us at (address)]. You must **make** your claim within 40 calendar days of the later of these **two** dates:

(1) ~~The~~ date that **we** delivered the account statement showing the charge that you are disputing, or

(2) The date on which **we** made the substitute check available to you.

If there is a good reason (such as a long trip ~~or~~ a hospital stay) that you cannot **make** your claim by the required day, we ~~will~~ **must** give you additional time.

Your expedited refund claim must —

(1) Describe **why** you think the charge to your account was incorrect;

(2) Estimate how much money you have lost because of the substitute check charge;

(3) Explain **why** the substitute check is not sufficient to show whether or not the charge to your account **was** correct; and

(4) Provide us with a copy of the substitute check or give us information that will help us to identify the substitute check and investigate your claim (for example, the check number, ~~the name of the person to whom you wrote the check,~~ and the amount of the check).

Our Responsibilities for Handling Your Claim

We ~~will~~ **must** investigate your claim promptly. If we cannot **show** you that we correctly ~~conclude that we incorrectly~~ charged your account, we ~~will~~ **must** refund to your account the amount of your claim (**up to** the amount of the substitute check, plus interest if your account earns interest) within one business day of making that decision. If we ~~conclude~~ demonstrate that we correctly charged your account, we ~~will~~ **must** send you a notice that explains the reason for

our decision and includes either the original check or a better copy of the original check than the one you already received. If we **have** not made a decision on your claim within 10 business days after you submitted it, **we will must** refund the amount that we owe to your account, up to \$2,500, plus interest, **by** that date. We will refund the remaining amount, if any, plus interest, to your account by the 45th calendar day after you submitted your claim,

If **we** refund your account, on the next business day we will send you a notice that tells you the amount of your refund and the date on which you may withdraw that amount. Normally, you may withdraw your refund on the business day after we make it. In limited cases, **we may** delay your ability to withdraw up to the first \$2,500 of the refund until the earlier of these two dates: (1) The day after **we** determine that your claim **is** valid; or (2) the 45th calendar day after the day that you submitted your claim.

Reversal of Refund

We may reverse any refund that we have **given** you up to (time) if we later determine that the substitute check **was** correctly charged to your account. We also may reverse any interest we have paid you on that amount **if** your account earns interest. Within one business day after we reverse a refund, we **will must** send **you** the original check or a better copy of the original check than the one you previously received, explain to you **why** the substitute check was correctly charged to your account, and tell you the amount and date of the reversal.

Your Other Rights about the Substitute Check

You have the right to ask your bank for a substitute check. If a substitute check was used in processing your check, you also have a warranty right against your bank if the check was paid twice or was paid for the wrong amount. This new law also gives you rights if you are harmed because you can't get the original check.

* * * * *

The Checks You Write May Clear Faster

Because of this change in how checks are processed, the checks you write may clear faster. Do not write any check unless the funds are already in your account when you write the check.

26. In **appendix C**, after model C-21 add new models C-22 through C-25 to read as follows:

* * * * *

C-22--Expedited Recredit Claim, Pull Refund Notice Notice of Refund

~~We have determined that your claim that a substitute check was incorrectly charged to your account is valid. Your claim for a credit is granted. We are refunding (amount) [of which (amount) represents accrued interest] to your account. You may withdraw these funds as of~~

(date). [This refund **is** the amount in excess of the \$2,500 that **we** credited to your account on (date).] We can change our decision within days.

If within (time period), we later determine ~~that~~ the substitute check was correctly charged to your account, **we will** reverse the refund by charging your account. We will notify you within one day of any such reversal unless that day is on a weekend or a federal holiday.

C-23--Expedited Recredit Claim, Partial Refund Notice
Notice of Partial Refund

In response to your claim that a substitute check **was** incorrectly charged to your account, we are refunding (amount) [of which (amount) represents accrued interest] to your account, pending the completion of our investigation of your claim. You may withdraw these funds as of (date). [~~Unless we determine that your claim is not valid, the~~ We must credit the remaining amount of your refund will be credited to your account no later than the 45th calendar **day** after **you** submitted your claim unless we demonstrate that the check was properly charged to your account.]

If within (time period), we later determine rhar the substitute check **was** correctly charged to your account, we will reverse ~~the~~ refund by charging your account. We will notify you within one **day** of any such reversal unless that day is on a weekend or a federal holiday.

C-24--Expedited Recredit Claim, Denial Notice
Denial of Claim

We reviewed your claim that a substitute check **was** incorrectly charged to your account, **We arc** denying your claim. **As** the enclosed [(original check) or (copy of the original check)] shows, the charge to your account of (amount) **was** proper because (reason, e.g. amount charged is the **same** or the signature is authentic).

[**We** have also enclosed a copy of the other information we used to make our decision.]
[Upon your request, **we will** send you a copy of the other information that we used to make our decision. **There** is no fee for that information.]

C-25--Expedited Recredit Claim, Reversal Notice
Reversal of Refund

In response to your claim that a substitute check was incorrectly charged to your account, **we** provided a refund of (amount) by crediting your account on (date(s)). We now have determined that the substitute check was correctly charged to your account. We have reversed the refund. **As** the enclosed [(original check) or (copy of the original clieck)] shows, the charge to your account of (amount) was proper because (reason, e.g. amount charged **is** the same or the signature is authentic). **As** a result, we have reversed the refund to your account [plus interest we have paid you on that amount] by charging your account in the amount of (amount) on (date).

[We have also enclosed a copy of the other information we used to make our decision.]
[Upon your request, we will *sand* you a **copy** of the information we used to make our decision.]

Attachment Two: Descriptions of consumer organizations joining this letter

Consumers Union of U.S., Inc., is described in the footnote 1 to the comment letter.

The Consumer Federation of America is a non-profit association of 300 consumer groups, with a combined membership of more than 50 million people. **CFA** was founded in 1968 to advance the consumers' interest through advocacy and education.

The U.S. Public Interest Research Group (U.S. PIRG) serves as the national lobbying office for state Public Interest Research Groups. PIRGs are non-profit, non-partisan consumer and government reform organizations active in 37 states.

The National Consumer Law Center (NCLC) is a Massachusetts non-profit corporation established in 1969. NCLC provides assistance to legal services attorneys, governmental agencies, and private attorneys in advancing the interests of their low-income and elderly clients in the area of consumer law.

Consumer Action is a statewide consumer education and advocacy organization serving California consumers since it was founded in San Francisco in 1971. Consumer Action serves consumers nationwide by advancing consumer rights, referring consumers to complaint-handling agencies and publishing multilingual educational materials. Consumer Action also advocates for consumers in the media and before lawmakers and annually conducts comparison surveys for consumers on credit cards, banking issues and telecommunications issues-



Publisher of Consumer Reports

West Coast Regional Office
1535 Mission St.
San Francisco, CA 94103
415-431-6747

May 14, 2004

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

By electronic filing

Docket # R-1176, Check 21
Invited supplemental comments following May 3, 2004 MICR line meeting

These comments are filed by Consumers Union, the nonprofit publisher of *Consumer Reports*,¹ the Consumer Federation of America, U.S. PIRG, and Consumer Action.

These comments respond to the invitation extended by the Federal Reserve Board staff on May 3, 2004 for further comments related to the MICR line issue discussed at the public meeting held that day. Staff asked for additional comments by May 17, 2004.

At the public meeting, a number of banks and bank trade associations called for the Federal Reserve Board to expand the definition of a substitute check beyond, and in contravention of, the definition contained in Check 21. If such an such expansion were to be made, it would protect some consumers in some instances where a defective or incomplete substitute check has been paid, but it would also expose consumers generally to new risks that items which have less information than Congress contemplated for a substitute check would become legally equivalent to the original check, and thus chargeable to a consumer's account, when they otherwise could not have been properly charged to the consumer's account. This will broaden the universe of instances for which the consumer may need to resort to the right of recredit conferred by the Act.

If the Federal Reserve Board pursues any deviation from the statutory requirements for a substitute check, we ask that the following five principles be followed. These five principles are designed to minimize the potential for harm to consumers that a broader definition of "substitute

¹ Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide consumers with information, education and counsel about goods, services, health, and personal finance; and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life of consumers. Consumers Union's income is solely derived from the sale of *Consumer Reports*, its other publications and from noncommercial contributions, grants and fees. In addition to reports on Consumers Union's own product testing, *Consumer Reports* with approximately 4 million paid circulation, regularly carries articles on health, product safety, marketplace economics and legislative, judicial and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

check” could mean that incomplete and possibly inaccurate payment messages are more likely to enter or move in the payments system.

- Whenever payment has been made from the consumer’s account based upon a substitute check or an item or payment instruction that was created or transferred in the using a substitute check the payment should be treated as a substitute check after payment, even if the payment instruction did not meet the definition of a substitute check. A different approach would give fewer protections when a payment has been made based on disqualifying, incomplete information than when payment has been made based on fully qualifying, complete information.
- The right of recredit must be triggered by “use” of substitute check, whether or not that substitute check was also provided to the consumer. Any modification in the definition of a substitute check to excuse compliance with an element required by Congress makes the substitute check less complete than contemplated by Congress, increasing the importance of free and easy access to the right of recredit.
- All breaches of warranty must trigger access to the right of recredit, when that right is otherwise available under the statute (*i.e.* a substitute check is used).
- The possibility that the regulations will recognize as substitute checks items not meeting the statutory definition makes it particularly important that the regulations guarantee consumers the right to a substitute check on request.
- A substitute check meeting the full statutory definition, not a broader category of items which might be defined by the Federal Reserve Board as included within the term “substitute check,” should be the only type of substitute check which can be produced in lieu of the original check or a copy of the original check to eliminate a warranty claim under section 6.

1. Items which were paid because they were presented somewhere in the payments chain as actual or apparent substitute checks should be treated as substitute checks after they have been paid.

There are significant pros and cons for consumers of a loosened definition of substitute checks, because such a definition will authorize payment from the consumer’s account based on items that are less complete than Congress contemplated when it defined a substitute check. Once an item has been paid, however, denying the existence of a substitute check because the item was defective would deny the consumer whose account has been debited with the protections provided by Check 21. Wherever the line is drawn for how close to meeting the statutory definition something must be to qualify as a substitute check, when a substitute check or payment information from a substitute check was transferred in the payment stream and has been paid, the regulations should either:

- 1) retain the concept of a purported substitute check and apply that concept to the paid item; or

2) include the paid item in the definition of a substitute check, for purposes of the warranty and recredit rights, even if it is not considered to be within that definition for all other purposes.

For consumers, the key protection is the right of recredit when a substitute check "was not properly charged to the consumer's account" or "the consumer has a warranty claim." To eliminate application of this protection when the reason that the consumer's account was charged is that a bank in the payment chain used a document that it erred in thinking qualified as a substitute check would turn these protections upside down. Thus, regardless of how the definition is applied before items are paid, if an item has been paid relying on a defective or incomplete substitute check, the regulations should either retain the purported substitute check concept or should include that item in the definition of a substitute check for purposes of warranty and recredit, and for the purpose of triggering, but not of satisfying, the indemnity obligation.

2. The right of recredit must be triggered by "use" of substitute check, whether or not that substitute check was also provided to the consumer.

Any modification in the definition to excuse compliance with the Congressional requirement that a substitute check bear the full MICR line of the original check means that the substitute check will be less complete than contemplated by Congress, making access to the right of recredit of greater importance. Because any expansion beyond the statutory definition of a substitute check enhances the risk that defective or incomplete items will be paid, the statutory remedy for payment of an item not properly charged to the consumer's account must be easy to access. For this reason, the regulation should be modified to allow access to the right of recredit when a substitute check or information from a substitute check was used in the processing of the payment *or* was provided to the consumer. If the right of recredit is easily accessible, and not limited to persons who were provided with the substitute check, this should help to ameliorate the risk to consumers of an improper charge to the consumer's account due to a defect in a substitute check that would not meet the statutory definition, but might meet some broadened definition adopted by the Federal Reserve Board by regulation.

3. All breaches of warranty must trigger access to the right of recredit, when that right is otherwise available under the statute (*i.e.* a substitute check is used).

Because any expansion beyond the statutory definition of a substitute check enhances the risk that defective or incomplete items will be paid, the statutory remedy of recredit when an item not properly charged to the consumer's account has been paid, or when there has been a breach of warranty, must be broadly construed.

Some of the bank comments to the proposed rule seek to narrow the right of recredit solely to breach of Check 21 warranties. The statute does not support such a narrow interpretation. Section 7(a)(1)(B)(ii) permits recredit when the consumer "has a warranty claim with respect to the substitute check," without restriction as to whether that warranty claim arises under the UCC or Check 21. A narrower interpretation of the right of recredit would be particularly inconsistent with a broadening of the items which qualify under the definition of a substitute check, since broadening that definition would permit more items to be charged to the consumer's account. If

one of those items goes awry under either the UCC warranties or the Check 21 warranties, the consumer has the same need for recredit.

The possibility that incomplete items will meet the definition of a substitute check under a regulatory definition that is weaker than the statutory definition makes this of special importance, because those items will be conferred legal equivalent status that they otherwise would lack if they are treated as a substitute check. This is true whether the warranty which has allegedly been breached is a UCC warranty such as the warranty that the item is properly payable or the encoding warranty, or is a Check 21 warranty such as the warranty of legal equivalence or the no double debit warranty.

4. If less-than-complete items will qualify as meeting the definition of a substitute check, this heightens the importance for consumers of a right guaranteed by the regulation to receive a substitute check on request.

Consumers need a way to see what was charged to their accounts. If the substitute check definition is to include items less complete than those defined by Congress to be substitute checks, then it becomes even more important that the regulation be amended guarantee consumers a right to receive a copy of the substitute check, on request. However, if less than complete items will qualify as substitute checks, then the consumer and law enforcement may also need a right to the original check or a copy of the original check, something which is also not guaranteed by the proposed regulations.

5. An additional change would be needed to prevent an item falling under a too-broad definition of "substitute check" from serving as the type of substitute check that eliminates an indemnity claim under section 6.

The final problem with any expanded definition is that a substitute check is the type of copy of an original check which eliminates an indemnity claim for harm due to non-receipt of the original check. The statute eliminates the indemnity claim when the indemnifying bank "produces the original check or a copy of the original check (including an image or a substitute check) that accurately represents all of the information on the front and back of the original check (as of the time the original check was truncated) or is otherwise sufficiently to determine whether or not a claim is valid..." The key here is that an item meeting an expanded definition of a substitute check should not automatically be a document that eliminates the indemnity.

To address this, two clarifications should be made. First, if the definition of "substitute check" is broadened, then the regulations under section 6 should be clarified to emphasize that the mere production of a (more broadly defined) substitute check does not necessarily eliminate the indemnity claim. Instead, in addition to being a substitute check, the copy which can be effective to eliminate the indemnity claim must meet the additional statutory requirement that it: "accurately represents all of the information on the front and back of the original check (as of the time the original check was truncated) or is otherwise sufficient to determine whether or not a claim is valid..." The regulation should clarify that mere status as a substitute check does not necessarily meet this part of the test for a copy to eliminate an indemnity claim.

Second, any expanded definition of what can qualify as a substitute check makes it more important that the determination of what kind of copy is "otherwise sufficient to determine whether or not a claim is valid..." should be judged by, or at least from the perspective of, the consumer, not the bank. The proposed regulations are silent on this point, and should be changed.

Without these two clarifications, a broader definition of substitute check is likely to have the unintended effect of allowing a bank to circumvent indemnity liability in circumstances where Congress intended to impose it, because the copy provided to the consumer qualifies as a substitute check under the broadened definition but would not have qualified under the statutory definition.

Conclusion

The Check 21 Act was adopted by Congress under the principle and the promise that enhanced efficiency could be introduced into the banking system in a way that protects consumers. The substitute check and the associated rights or recredit, warranty, and indemnity are supposed to provide this protection. While maintaining ongoing objections to the Act itself, consumer groups supported the "purported substitute check" approach in the proposal regulations. The change proposed by the banking industry to replace this concept with an expanded definition of a substitute check beyond a document that bears the original MICR line protects consumers with respect to an item that has already been paid, but exposes consumers to new risks that an incomplete or inappropriate item will qualify as a legally equivalent and properly changeable item; that is, a substitute check. If this approach is proposed, it must be accomplished in a way that satisfies the five principles outlined above, particularly by providing broad and simple access for consumers to the right of recredit.

Very truly yours,

Gail Hillebrand
Senior Attorney
Consumers Union
West Coast Regional Office
1535 Mission St.
San Francisco, CA 94103
415-431-6747 (phone)
415-431-0906 (fax)
hillga@consumer.org

Ed Mierzwinski
U.S. PIRG
218 D Street, SE
Washington, DC 20003

Jean Ann Fox
Consumer Federation of America
1424 16th Street, NW, Suite 604
Washington, DC 20036

Ken McEldowney
Consumer Action
717 Market St. Suite 310
San Francisco, CA 94103