

March 12, 2004

Ms. Jennifer J. Johnson, Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> and C Streets, N.W.  
Washington DC 20551

Re: Comments to Proposed Amendments To Regulation CC  
Docket No.: R-1176

Dear Ms. Johnson:

KeyBank NA appreciates the opportunity to comment on the proposed regulations to Reg. CC implementing the Check Clearing in the Twenty First Century Act. We feel that this legislation and its accompanying regulations are critical to providing a secure, modern and efficient payments system, and will be beneficial to consumers, companies and financial institutions of all sizes if properly implemented.

### **About KeyCorp**

Cleveland-based KeyCorp is one of the nation's largest bank-based financial services companies, with assets of approximately \$84 billion. Key companies provide investment management, retail and commercial banking, consumer finance, and investment banking products and services to individuals and companies throughout the United States and, for certain businesses, internationally. The company's businesses deliver their products and services through branches and offices and a network of approximately 2,200 ATMs.

### **General Comments**

KeyBank has also co-signed letters from joint comments from The Financial Services Industry group, ECCHO (the Electronic Check Clearing House Organization), and SVPCo (the Small Value Payments Company) and urge you to carefully consider the various comments which make up these opinions.

In addition to our specific comments listed below, we wish to strongly reiterate our belief that for Check 21 to have the effect that was desired by Congress and the President in passing and signing the legislation it is crucial that substitute checks be accepted as a safe, secure, reliable and final payment method. The interest of our customers, both consumer and business, will be best served if the needs of both those making payments and those receiving those payments are protected. Our customers have a right to expect that their payments will be accepted without undue complications as well as to expect that these items will be debited correctly against their accounts.

We feel that the concept of a ‘purported substitute check’ is the greatest deficiency in the proposed regulations. If substitute checks do not keep their legal validity as an enforceable payments instrument throughout the payment system their acceptance in the marketplace will never be assured. We feel that the indemnities and warranties inherent in the legislation provide ample protection to the consumer, and that there is no need for the ‘purported substitute check’ category to be recognized. Creating this legally ambiguous instrument, which can shift its legal status throughout the collection stream, depending on how it is handled or mishandled, will only create uncertainty and confusion.

Aside from our general concerns about the regulations, our specific comments follow:

### **Purported Substitute Checks**

The Act requires that, in order for a document to meet the requirements of the definition of a “substitute check”, the check must, among other requirements, (i) bear a MICR line with the MICR information from the original check, and (ii) be suitable for automated processing in the same manner as the original check. Section 229.51(c) of the Proposal provides that if a bank transfers and receives consideration for an item that meets all the requirements of a substitute check except for the MICR line requirement in Section 229.2(zz)(2), that the item is a substitute check for purposes of the expedited recredit, indemnity and warranty provision of the regulation. However, Section 229.51(c) provides that such an item is not a legal equivalent of the original check. We believe that Section 229.51(c) raises two related issues regarding MICR lines on substitute checks. These two issues are discussed below.

#### **A. Remove Section 229.51(c) from Final Regulation**

We believe that this Section 229.51(c) should be deleted in its entirety from the final regulation. As discussed in the prior section, there is no reason why an item that otherwise meets the requirements for a substitute check, but contains incorrect MICR encoding, should not have legal equivalency to the original check. Given receiving banks’ and customers’ potential lack of knowledge of an imperfect MICR line on a substitute check, it does not seem appropriate to “punish” receivers of a substitute check by denying the substitute check “legal equivalency” because the MICR line on the substitute check fails to accurately represent the MICR line on the original check. The warranty and indemnity provisions under the Check 21 Act would protect banks and customers that receive such a substitute check, to the extent that any loss arises from the incorrect MICR encoding.

Accordingly, we request that the Purported Substitute Check provision of the Proposal be deleted in its entirety in the final rule. The final rule should instead include the provisions, discussed in the prior section, regarding the legal equivalency of a substitute check, notwithstanding incorrect or altered MICR line information.

#### **B. Creation Of A Substitute Check Without MICR Ink By Paying Bank**

We request the final rule include a new provision that expressly authorizes a paying bank to create a substitute check without printing the MICR line information in MICR ink. Substitute checks that are paid and canceled by the paying bank, and are being delivered by the paying bank to its drawer customers, do not need to be printed in MICR ink. These substitute checks will not be further processed on an automated basis, either on a forward collection or return basis. Accordingly, it is not reasonable to require a paying bank to incur the cost of using MICR ink to create this class of substitute checks. From a customer's point of view, it should not matter whether the MICR line is printed in MICR ink. We do not believe that receiving a paid substitute check that is not MICR-encoded would disadvantage a customer. Since customers do not use MICR line readers, and can visually read all the information on the substitute check, including the information contained in the MICR line, there is no detriment to customers by receiving a non-MICR ink substitute check.

By authorizing non-MICR ink substitute checks in the final rule, the Federal Reserve will further the purposes of the Act to facilitate check truncation and improve the efficiency of the Nation's payments system. It is generally anticipated that it will be less expensive to print a non-MICR substitute check, and therefore paying banks can produce non-MICR substitute checks on a cost-effective basis to reach those customers who have not agreed to receive images of their checks or those customers that require a sufficient copy, as defined in 229.2 (aaa) and the respective commentary. With this lower cost capability, paying banks will be more willing to enter into arrangements with other banks to exchange check image only files, instead of exchanging a mix of paper checks and check images. This will allow depository and collecting banks to image a greater number of checks much earlier in the check collection process. We propose the below Rule text to implement the above position.

*Suggested Regulatory Text:*

“Exemption From Requirement to MICR Encode Substitute Checks: A paying bank may at its option print the MICR line information from the original check on a substitute check with non-MICR ink, and such substitute check does not otherwise need to be suitable for automated processing in the same manner as the original check, provided: (i) the check has been paid by the bank and will not be further processed on an automated basis through the forward or return bank check collection process, (ii) the paying bank is the reconverting bank and is delivering the substitute check to its own customer, for the customer's personal use; (iii) the information from the MICR line on the original check is printed in non-MICR ink and in MICR font on the substitute check in the same location as on the original check; and (iv) the paying bank otherwise complies with the requirements for substitute checks under the Act. In this situation, this substitute check without MICR ink would be deemed to satisfy the requirements of a “substitute check” for all purposes under the Act and this regulation.”

## **Expedited Recredit in Writing**

Proposed section 229.54 (b) (3) Form and submission of claim: computation of time clarifies that a bank that requires a consumer to submit an expedited recredit claim in writing must compute the time period for acting on the claim from the date that the consumer submitted the written claim, even if the consumer previously provided some information relating to the claim in another form. Proposed § 229.54(c) provides that “banking day” (instead of “business day” under Check 21) is to be used to begin measuring the time period for a bank’s action.

Comment: We agree that a bank’s time period for acting on a consumer’s expedited recredit claim should be computed from the date that the consumer submitted the written claim even if the consumer previously provided information regarding the claim in another form. We also agree that “banking day” should be used to begin measuring the time period for a bank’s action. We recommend that the written request for recredit be in a paper writing delivered to an address specified in the consumer awareness disclosure to ensure that it receives timely and accurate attention. We feel that this provision will benefit both consumers and financial institutions because the tight timeframes under Check 21 will require specialized staff that is trained in the intricacies of the law.

## **Model Consumer Education**

KeyBank feels that a briefer, clearer, and more concise consumer education language would be in the best interest of our customers. Lengthy complex language may not be read or may be misunderstood by our customers. The Federal Reserve should allow banks to publish a much shorter document with instructions on how to receive more detailed information. This shorter document would better serve our customers need to be informed, as long as additional detailed information was available for those who felt that it was warranted.

## **Remotely Created Demand Drafts**

KeyBank supports the concept of bringing these instruments under the coverage of Reg. CC and encourages the Federal Reserve to submit appropriate regulations for comment as soon as feasible. Our customers need to have warranty protection and the certainty that unauthorized demand drafts cannot be charged against their accounts, which only national regulations can create.

## **Education of the Legal Profession**

Although no comment was requested on this subject, KeyBank urges the Federal Government (either via the Federal Reserve or the OCC) to initiate a program to educate Federal, State and Local legal professionals as well as law enforcement agencies on the ramifications of Check 21 and its implementing regulation. Many of these professionals

may not receive the consumer education because they may not receive check enclosed bank statements. Our customers need to be confident that if they are involved in a legal dispute where a substitute check is part of the facts in the case they will not be disadvantaged by a misunderstanding relating to Check 21 or the revisions to Reg. CC. Specific legal education needs to be distributed to Judges, Prosecutors and other legal organizations explaining Check 21 and the changes to Reg. CC until sufficient time has passed for legal precedent to be established throughout the various jurisdictions. Only a uniform national approach to this problem can ensure that consumers and businesses will not be unduly burdened by any confusion or misinterpretation when this law takes effect in October 2004.

### **The Need for Timely Completion**

Finally, KeyBank wishes to thank the Federal Reserve Board for their instrumental role in the creation, passage, and implementation of Check 21. We strongly support these efforts to make our payment system safer and more modern. We urge that the Board not only carefully consider the comments of all payments system participants, but also act quickly in finalizing the implementing regulations. In order for financial institutions to be prepared to comply with this law and its accompanying regulations, much work needs to be completed. Releasing complete and considered regulations in an expeditious manner will be critical for a successful implementation on October 28<sup>th</sup> 2004.

Sincerely,

Michael P. Barnum  
Executive Vice President of Client Services