



March 11, 2004

Via E-Mail -regs.comments@federalreserve.gov

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

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

Dear Ms. Johnson:

The Electronic Check Clearing House Organization (“ECCHO”) is a not-for-profit national clearinghouse dedicated to promoting electronic check collection and related payment system improvements. Membership in ECCHO is available to any depository institution, as defined by the Federal Reserve Act, and various membership classes are available to serve banks from the very smallest to the very largest. ECCHO’s current membership consists of approximately 20 banks from across the United States representing approximately 60% of the total deposits of the nation’s banks.¹

ECCHO is pleased to provide the Federal Reserve Board (the “Board”) with comments to the proposed regulation (the “Proposal”) to amend Regulation CC to implement the Check Clearing for the 21st Century Act (the “Check 21 Act”). ECCHO has also worked with other financial services organizations and associations to prepare a separate joint comment letter to the Board on the Proposal. ECCHO has not restated the comments from the joint comment letter in this letter and strongly supports all of the comments on the Proposal that are made in the joint comment letter.

Comments to Specific Sections of the Proposal

1. Section 229.2(z) -- Definition of “Paying Bank”

The Proposal provides that a “Paying Bank” includes the Treasury of the United States and the U.S. Postal Service with respect to a check payable by that entity and sent to that entity for payment or collection. This definition varies from the Act. The Act defines a “bank” to include the Treasury of the United States and the U.S. Postal Service “to the extent it acts as a payor.” See Section 3(2) of the Act. There is no requirement under the Act that the Treasury check or Postal money order be “sent to that entity for

¹ The views expressed in this letter do not necessarily reflect the views of each ECCHO member bank. Many of the ECCHO member banks may be submitting their own comments on this Regulation CC proposal.

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payment or collection.” Accordingly, it is not clear what the “sent for payment or collection” requirement is supposed to add to the definition of paying bank with respect to the Treasury and the Postal Service. We are concerned that this definition in the regulation could be read to exclude certain classes of Treasury checks and Postal Service money orders that are not sent directly to the Treasury or Postal Service for payment and collection. For example, it is not clear how Treasury checks sent to the Federal Reserve Banks for payment would be treated under this definition.

To avoid uncertainty on this issue, we recommend that the final rule revise the definition of “paying bank” to provide that a paying bank includes the Treasury of the United States and the U.S. Postal Service “for a check that is payable by that entity or that is sent to that entity for payment or collection.”

2. Section 229.2(aaa) -- Definition of Sufficient Copy

The Proposal includes a new definition of “sufficient copy” to address situations where another substitute check or a copy of the substitute check must be provided to the customer or a claimant bank in the context of a warranty claim or an expedited recredit claim. We support the general concept behind this definition as providing clarity and consistency to the implementation of the Act.

We are concerned, however, with how this definition appears to treat the delivery of “electronic check images” to customers. The Proposal provides that an electronic check image is not a “sufficient copy” unless it is a “paper print out” of that check image. This is reflected both in the definition of a sufficient copy itself and in the Commentary on electronic delivery generally. See Section 229.2(aa) and Commentary Section 229.2(aa)-2.

While it is unclear exactly how this text would be applied, it is possible that this definition of “sufficient copy” could require that the customer print out the check image before the image is deemed a “sufficient copy.” Such a restrictive interpretation would cause significant technological and operational problems for banks that seek to use electronic communications to communicate with their customers regarding checking account inquiries. In particular, based on current email technology, a bank will never know whether or when a customer prints an electronic check image that the bank sends to the customer. As a result, the bank will not be able to transmit electronic check images to customers to satisfy a customer inquiry regarding a substitute check. This will impose a burden on banks and deny customers the advantages of the fast and reliable responses provided by electronic communications.

We recommend that the final rule clarify that an electronic check image comes within the definition of “sufficient copy” if the recipient has agreed to accept such a copy of the original check electronically, regardless of whether or when the recipient prints out the electronic check image on paper. This recommendation for the treatment of electronic check images is consistent with the treatment under the Proposal of electronic communications generally in Section 229.58 of the Proposal. It also would be consistent

with the use of electronic communications for required disclosures under other consumer regulations administered by the Federal Reserve, such as Regulation E and Regulation Z.

3. Section 229.35(a) -- Liability for Indorsements

Section 229.35(a) of the Proposal states that a bank (other than a paying bank) must indorse a check "in a manner that enables a subsequent collecting bank, paying bank, or returning bank to interpret the indorsement."

We believe that the final rule should clarify that a bank is not responsible if its indorsement (placed on the check in compliance with all applicable requirements) is obscured by a subsequent endorser or by some other person in the check collection process. Assuming a bank places its indorsement in the proper location on the check, it is not possible for the bank to prevent a party subsequent in the check collection process from obscuring its indorsement.

4. Section 229.51(b)(2) and (3) -- Indorsement Location

Section 229.51(b) of the Proposal and Appendix D(3) set forth detailed requirements for the indorsement location of both the reconvertng bank and the truncating bank on a substitute check. The Proposal would require that a reconvertng bank print the truncating bank's 9-digit routing number (without arrows) and a bracket at each end of the number, on the front of the check, between 2.10 and 2.50 inches from the trailing edge of the check and within 2.6 inches from the top of the check. The Proposal also would require that a reconvertng bank print the reconvertng bank's 9-digit routing number (without arrows) and an asterisk at each end of the number, on the front of the check, between .25 and 2.10 inches from the trailing edge of the check and within 0.575 inches from the top of the check.

While the Proposal's requirement for identifying the truncating bank and the reconvertng bank would generally conform with the current industry standard, we do not believe it is appropriate to provide this level of technical requirements in the regulation itself. Rather, the final rule should only require the identification of the truncating bank and the reconvertng bank on the substitute check, and leave the technical details for the manner and location of the bank identifications up to generally applicable industry standards. This approach will give the financial services industry the flexibility to develop and modify over time the requirements for truncating bank and reconvertng bank identification.

5. Section 229.52(a) -- Duplicate Payment Warranty

The Commentary to Section 229.52(a) of the Proposal states that a reconvertng bank is potentially responsible for a breach of a duplicate payment warranty, even if the demand for duplicate payment results from a fraudulent substitute check about which the warranting bank had no knowledge. See Commentary Section 229.52(a)-5. This situation could arise, for example, when a fraudster uses a second bank to send a

duplicate check or substitute check for collection, and the first reconverting bank has had no involvement with the creation or collection of the fraudulent substitute check.

We believe that the final rule should recognize that the loss arising from such a situation should ultimately be transferred to the depository bank that took the duplicate check or substitute check for deposit from the fraudster. The bank that dealt with the fraudster is the appropriate bank to bear the ultimate liability arising from the breach of the duplicate payment warranty because that bank is best positioned to reclaim the funds arising from the second check or to prevent such frauds from occurring in the first place.

To place the liability on the bank that dealt with the fraudster that created the unauthorized second check or substitute check, we recommend that the final rule either: (i) provide that the Section 229.52(a) warranty does not apply in this situation and that the recipient has a cause of action against the depository bank that submitted the fraudulent check into the check collection system, or (ii) provides that the first warranting bank that pays a warranty claim in these circumstances may bring a cause of action (such as through subrogation to the rights of the paying bank) against that second depository bank that dealt with the fraudster and was responsible for the second check being presented against the account.

6. Section 229.53(a) -- Scope of Indemnity

The Check 21 Act provides that the indemnity under Section 6 of the Act runs to recipients of substitute checks, and not to recipients of paper or electronic forms of the substitute check. By comparison, the warranties made with respect to a substitute check under Section 5 of the Act travel with the substitute check and any subsequent electronic or paper forms of the substitute check or the original check. This is an important distinction between the scope of the warranties and the indemnities. Accordingly, we believe that the Commentary in Section 229.53 of the Proposal should clearly state this important limitation on the scope of the indemnity. A clear statement to this point in the Commentary will assist users of the regulation in understanding how the warranty and indemnity provisions interrelate.

Suggested Commentary Text:

“Section 229.53(a). Limitation of Application of Indemnities. Unlike the warranties, the indemnity is not provided to a person who received a paper or electronic representation of the substitute check, rather than the substitute check itself. For example, where the depository bank transfers a substitute check to a collecting bank and that collecting bank, pursuant to its agreement with the paying bank, transmits an electronic representation of that substitute check to the paying bank, the indemnity is provided to the collecting bank but not to the paying bank or the drawer.”

7. Section 229.53(a) -- Losses Covered By Indemnity

The Act provides that the indemnity covers a loss if that loss occurred “due to” the receipt of a substitute check instead of the original check. However, the Proposal provides that a loss is covered by the indemnity if the loss was “ultimately traceable” to the receipt of a substitute check instead of the original check. See Commentary Section 229.53(a)-2. We are not sure what is meant by the inclusion of the phrase “ultimately traceable,” and how it could be interpreted as being different than the “due to” standard in the Act itself. There is the potential that the “ultimately traceable” standard could be viewed as somewhat broader than the “due to” standard.

A related issue arises in Commentary Section 229.53(a)-2a which states that a loss is covered under the indemnity if the paying bank would have inspected the original check for security features and “likely” would have detected the fraud and returned the original check before its midnight deadline. Similarly, Commentary Section 229.53(b)-1a provides that the drawer could assert an indemnity claim if the bank “likely” would not have charged the drawer’s account had the original check been presented instead of the purported substitute check. Finally, Commentary Section 229.53-2b provides that the paying bank could have an indemnity claim if it “likely” would have returned the check by its midnight deadline had it received the original check. Again, it is unclear why different terminology is used in these Commentary sections to describe the scope of losses covered under the indemnity.

Accordingly, we request that the above referenced Commentary sections in the final rule be revised to conform to the standards for the scope of losses covered under the indemnity as set forth in Act.

Suggested Commentary Text:

Section 229.53(a)-2

“2.....The indemnity would not, however, cover a loss that was not *due to* the receipt of a substitute check instead of the original check.” [New text in italics].

Suggested Commentary Text

Section 229.53(a)-2a

“2a.....The amount and other characteristics of the original cashier’s check are such that, had the original check been presented instead, the paying bank would have inspected the original check for security features and [~~likely~~] would have detected the fraud and returned the original check before its midnight deadline.” [Deleted text in overstrike].

Suggested Commentary Text

Section 229.53(b)-1a

“1a..... The drawer also could assert an indemnity claim, because if the original check had been presented instead of the substitute check, the bank [~~likely~~] would not have charged the drawer’s account.” [Deleted text in overstrike].

Suggested Commentary Text

Section 229.53-2b

“b. As described more fully in the commentary to § 229.53(a) regarding the scope of the indemnity, a paying bank could have an indemnity claim if it paid a legally equivalent substitute check that was created from a fraudulent cashier’s check that the paying bank [~~likely~~] would have returned by its midnight deadline had it received the original check.” [Deleted text in overstrike].

8. Section 229.53 -- Bank Responsibility for Indemnity Claims

The Commentary to Section 229.53 of the Proposal provides examples of situations where a bank is responsible for the loss to a drawer customer arising from receipt of a substitute check. For example, the Commentary provides that if the drawer suffered a loss because it could not prove a forgery based on the substitute check, because proving the forgery required analysis of pen pressure that could be determined only from the original check, the drawer would have an indemnity claim. Commentary 229.53(b)-2a.

We believe that it would be appropriate if the Commentary in the final rule also included examples of when a bank may deny a consumer’s claim that a fraud loss allegedly was incurred as a result of non-receipt of the original check. For example, the Commentary could state that a bank can deny a consumer’s claim that he or she needed the original check to prove a fraudulent drawer’s signature on the check if the bank has information, from the substitute check itself or from other sources, that indicates that the check was authorized by the consumer and is not fraudulent.

Suggested Commentary Text:

“Section 229.53. Notwithstanding a customer’s claim that he or she needs the original check to prove a fraudulent drawer’s signature, a bank may deny a claim from the drawer customer without providing the original check to the customer if the bank can conclude, based on information from the substitute check itself or from other sources, that the check was authorized by the customer. For example, if the bank can show that the check was deposited into an account controlled by the customer or the check was paid to a credit card company in payment of the customer’s credit card account.”

9. Section 229.54(b) -- Expedited Recredit Claim In Writing

Under Section 7(b)(2) of the Act, a bank may require that a consumer put an expedited recredit claim in writing. Commentary Section 229.54(b)-7 of the Proposal

provides examples of how a bank could inform the consumer of this writing requirement for expedited recredit claims. The two example options in the Proposal are: (i) placing the writing requirement in the consumer awareness notice, or (ii) if the consumer attempts to make a claim orally, by informing the consumer at that time of this requirement. Commentary 229.54(b)-7.

While we support the two notice options provided in the Proposal, we recommend that the final rule also include as an example the bank providing this information to the consumer in the deposit account agreement or other account disclosures provided to the consumer. Banks should have the flexibility of including the writing requirement for expedited recredit claims in any checking account related agreement or disclosure.

10. Section 229.54(a)(3) -- Determination Of Invalidity Of Claim

The Commentary to Section 229.54(a)(3) of the Proposal provides examples of scenarios that would support a consumer's claim for expedited recredit. For example, a consumer is entitled to recredit when the consumer receives a substitute check and believes that he or she wrote the check for \$150 but the bank charged his or her account for \$1,500. However, the Proposal provides no examples for the bank to use for determining that the consumer's claim is not valid.

We recommend that the Commentary in the final rule include examples of situations where a bank may determine that the consumer's expedited recredit claim is not valid. These examples could parallel the examples provided in the Commentary for consumer expedited recredit claims. These examples would be very useful to banks as they implement this entirely new expedited recredit process.

Suggested Commentary Text

Section 229.54(a)-3

“Examples. A consumer would not meet the requirements for the expedited recredit in the following situations:

1. A consumer who received a substitute check can determine from the image that the payee line on the check has been altered and made payable to a different payee than the payee that was originally indicated. Because the consumer can determine the altered payee from the image in the substitute check, the consumer could not attempt to recover his or her losses by using the expedited recredit procedure.

2. A consumer who received a substitute check can determine from the image that the dollar amount on the substitute check is different from the dollar amount that was charged to the consumer's account. Because the amount of the check can be determined from the image in the substitute check, the consumer could not attempt to recover his or her losses by using the expedited recredit procedure.”

11. Section 229.54(c)(4) -- Reversal of Interest

The Federal Reserve requests comment in the Proposal as to whether interest earned on funds credited to an account as part of an expedited recredit should be reversed when the recredit is also reversed. The Check 21 Act does not explicitly address reversal of earned interest when reversing an expedited recredit.

We support the final rule permitting the reversal of the amount of any interest recredited to the account as part of an expedited recredit or interest earned in the account on the amount of the expedited recredit prior to reversal. A bank should be permitted to reverse interest in both cases to avoid unjust enrichment of the customer. We suggest a change to the current Commentary text to clarify a financial institution's authority to reverse interest earned on the recredited amount.

Suggested Commentary Text:

Section 229.54(c)

"2. A bank that provides a recredit to the consumer, either provisionally or after determining that the consumer's claim is valid, may reverse the amount of the recredit if the bank at any time later determines that the claim in fact was not valid. A bank that reverses a recredit also may reverse the amount of any interest that it has paid, *either at the time of the recredit or while the recredit was in the consumer's account*, on the previously recredited amount." [New text in italics]

12. Interest Recovery on Inter-Bank Claims

Under Section 8 of the Check 21 Act and Section 229.55(c)(1) of the Proposal, a claimant bank may seek to recover from a warranting bank both the amount of the check and interest, if applicable. While we support the concept of the claimant bank receiving interest on the amount of a claim, we believe that, for processing efficiency and predictability of interbank claims, the interest on the amount of the claim should be based on the standard interest calculation formulas that banks use today for handling adjustments, rather than on the amount of interest that the claimant bank paid to its customer. Given banks' substantial experience and procedures in calculating interest on traditional interbank check claims, it does not make sense for the Proposal to mandate a different rule for interest calculation on a subset of interbank check claims. This is particularly true given that it is anticipated that interbank claims for recredit under the Check 21 Act will be handled as part of the standard bank adjustment process.

In this regard, we recommend that the final rule provide that a warranting bank's liability to a claimant bank for interest under Section 8 of the Act and Section 229.55 of the final rule be based on the interest calculation formulas set forth in the guidelines established by the National Council for Uniform Interest Compensation.

13. Section 229.54(d) -- Availability of Interest

Section 7(d) of the Act permits a bank to delay availability of an expedited recredit in certain circumstances. The amount of the recredit includes both the amount of a substitute check and any lost interest, if the account is interest bearing. We recommend that Commentary Section 229.54(d)-1 reference interest, as well as the first \$2,500 that it provisionally credits to the consumer's account, in its discussion of what can be subject to delayed availability in the specified circumstances. This will clarify that a bank can delay recredit of interest as well as the amount of the check.

Suggested Commentary Text:

Section. 229.54(d)

"1.However, a bank may delay the availability of up to the first \$2,500 *and any interest (if applicable)* that it provisionally recredits to a consumer account under § 229.54(c)(3)(i) if (1) the account is a new account, (2) without regard to the substitute check giving rise to the recredit claim, the account has been repeatedly *overdrawn* during the six month period ending on the date the bank received the claim, or (3) the bank has reasonable cause to believe that the claim is fraudulent." [New text in italics.] [Replaced "withdrawn" with "overdrawn".]

14. Section 229.56(c) -- Accrual of Cause of Action

Section 229.56(c) of the Proposal provides that a cause of action for a claim under the Act does not accrue, for purposes of the one year statute of limitations, until the claimant determines the identity of the bank against which the action is to be brought. By comparison, the statute of limitations provided for in the Act does not define the one year period in terms of identifying the bank against which the action is to be brought.

We recommend that the final rule delete the reference to determining the identity of the bank as a controlling factor for the accrual of the cause of action. The identity of the bank may or may not be important or relevant to the calculation of the one year period. The relevance of the identity of the bank will depend on the facts and circumstances of a particular situation. There may well be other factors relevant to calculation of the one year period that are not identified or highlighted with equal prominence in the Proposal. Accordingly, it is not clear why the Proposal singles out the identity of the bank as a controlling or determining factor for the accrual of the cause of action. We believe that courts should have flexibility to determine the timeliness of a claim considering all the relevant facts and circumstances of that particular case under the terms of the statute of limitations provided for in the Act.

Suggested Regulatory Text:

Section 229.56(c)

"Jurisdiction. A person may bring an action to enforce a claim under this subpart in any United States district court or in any other court of competent jurisdiction. Such claim must be brought within one year of the date on which the person's cause of

action accrues. For purposes of this paragraph, a cause of action accrues as of the date on which the injured party first learns, or by which such person reasonably should have learned, of the facts and circumstances giving rise to the cause of action, ~~including the identity of the warranting or indemnifying bank against which the action is brought.~~ [Deleted text in overstrike].

15. Specific Changes to Model Consumer Education Document

As indicated in the joint comment letter that ECCHO signed along with numerous other financial institutions and organizations, ECCHO believes that the Proposal's draft of the model consumer education document is too long and should be substantially shortened. However, we have provided some suggested changes to the existing text set forth in the Proposal, in the event the Federal Reserve determines to use this longer text. These suggestions are set forth below:

- (1) In the How to Make a Claim For Expedited Recredit section, replace "additional time" with "additional reasonable amount of time".
- (2) In the Our Responsibilities For Handling Your Claim section, replace "claim" with "loss" in the second line, replace "a better copy of the original check than the one you already received" with "a copy of the original check that accurately represents all of the information on the front and back of that check as of the time it was truncated or that otherwise is sufficient to determine the validity of your claim", and add in the 4th sentence after "submitted it," the following "pending completion of our investigation."
- (3) In the Reversal of Refund section, replace in the heading "Refund" with "Recredit" and replace "a better copy of the original check than the one you already received" with "a copy of the original check that accurately represents all of the information on the front and back of that check as of the time it was truncated or that otherwise is sufficient to determine the validity of your claim."

16. Indorsements Appended to Check Images

Section 229.51(b)(1) of the Proposal would require that a substitute check bears all indorsements applied by parties that previously handled the check in any form. We request that the final rule include a Commentary provision interpreting this Section to clarify that indorsements that are physically applied to the original check after image capture will not appear in the image of the original check.

An indorsement will not appear on the image when the imaging camera at a financial institution is installed "upstream" from the indorser. That is, the image of the check is captured before the check is physically indorsed. This scenario could occur in a traditional reader sorter that images the checks before the indorsements are added to the checks. This scenario could also arise when other types of image capture equipment, such as ATMs, POS, table top devices, etc., are used to capture the check image before indorsing the items.

Physical indorsements applied after imaging will be conveyed as electronic indorsement(s) and will be printed or "overlaid" on the substitute check by the reconverting bank. Only indorsements physically applied to the original check prior to imaging will be visible in the image of the original check.

This approach is consistent with the current standards for indorsements, such as DSTU X9.37 Annex J (Indorsements). DSTU X9.37 Annex J states that "The physical indorsement for the image creator will not appear in the image if the image is captured prior to the item being physically indorsed. This is acceptable, as the electronic indorsement for the image creator institution will appear in the X9.37 file as either a physical and electronic indorsement or as an electronic indorsement alone."

Suggested Commentary Text:

Commentary Section 229.2(zz)-(##)

"Indorsements Applied After Imaging. In certain cases, a bank may not apply its indorsement until after the original check has been imaged. In such cases, the indorsements applied to the check after image capture will not appear in the image of the original check. Rather, the electronic indorsement for the image truncating bank will be conveyed as either a physical (image) and electronic indorsement, or as an electronic indorsement alone. Electronic indorsements will be printed or overlaid on the substitute check by the reconverting bank."

17. Indorsement Ink Color

The Appendix D of the Proposal requires that indorsements be printed in black ink. A significant number of item-processing transports installed at financial institutions today use purple indorsement ink. We understand that in some cases black ink is currently not available and may require new black ink formulations to be developed. Switching over to black ink also requires time for the effect of the purple ink to work its way out of the indorsement system.

We request that a "grace period" be established in the final rule to allow sufficient time for financial institutions to comply with the "black ink only" requirement. This grace period is appropriate since it would take time for (i) check processing equipment vendors to make black indorsement ink and ribbons fully available for purchase by financial institutions, and (ii) for financial institutions to use up existing stocks of non-black indorsement ink and ribbons.

Suggested Text:

Appendix D (4)

“Any indorsement, reconverting bank identification, or truncating bank identification placed on an original check or substitute check shall be printed in black ink. *This requirement shall be effective one year after [enactment of the Regulation].*”
[Changes in italics].

Appendix E XXI.A 4

“To ensure that indorsements can be easily read and imaged, the standard requires all indorsements applied to original checks and substitute checks to be printed in black ink. *This requirement shall be effective one year after [enactment of the Regulation].*” [Changes in italics].

18. Section 229.2(zz) -- Application of Definition of Substitute Check to Certain Check Documents

The Commentary to Section 229.2(zz) of the Proposal states that “[B]ecause a substitute check must be a representation of an item that is defined as a check under Section 229.2(k), a paper reproduction of an image of something that is not a check cannot be a substitute check.” While we agree with the general concept set forth in this Commentary, we request that the final rule provide additional guidance on this subject in the context of certain types of check documents that are converted into ACH debits and other electronic funds transfers, instead of being processed as check transactions.

There are a number of programs currently underway and in development that permit a merchant to convert a check, received at the point of sale or through a lockbox operation, into an ACH debit or an electronic funds transfer (collectively referred to herein as “ACH debits”). While the Check 21 Act is not implicated by these programs when the transaction is processed as an ACH debit, there are some specific situations on which we seek additional guidance. Specifically, we seek guidance in the final rule on whether a check document (or an image of that check document) would qualify as a “check” for purpose of Section 229.2(k) and therefore would be eligible to be converted into a substitute check in the following cases: (i) the check document was received by the merchant as a source document for an ACH debit and the merchant decided for any reason to not process it as an ACH debit, (for example, because the check document did not qualify for conversion to an ACH debit or it was faster to collect the check document through the check collection system), or (ii) the ACH debit is returned to the merchant or its financial institution and is not collectible through the ACH network for any reason.

We seek the Federal Reserve’s guidance, either under the final rule or under a separate rulemaking pursuant to Regulation E, as to the potential application of the Check 21 Act to check documents as described above.

19. Optional Placement of Bank Name in Indorsement

Appendix D of the Proposal would make it optional for a depository bank to place its name in its indorsement on a substitute check or an original check. We recognize that, at least with respect to substitute checks and check images, there will be insufficient

space in the current file formats to include the bank name in the indorsement. However, financial institutions have found that the bank name in the indorsement is useful to identifying the bank that has indorsed a check and in quickly resolving issues relating to processing the check. Accordingly, we request that the Federal Reserve revise Appendix D in the final rule to make the bank name optional for electronic indorsements on substitute checks and check images and mandatory for physical indorsement on original checks.

Suggested Text:

Appendix D

(1) The depository bank shall indorse an original check or substitute check according to the following specifications:

(i) The indorsement shall contain—

(A) The bank's nine-digit routing number, set off by an arrow at each end of the number and pointing toward the number, and, if the depository bank is a reconverting bank with respect to the check, an asterisk outside the arrow at each end of the routing number to identify the bank as a reconverting bank;

(B) The indorsement date; and.

(C) The bank's name or location, if the indorsement is a physical indorsement.

(ii) The indorsement also may contain—

(A) The bank's name or location; *if the indorsement is created from an electronic indorsement*

(B) A branch identification;

(C) A trace or sequence number;

(D) A telephone number for receipt of notification of large-dollar returned checks; and

(E) Other information provided that the inclusion of such information does not interfere with the readability of the indorsement. [New text in italics.]

20. Issues Relating To Formatting of Substitute Checks

We have two general comments on the Proposal regarding the format of substitute checks. First, the Proposal makes a number of references to the relative size of the check image contained in a substitute check, as opposed to the size of the original paper check. For example, the proposal states that "images of personal-sized checks will be

reduced to about 80 percent of their original size.” It is our understanding that this is not a correct analysis of the relative size of the check image of the original check. In order to avoid confusion on this issue, we recommend that the final rule delete the references in the Proposal to specific percentages requirements, and only indicate that the check image is a reduced size from the original check according to the substitute check standards.

Second, given that the substitute check represents a new type of check document, we believe that it would be helpful to the financial services industry and other users of Regulation CC if the final rule included pictorial examples of the indorsements as applied to substitute checks. These pictorial examples should be based both on the requirements of the regulation as well as the current industry standards for indorsements of substitute checks.

21. Encoding For A Returned Substitute Check

We have received a number of questions regarding the encoding of a “5” in position 44 on a returned substitute check. There appears to be confusion as to whether the “5” is placed in the MICR line on the substitute check itself, or on a qualified return strip attached to the substitute check. The generally applicable industry standards require that the “5” encoding be placed on the strip. However, the Proposal has a few references to the encoding that could be misinterpreted as stating that the “5” is encoded on the check itself. We believe that it would be helpful if the final rule clarifies that in the context of a qualified return the “5” encoding is placed in the position 44 of the returned strip, not the check itself.

We have set forth suggested text below.

Suggested Text

Appendix E, Paragraph II.BB.1

1. * * * Returned checks are identified by placing a “2” or, in the case of a substitute check, a “5,” in position 44 of the MICR line *of the qualified strip of the returned substitute check* as a return identifier in accordance with American National Standard Specifications for Placement and Location of MICR Printing, X9.13 (hereinafter referred to as “ANS X9.13”) for original checks or American National Standard Specifications for Image Replacement Documents, X9.90 (hereinafter referred to as “ANS X9.90”) for substitute checks. [New text in italics].

Commentary Section 229.2(zz)-5a

a. The generally applicable industry standards contained in ANS X9.90 require the number appearing in position 44 of the MICR line of a substitute check to differ from the number that appeared in position 44 of an original check. On an original check, position 44 generally is left blank for forward collection and contains a “2” *in the attached strip* for a qualified returned check. ANS X9.90 provides that a substitute check used for forward collection *or return must have a “4” in position 44 of the*

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substitute check MICR line and a qualified returned substitute check should have a "5" in position 44 in *the MICR line on the attached qualified strip*. [New text in italics].

* * * * *

ECCHO very much appreciates this opportunity to comment on the Proposal. In the event of any questions concerning this letter or if ECCHO can be of further assistance to the Board in its consideration of the Proposal, please do not hesitate to contact me at (214) 273-3201.

Sincerely,

David Walker
President