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May 3, 2005

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

Via e-mail (regs.comments@federalreserve.gov)
and via fax: 202-452-3819

Re: Regulation CC Proposed Rule; Docket No. R-1226

Dear Ms. Johnson:

The Board of Governors of the Federal Reserve System (the “Board”) has requested comments on its proposed amendments (“Proposal”) to the Board’s Regulation CC (“Regulation CC”), with respect to remotely created checks (“RCC”) and the creation of transfer and presentment warranties for such checks. JPMorgan Chase & Co., on behalf of its lead subsidiary bank, JPMorgan Chase Bank, National Association and its affiliates, appreciates the opportunity to submit this response.

JPMorgan Chase & Co. is a leading global financial services firm with assets of \$1.2 trillion and operations in more than 50 countries. The firm is a leader in investment banking, financial services for consumers and businesses, financial transaction processing, asset and wealth management, and private equity. Under the JPMorgan, Chase and Bank One brands, the firm serves millions of consumers in the United States and many of the world’s most prominent corporate, institutional and government clients. Information about the firm is available on the Internet at www.jpmorganchase.com.

JPMorgan Chase & Co. generally supports the Proposal, which follows the general trend in both state law and clearinghouse association rules. As the Board noted, 14 states have amended their versions of the Uniform Commercial Code to incorporate warranties for the transfer and presentment of RCCs. In addition, Rule 8 of the Uniform Rules for Paper Check Exchange, as issued by The Clearing House Payments Company L.L.C. and other regional clearing house associations, contains similar transfer and presentment warranties. Clearly, this indicates the direction of legislation and industry trends with respect to this topic. Towards this end, we urge that applicable law on this topic be uniform to whatever extent possible.

Although the UCC places the liability for paying unauthorized checks on the drawee bank, a drawee bank does not have the ability to verify whether its customer has authorized a RCC. Assuming the drawee bank can identify a RCC as such, the drawee bank can try to contact its customer, which is not a practical solution, or return the RCC unpaid and assume the risk that the RCC was, in fact, authorized by its customer. This raises potential liability for the drawee bank as well as an adverse impact on customer service. Consequently, it makes sense that the depository bank make the transfer and presentment warranties. The depository bank is in the best position to know its customer who introduces the RCCs into the collection process.

Our more specific comments are set forth below. In addition, we concur with the comment letters submitted by The Clearing House and the Electronic Check Clearing House Organization.

Consumer/Commercial Accounts

The Proposal does not distinguish between RCCs drawn on consumer accounts and those drawn on commercial accounts. We agree that there should not be any distinction. The warranties should apply equally to both situations. We recognize that most RCCs probably are drawn against consumer accounts but there is no reason to limit the warranties to consumer accounts. Furthermore, sometimes it may be difficult to determine whether a check was drawn on a consumer or commercial account.

Definition of RCC

Account: Proposed §229.2(fff) states that a check is drawn on a customer *account*. Regulation CC §229.2(a) defines “account” as a transaction account as described in Board Regulation D (12 CFR §204.2(e)). However, we believe that definition is too narrow for the RCC warranties. Those transaction accounts would be traditional demand deposit accounts and NOW accounts. There are other bank products that are non-transaction accounts, such as money market deposit accounts, home equity lines of credit and credit cards with check writing capabilities. Since it is possible for a RCC to be drawn on any of these non-transaction accounts the RCC warranties should apply to these products as well as an account as defined under Regulation D. We suggest that if the Board chooses not to modify the proposed definition, the Official Commentary be quite clear that a RCC drawn on any type of an account is covered by these warranties.

Created by the payee: Proposed §229.2(fff) further states that the check *is created by the payee*. The paying bank may not have any reasonable way in which to determine whether or not a RCC was created by the payee or its agent. A clearer standard would be that a RCC “is not created by the paying bank” and we suggest that the definition be revised accordingly. This would make it more likely that the paying bank will be able to determine whether a check is a RCC and reduce the possibility that it will make inappropriate breach of warranty claims (for checks that are not RCCs) against the depository bank.

Does not bear a signature in the format agreed to by the paying bank and its customer: This portion of the definition would inappropriately include checks bearing forged signatures or counterfeit checks bearing a computer generated facsimile signature or other types of facsimile signatures, such as signature stamps. Clearly, such items are not within the intended scope of the RCC warranties. It is our experience that RCCs do not contain any of the above types of signatures. Generally, RCCs contain a statement such as “authorized by customer” or “signature on file” and do not contain anything that purports to be a signature. We recommend that the Board not attempt to describe all of the potential variations that a wrongdoer may employ to create unauthorized signatures. Instead, we recommend that the definition contain the following language: “does not bear a signature purporting to be the signature of the customer.”

Transfer and Presentment Warranties

According to the terms stated on the check: This portion of the definition is overly broad. For example, could this be construed to include indorsements and the date? We suggest that the Regulation CC warranty for RCCs be consistent with the Rule 8 RCC warranty. In Rule 8(a), in addition to other warranties under applicable law, with respect to a RCC, the Sending Bank warrants that “the person on whose account the check is drawn authorized the issuance of the check in the amount for which the check is drawn. The Board noted that the Proposal differs from the UCC provisions to the extent that the Board’s proposed warranties cover all of the terms of the check while the UCC provisions cover only authorization of the issuance of the check in the amount for which the check is drawn. We recommend that the Regulation CC warranty for RCCs be consistent with the UCC and Rule 8 approaches. In the alternative, we recommend that the scope of the warranty cover the “terms stated on the face of” the RCC, with the exception of the date of the RCC. Generally, the date of a check is not covered by UCC warranties. Issues concerning the date are covered elsewhere under the UCC in terms of post dating, antedating and stale dated checks. It is not necessary for the Regulation CC warranty to extend to the date of the check. Consistency with state law and the Uniform Rules, where applicable, will avoid the possibility of the same set of facts generating different types of claims based upon the location of the banks involved and or participation in clearing houses. That cannot be a desired result.

Another issue to consider is the applicable statute of limitations for a breach of warranty claim. Generally, under the UCC, there is a three year limitations period during which an action for a breach of warranty must be commenced. In New York, however, the UCC does not contain a three year statute of limitations. Instead, if a breach of warranty claim is framed as a breach of contract, the applicable limitations period is six years. It would be preferable for all banks to know that, with respect to RCCs, the Regulation CC one year statute of limitations applies uniformly across all 50 states. Consequently, we recommend that the Board state that the Regulation CC statute of limitations preempt similar state law.

In addition, the proposed warranties would apply only to banks and would ultimately shift liability for the loss created by an unauthorized RCC to the depository bank. Again, this differs from the UCC warranties, which apply to any person that transfers a RCC. The proposed warranties should be consistent with UCC RCC warranties as well as the general warranties made by any transferor of any check, such as the warranties relating to indorsements and alterations. We recognize that the depository bank can have recourse against its depositor by including a RCC warranty in the deposit account agreement but consistency in the law for similar purposes should be a goal.

Defenses to a Warranty Claim

The Proposal is silent as to the extent to which a bank making a RCC warranty can assert any defenses that it might otherwise be able to assert on other types of warranty claims. For example, if a paying bank can assert against its customer any defenses available under the UCC, such as negligence or an untimely claim, the warranting bank should be able to assert such defenses against the drawee bank. Otherwise, the drawee bank is inappropriately passing along a loss to the depository bank. Under these circumstances, the party who should bear the loss, namely the drawer, may be able to avoid liability. As previously stated, such rights and obligations ought to be consistent with other laws applicable to very similar circumstances.

MICR Line Identifier

The Board requested comment on how to distinguish RCCs, to which the proposed warranty would apply, from other fraudulent checks, which would not be subject to the proposed warranty. The Board suggested assigning digits to Position 44 of the MICR line to RCCs. The Board recognizes that the practical utility of a MICR line code for identifying fraudulent RCCs may be low because the person depositing a fraudulent RCC would be unlikely to place such an identifier in the MICR line. We do not disagree. We recognize that, at this time, it is unknown whether the increased processing costs versus the benefits to be derived would make it worthwhile for a MICR line identifier to be added. However, it should not be overlooked that there may be value and benefit to the depository bank when MICR identifiers can be used in conjunction with automated fraud prevention tools. An additional piece of information that enhances the deposit making activities profile of a customer may assist a depository bank in identifying fraudulent RCCs. Upon identification of a fraudulent RCC, the depository bank would have the opportunity to hold the fraudulent deposit and review the account relationship for possible closure thereby preventing the bank from potential loss. If an identifier is to be used, we suggest that it contain a minimum number of codes because there are other demands for the number of available spaces on the MICR line as well as a limited number of codes.

Extension of the Midnight Deadline

The Board requested comment on allowing a drawee bank to return an unauthorized RCC through the check system by extending the UCC midnight deadline for a period of time, such as 60 days. We disagree. The Board correctly points out that a rule extending the midnight deadline would delay finality of payment and discharge of the underlying obligation with respect to RCCs. Furthermore, creating different deadlines for different types of checks raises the possibility of banks applying the wrong deadlines for the wrong checks. This will cause an undesirable blurring of the well-established legal principle of the midnight deadline.

Claim Process

The Proposal raises questions as to the process for making a claim for a breach of the RCC warranty. We recommend that the Board endorse the procedure set forth in Rule 8. Pursuant to Rule 8(b), the paying bank may make a warranty claim by delivering the RCC to the clearing house for settlement. Although we do not have data on the specifics of RCC claims, we believe that most RCCs are low dollar amounts. If that is true, it may not be in the best interests in the depository bank to expend time and money to research the validity of a RCC claim. As such, it may be in the best interests of all parties for such claims to be handled in an expeditious manner as prescribed by Rule 8.

Implementation

We recommend that, if adopted, the Proposal not be implemented for a period of at least six months. This will afford banks the time to modify deposit account agreements, develop new procedures for handling these claims and, perhaps most importantly, educate customers who deposit RCCs.

JPMorgan Chase & Co. appreciates the opportunity to comment on this subject and would be pleased to discuss any of the points raised in this letter in more detail. Should you have any questions, please contact Lloyd Harris at 212-552-1785.

Sincerely,