From: Linda Garner

Subject: Collection of Checks and Funds Transfers Through Fedwire and Availability of Funds

Date: May 03, 2005

Proposal: Regulation J and CC- Collection of Checks and Other Items By Federal Reserve Banks and Funds Transfers Through Fedwire and Availability of Funds and Collection of Checks
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Comments:

@@@May 3, 2005
Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th and C Streets, N.W.
Washington, DC 20551

Re: Docket No. R-1226 – Comments to Proposed Amendments To Regulation CC
Dear Ms. Johnson:
U.S. Bancorp, with assets of $198 billion, is the 6th largest financial services holding company in the United States. The company operates 2,377 banking offices and 4,654 ATMs providing a full line of banking, brokerage, insurance, investment, mortgage, trust and payment services products to consumers, businesses and institutions.
U.S. Bank is pleased to submit our summary comments on the proposed amendments to Regulation CC. We have discussed the proposed amendments with other financial institutions and financial industry services groups. While our comments reflect U.S. Bank's views on the Board's proposal, we would note that they are representative of other financial services industry comments we are familiar with.
1. Application of Remotely Created Check (RCC) Warranty to Consumer and Business RCCs.
We support the current approach in the Proposal that applies the RCC warranty to RCCs that are drawn both on consumer accounts and business accounts. Treating consumer and business accounts the same for claims and adjustment processing supports a more efficient process and reflects the position of the 17 states that have adopted UCC amendments related to RCCs
2. Definition of Remotely Created Check.
Our primary concern with the definition as currently proposed concerns the requirement that the RCC is created by the payee or an agent of the payee. There are some RCCs that are created by persons other than the payee or the payee's agent. For example, a customer may contract with a third party bill

payment company. We believe that it is appropriate to have the same warranty protection apply to this type of RCC as applies to those created by the payee. It is not clear how a paying bank can determine from examining the RCC, or even from contacting the paying customer, whether or not a particular RCC was created by the payee or its agent. This could result in disputes between the paying bank and the depository bank as to whether the warranty is applicable to the RCC or not.

We have been working with ECCHO and other industry groups to issue a proposed modification to the definition of Remotely Created Check to better address our concerns and the concerns of the industry. We fully support the following definition of Remotely Created Check:

Section 229.2(fff): "Remotely created check" means a check that is drawn on a customer account at a bank, is not created by the paying bank, and does not bear a signature purporting to be the signature of the customer.

3. Warranty for RCCs

A. Scope of Warranty.

Under the Proposal, the new RCC warranty under Regulation CC would provide that the RCC is authorized by the customer "according to the terms stated on the check." We support this broad authorization warranty for RCCs, and believe that the RCC warranty should require that the name of the payee and the dollar amount be consistent with the customer's authorization. We request that the Federal Reserve consider adding guidance in the Commentary that provides a further explanation of the full scope of the RCC warranty. For example, the Commentary could give an example of how the RCC warranty would apply in a situation where the name of the payee varies from the name of the payee as identified to the customer in the context of the authorization. Such a situation can occur when the payee's trade name is used in the customer authorization process, but the payment is completed under the legal name of the payee.

B. Situations Not Covered Under Warranty.

We recommend that the Commentary to the final rule address two situations in which the RCC warranty should not apply. First, the RCC warranty should not extend to a claim by the customer that an RCC was unauthorized because the agreed payment period varied from the date printed on the RCC or from the date of actual payment of the RCC by the paying bank. For example, a drawer customer could seek credit from the paying bank, claiming that he or she had authorized the RCC to be issued only after a certain date. The existing rules under the UCC on payment of stale or post-dated checks should apply to RCCs in the same manner as traditional checks.

We also recommend that the Official Commentary to the final rule clarify that the RCC warranty does not extend to situations of "buyer's remorse" where the RCC is otherwise authorized according to the terms on its face. We believe that the RCC warranty should not permit a paying bank to make a warranty claim to a depositary bank in a situation where the paying bank has accommodated its customer by recrediting a check payment in the event of buyer's remorse.

C. Application of Warranty To Customers.

As set forth in the Proposal, the warranty for RCCs only applies between banks in the check collection process, and does not extend to a claimant bank's customers. This is a reasonable approach because the claimant bank's customer is currently protected against liability for an unauthorized RCC under the existing protections in the Uniform Commercial Code. Accordingly, we support the current scope of the RCC warranty as set forth in the Proposal.

4. Alternatives to RCC Warranty.

The Federal Reserve requested comment on the following alternatives to the new warranty for RCCs: (i) extending the midnight deadline for RCCs, and (ii) waiting for additional states to adopt the UCC revisions on RCCs. We do not support either of these two identified alternatives. With respect to extending the midnight deadline, we believe that this alternative would raise issues of finality of payment and possible other unanticipated results. Rather, we support the development of procedures under clearinghouse rules and Operating Circular 3 for the Federal Reserve Banks that would allow all or some of these RCC warranty claims to be handled through return-like processes and with settlement entry.

We also do not support waiting for additional states to adopt the UCC Revisions addressing RCCs. Given the experience with other UCC amendments and the UCC amendments addressing RCC specifically, it cannot be anticipated that a critical mass of states will enact the relevant amendments in the near future. In addition, we view the Proposal as an improvement over the UCC amendment in many respects.

5. MICR Line Identification of RCCs

The Federal Reserve requested comment on whether there should be a specific identifier for RCCs in the MICR line. We do not support establishing new codes in the MICR line to identify RCCs for the following reasons:

There are only a limited number of available spaces in the standard MICR line and a limited number of codes for such available spaces. These limited spaces and codes sets for the MICR line should be reserved for other check products and services that have a greater need for MICR line identification.

There are also practical problems and cost issues with using Position 44 to identify RCCs. It is understood that there have been issues with false reads and mis-reads in that position. This problem is compounded by the fact that most RCCs are six-inch size checks, as opposed to the longer business size checks used for substitute checks. In terms of cost issues, banks would incur substantial costs to make the necessary systems changes to encode and verify MICR lines on RCCs. System changes would be required for check sending, check receiving and even return processing. These system change costs are not justified, given the protections that are provided to a receiving bank under the proposed RCC warranty.

If the Federal Reserve considers the use of a MICR line identifier for RCCs, the Federal Reserve should also address in the final rule what enforcement mechanism will be used to ensure that creators or transferors of an RCC will properly encode the MICR line with the new identifier. For example, would the failure of a presenting bank to ensure that the RCC is encoded properly automatically result in an RCC that is “unauthorized” and subject to the warranty claim by the paying bank? The additional complexity that would accompany a necessary enforcement mechanism for the MICR line identification of RCCs is another basis for our opposition to any requirement in the final rule for MICR line identification of RCCs.

6. Transition Period For Final Rule

In the event that the Federal Reserve determines to amend Regulation CC to include a new RCC warranty, we request that the final rule have a delayed effective date of at least six months. This delayed effective date will give the financial services industry appropriate time to develop new procedures for

handling warranty claims, to update customer agreements as appropriate, to revise clearing house rules as needed, and to educate large users of RCCs regarding the impact of new inter-bank warranty. If the Federal Reserve requires MICR line identification of RCCs in the final rule, the financial services industry would require a delayed effective period greater than six months, to make the necessary system and procedure changes.

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U.S. Bank appreciates this opportunity to comment on the Proposal. In the event of any questions concerning this letter or if we can be of further assistance to the Board in its consideration of the Proposal, please do not hesitate to contact me at (513) 979-1350.

Sincerely,
Linda Garner
Senior Vice President
Enterprise Payments

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