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July 22, 2011

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

RE: Docket No. R-1419; RIN 7100 – AD 76

Dear Ms. Johnson:

I write on behalf of the Federal Reserve Bank of New York ("FRBNY") in response to the request for comment by the Board of Governors of the Federal Reserve System (the "Board") in connection with the Board's proposed amendment (the "Proposed Amendment") to Regulation E ("Reg E").[1] FRBNY is grateful for the opportunity to comment on the Proposed Amendment and hopeful that the Board or the Bureau of Consumer Financial Protection (the "Bureau") will take steps to address our comments, which FRBNY believes provide further clarity to a complex issue. As you know, FRBNY is responsible for managing and operating the Federal Reserve Banks' Fedwire® Funds Service, one of the nation's leading wire transfer systems.[2] As such, our comments focus on the effect of the Proposed Amendment on wire transfers, though many of the concerns we express are also relevant for other types of funds transfers, such as Automated Clearing House ("ACH") credit entries.

We believe that certain modifications to the Proposed Amendment, which is intended to implement the amendment to the Electronic Fund Transfer Act ("EFTA")[3] contained in section 1073 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Section 1073"),[4] may help correct what FRBNY believes are unintended consequences of Section 1073 and will help clarify the Proposed Amendment's application.

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[1] Electronic Fund Transfers, 76 Fed. Reg. 29902 (proposed May 23, 2011).
[2] "Fedwire" is a registered service mark of the Federal Reserve Banks.
[3] 15 U.S.C.S. §§ 1693-1693r (LexisNexis 2011).
[4] Pub. L. 111-203, § 1073, 124 Stat. 1376, 2060-67 (2010).

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I. Reinstatement of Article 4A of the Uniform Commercial Code

As the Board noted in the preamble to the Proposed Amendment, section 4A-108 of article 4A of the Uniform Commercial Code ("Article 4A") states that Article 4A does not apply to a funds transfer any part of which is governed by EFTA.[5] This provision was not problematic in the context of wire transfers prior to the adoption of Section 1073 because wire transfers, a subset of Article 4A funds transfers, were by definition excluded from EFTA as transfers that are not electronic fund transfers.[6] However, with the enactment of Section 1073, certain wire transfers, specifically wire transfers that are remittance transfers (each a "Wire Remittance"), are now governed by EFTA.[7] As a result, because of section 4A-108 of Article 4A, none of the provisions of Article 4A—the majority of which set forth rules governing the relationship between the banks in a wire transfer—apply to remittance transfers made by wire.

This outcome is undesirable in that it creates legal uncertainty. Introducing legal uncertainty into wire transfer systems frustrates two core objectives of those systems—keeping payments moving quickly and keeping costs down. The drafters of Article 4A recognized this, noting that parties to funds transfers need to be able to predict risk with certainty, insure against that risk, and adjust operational and security procedures accordingly.[8] The introduction of this uncertainty is not necessary and is ill advised. It would be preferable if Section 1073 applied, as proposed, to the relationship between the consumer sender and the remittance transfer provider but Article 4A were allowed to continue to apply to other aspects of the wire transfer, as well as to those matters involving the consumer and the remittance transfer provider that Section 1073 does not govern, such as unauthorized transactions.

We believe the Bureau has sufficient flexibility under EFTA to address this problem through the rulemaking process and to adopt a framework establishing the rights, liabilities, and responsibilities of parties to remittance transfers where such a framework is absent. Accordingly, the Bureau should clarify that to the extent that the operative provisions of EFTA and Reg E do not apply to one or more aspects of a Wire Remittance (*e.g.*, the obligation of a sender to pay a receiving bank), the applicable provisions of Article 4A, as enacted by the relevant state, apply, including the risk of loss for unauthorized funds transfers. To be clear, FRBNY is not advocating for any changes to the consumer protections created by Section 1073 that are now in EFTA and that are to be implemented through Reg E, but the Bureau must

[5] 76 Fed. Reg. at 29908 (referring to U.C.C. § 4A-108 (1989)).
[6] 15 U.S.C.S. § 1693a(6)(B).
[7] *See id.* § 1693o–1(g)(2).
[8] U.C.C. § 4A-102 cmt.

recognize as the Board did in the 1990s when it incorporated Article 4A into Regulation J that a legal framework ought to govern the right and obligations of every party to a funds transfer.[9]

If the Bureau determines it does not have sufficient authority under EFTA to close the described gap in commercial law, the Board should address the issue using its authority under the Expedited Funds Availability Act to regulate "any aspect of the payment system" and prescribe related regulations as it deems appropriate.[10]

The application of EFTA to Wire Remittances through the Fedwire Funds Service is more nuanced in the context of the Board's Regulation J ("Reg J") because Reg J "governs a funds transfer that is sent through Fedwire . . . even though a portion of the funds transfer is governed by the Electronic Fund Transfer Act, but the portion of such funds transfer that is governed by the Electronic Fund Transfer Act is not governed by" Reg J.[11] Prior to the enactment of Section 1073, this could have only referred to funds transfers that were made through more than one payment system. For instance, if a funds transfer began as an ACH transaction but was completed through a Fedwire transaction, EFTA and Reg E would apply to the "portion" of the funds transfer that was made over the ACH network, while Reg J (with its incorporation of Article 4A) would apply to the Fedwire "portion." With the enactment of Section 1073, however, it is now possible for Wire Remittances subject to EFTA to be carried out wholly through the Fedwire Funds Service.

Subsection 210.25(b)(3) of Reg J could be read to mean that only those portions of a Wire Remittance specifically addressed by EFTA (namely, the portion between the consumer and the remittance transfer provider) are subject to the Proposed Amendment, while other aspects of the Wire Remittance remain subject to the provisions of Article 4A as incorporated in Reg J. But we are concerned that because EFTA defines a remittance transfer as a transfer of funds from a sender to a recipient, it could be argued that all of a Wire Remittance is governed by EFTA, leaving nothing governed by Reg J. We believe this uncertainty is harmful for the reasons noted above and would ask the Board to amend Reg J to ensure its provisions apply except to the extent the specific rules established by Section 1073 apply. Alternatively, the Board might be able to accomplish this through clarification of its commentary to Reg J.[12]

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[9] *See* Funds Transfers Through Fedwire, 55 Fed. Reg. 40791, 40791 (Oct. 5, 1990).
[10] 12 U.S.C.S. § 4008(c) (LexisNexis 2011).
[11] 12 C.F.R. § 210.25(b)(3) (2011). It is worth noting that appendix B to subpart B of Reg J incorporates section 4A-108 of Article 4A, along with the rest of Article 4A. This does not raise the same issues as presented by state law because Reg J states that the main text of the regulation prevails over appendix B to the extent of any inconsistency. *Id.* § 210.25(b)(1).
[12] Separately, we note a portion of the commentary to Reg J is no longer accurate following enactment of Section 1073. The commentary currently reads in pertinent part: "Fedwire funds transfers to or from consumer accounts are

II. Accounts of Designated Recipients

Under the Proposed Amendment, a designated recipient must be a person, which may include a natural person and a number of different types of entities, but does not by its terms appear to include an account.[13] It is not, however, clear that in a typical wire transfer a sender would identify the recipient of the funds other than by the recipient's account number. The Bureau should consider whether to make clear in the regulation's definition of person (or elsewhere in the regulation) that if the sender provides the remittance transfer provider with an account number, the account is to be treated as the recipient. If the account is the recipient, then once the funds are transferred to that account, the remittance transfer provider ought to have satisfied its obligation to deliver funds to the recipient regardless of what happens next (*e.g.*, the recipient's bank exercises rights of setoff against the account before the credit can be withdrawn, or a person other than the designated recipient who has rights to control the account—as in the case of a joint account—withdraws the credit). This becomes clearer when one considers the error resolution procedures under the Proposed Amendment. For example, if the sender provides incorrect information to the remittance transfer provider (*e.g.*, an incorrect account number), the sender is apparently entitled either to a refund of the amount tendered or to another opportunity to send a remittance transfer free of charge, even though the remittance transfer provider faithfully executed the sender's instructions.[14]

A related problem concerns the ability of the remittance transfer provider to give the sender the opportunity to correct the information and resend the remittance transfer so it reaches the intended recipient, as proposed subsection 205.33(a)(1)(iv) provides.[15] This seems to presuppose that the remittance transfer provider can reverse the transaction at that point. Even in a closed system, where the remittance transfer provider interacts with both the sender and the recipient, this would be challenging because a third party may have already collected the funds. But in the case of a Wire Remittance, where the remittance transfer provider may have little or no relationship with the recipient's financial institution, the problem will be even more acute. By the time the sender notifies the remittance transfer provider of the error, the sender's account in all likelihood will have been debited and the designated account credited, so the opportunity to correct the information will have passed.

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exempt from the Electronic Fund Transfer Act and Regulation E [citation omitted]." 12 C.F.R. pt. 210, subpt. B, app. A, cmt. (b)(4) to § 210.25.

[13] Electronic Fund Transfers, 76 Fed. Reg. 29902, 29939 (proposed May 23, 2011) (definition of *designated recipient*) (to be codified at 12 C.F.R. § 205.30(c)).

[14] This would seem to be the result if subsections 205.33(a)(1)(iv)(B) and 205.33(c)(2) of the Proposed Amendment are applied. *Id.* at 29941.

[15] *See id.*

III. Remedies Applicable to Errors

The Proposed Amendment tracks potentially ambiguous language in Section 1073 relating to error resolution. Specifically, proposed subsection 205.33(c)(2) provides that the sender may designate one of two remedies in the event of an error. These remedies would put the remittance transfer provider in the position of either:

> (i) Refunding to the sender the amount of funds tendered by the sender in connection with a remittance transfer which was not properly transmitted, or the amount appropriate to resolve the error; or (ii) Making available to the designated recipient, without additional cost to the sender or to the designated recipient, the amount appropriate to resolve the error.[16]

One could read this provision to say that a remittance transfer provider is required to refund only the amount of a remittance transfer that was not properly transmitted, or, if the sender chose, some other amount that is appropriate to resolve the error. This remedy appears on its face to be fair. In a simple example, if a sender tenders $100 but the designated recipient receives only $90, the remittance transfer provider would be required to refund $10 to the sender or make that amount available to the designated recipient.[17]

However, it is also possible to read clause (i) of proposed subsection 205.33(c)(2) to require the remittance transfer provider to refund the entire amount tendered if the sender requests it to do so. In certain circumstances, it would be reasonable for a sender to request a refund of the entire amount, such as if the designated recipient received none of the funds. But the language of proposed subsection 205.33(c)(2) would appear to permit the sender to choose that remedy in all cases, even in circumstances where it would seem inappropriate. For example, if a sender requests a remittance transfer that is executed late, and the result is that the designated recipient receives the funds after the stated date of availability, then in accordance with proposed subsection 205.33(c)(2), the sender may choose to instruct the remittance transfer provider to refund the entire amount of funds tendered in connection with the remittance transfer (because the transfer was not properly transmitted), even though the designated recipient eventually received the funds to which he or she was entitled.[18] In light of this potential ambiguity, the Bureau should consider revising clause (i) of proposed subsection 205.33(c)(2). In addition, if the Bureau believes that certain remedies would be inappropriate in some cases, it might wish to consider outlining those scenarios in the commentary to Reg E.

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[16] *Id.* (to be codified at 12 C.F.R. §205.33(c)(2)).

[17] This example assumes that no fees or exchange rate charges apply.

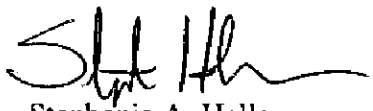
[18] In addition, under those circumstances, the remittance transfer provider must also refund any fees the sender paid. 76 Fed. Reg. at 29941 (to be codified at 12 C.F.R. §205.33(c)(2)(iii)).

IV. Exclusion of Remittance Transfers from Other Federal Regulations

Perhaps another unintended consequence of Section 1073 is that in addition to voiding the application of Article 4A to certain funds transfers, it also seems to void the application of certain federal regulations. For example, chapter X of title 31 of the Code of Federal Regulations ("Chapter X"), which implements significant aspects of the Bank Secrecy Act (as amended by, among other things, the USA PATRIOT Act), excludes funds transfers governed by EFTA from the key definitions of "funds transfer" and "transmittal of funds" under those regulations.[19] Accordingly, it seems Wire Remittances are no longer captured by regulations designed to disrupt money laundering and terrorist financing activities and to aid law enforcement in identifying those activities. We ask that the Bureau work with the Board and the Financial Crimes Enforcement Network of the Department of the Treasury to address the gaps created in Chapter X. Also, the agencies should consider whether other gaps exist in the regulatory framework.

Again, we appreciate the opportunity to comment and hope that you find our comments useful as you consider these issues.

Sincerely yours,



Stephanie A. Heller
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[19] *See* Transfer and Reorganization of Bank Secrecy Act Regulations—Technical Amendment, 75 Fed. Reg. 65806, 65814 (Oct. 26, 2010) (definition of *funds transfer*) (to be codified at 31 C.F.R. § 1010.100(w)); *id.* at 65816 (definition of *transmittal of funds*) (to be codified at 31 C.F.R. § 1010.100(ddd)).