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June 3, 2011

via <http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm>

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

Re: Docket No. R-1409 and RIN No. 7100 AD68,
Regulation CC, Availability of Funds and Collection of Checks

Dear Ms. Johnson:

The Independent Community Bankers of America (ICBA)¹ is pleased to submit comments on the Board of Governors of the Federal Reserve System (Board) proposed revisions to Regulation CC, Availability of Funds and Collection of Checks. We applaud the Board for its efforts to further facilitate the industry's continuing transition to a fully-electronic forward collection and return system by establishing a flexible and sound regulatory framework to accommodate the transition and future innovation in the electronic check clearing process.

ICBA has signed a separate joint comment letter with the Electronic Check Clearing House Organization (ECCHO), The Clearing House (TCH) and BITS. The purpose of this submission is to explain the unique perspective of community banks and to provide recommendations based solely on that perspective. Specifically, ICBA:

- Supports the Board's proposed expeditious return requirement framework, but opposes warranty exceptions when collecting and

¹ The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers they serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever changing marketplace.

With nearly 5,000 members, representing more than 20,000 locations nationwide and employing nearly 300,000 Americans, ICBA members hold \$1.2 trillion in assets, \$960 billion in deposits, and \$750 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

presenting banks agree to accept items not meeting the definition of an electronic collection item or electronic return.

- Encourages the Board to designate the FedReturn Endpoint Listing as the industry source for a paying bank ascertaining whether a depository bank has agreed to receive returns electronically.
- Strongly supports the Board's proposal for paying banks to have the prerogative to require that all same-day settlement presentments be delivered electronically and urges adoption of clarifications regarding paying banks' same-day settlement requirements in an electronic presentment environment. Additionally, the Board should retain provisions allowing a paying bank to require that all same-day settlement presentments (paper and electronic) be separated from other forward and return presentments.

Community Banks' Deployment of Electronic Check Imaging Technology

Community banks, given their size, are nimble and able to radically reengineer their operations to become more efficient and competitive far quicker than their larger competitors. Community banks' rapid adoption of check image exchange is an example of this nimbleness. ICBA believes that virtually all community banks are using electronic check imaging technology to clear and settle checks presented for forward collection. The *2009 ICBA Community Bank Payments Survey* revealed that approximately 85 percent of the survey respondents cleared and settled forward presentment checks via electronic imaging with an additional 12 percent planning to do so by 2011. ICBA's survey findings are consistent with the processing experiences of the Reserve Banks as of December 2010, noted in the proposal's commentary.

Seizing the opportunities created by the Check 21 Act and their nimbleness, community banks proceeded to implement merchant remote deposit capture at an unprecedented rate. The 2009 ICBA survey findings indicated that 62 percent of the respondents offered merchant remote deposit capture (RDC) with another 16 percent planning to offer RDC by 2011.

Although ICBA's 2009 survey did not address electronic check returns, ICBA believes that community banks are making considerable strides in adopting the technology.

ICBA Comments

Expeditious Return Requirement

Consistent with the Board's belief that a fully-electronic return check system is in the best interest of the nation's check payment system, the Board is proposing a framework wherein the risk of non-expeditious return rests with a depository bank that chooses not to accept electronic returns. Specifically, a depository bank would not be entitled to expeditious return unless it agrees to receive electronic returns directly or indirectly from the paying bank. ICBA supports the Board's proposed expeditious return requirement framework. However, ICBA opposes any industry suggestions that this risk allocation not apply in the event that collecting and presenting banks agree to accept items not meeting the definition of an electronic collection item or electronic return. Such a bifurcated system would create far too much uncertainty.

The proposed commentary provides examples of where a depository bank has agreed to receive electronic returns from a paying bank. One example is that a "depository bank has agreed to receive returns from a returning bank which holds itself out as willing to accept returns from a paying bank and the returning bank has agreed to handle items expeditiously." We believe that industry concerns regarding the difficulty or time necessary for a paying bank to determine which returning bank is a depository bank under this example is without merit.

ICBA encourages the Board to designate the FedReturn Endpoint Listing as the industry source for a paying bank ascertaining whether a depository bank has agreed to receive returns electronically. This listing is already in place and it is the definitive source for determining a depository bank's ability to receive electronic returns via the Federal Reserve System.

Same-Day Settlement Rule

The Regulation CC same-day settlement rule, effective in 1994, requires a paying bank to provide same-day settlement to a private-sector collecting bank if presentment is made by 8:00 am (local time of the paying bank) consistent with reasonable delivery requirements established by the paying bank and without the assessment of presentment fees. This existing same-day settlement regulatory framework allows collecting banks to present paper checks even though paying banks prefer to receive all of their interbank check presentments electronically.

Under the proposed § 229.36(a), the Board would allow paying banks to require checks presented for same-day settlement to be presented electronically as electronic collection items. The timeframes, deadlines and settlement methods for electronic same-day settlement presentments would be the same as those currently in effect for same-day settlement presentment of paper checks. ICBA strongly

supports the Board's proposal for paying banks to have the prerogative to require that all same-day settlement presentments be delivered electronically.

ICBA understands that there have been numerous reports of community banks operating full image clearing systems receiving requests for new paper-based same-day settlement presentments. With the adoption of image technology, few community banks maintain the ability to process paper same-day settlement and clearinghouse presentments in favor of the simpler and more efficient electronic mixed forward collection and electronic receipt process. Moreover, the increased efficiency of image and branch capture allows most community banks to complete forward processing well ahead of current end-of-day deadlines and receive 100 percent next-day availability of presented items without the additional complexity of a same-day settlement fine sort and separate settlement process.

Receiving paper same-day settlement presentments creates additional processing complexity for these community banks without providing measurable improvements in clearing and settlement risk. While paying banks should be required to accept and settle the same-day delivery from presenting banks if they deem there is value in making same-day settlement presentments, a regulatory framework requiring paying banks to accept paper same-day presentments would be contrary to the Board's directive under the Expedited Funds Availability Act to improve the nation's check processing system.

During the industry's review of the proposal, there was considerable debate regarding the proposed language in §229.36(d) (1) and (2), wherein the paying bank agrees to receive electronic collection items from the presenting bank under §229.36(a). Some expressed concern that the proposal does not clarify the term "agreement" used in the definition of an electronic collection item and electronic presentment point. Specifically, some are concerned that multiple bilateral agreements between each presenting bank and same-day settlement paying bank may create substantial legal burdens and operational hurdles that do not exist in today's paper same-day settlement rule.

ICBA does not believe that these concerns are valid. Numerous peer-to-peer image exchange relationships currently exist between the largest clearing banks, regional banks and community banks to minimize forward clearing expenses, particularly for the largest clearing banks. These existing agreements provide a reasonable market-based framework for the electronic presentment of same-day settlement items. Additionally, ICBA strongly believes that the marketplace – Reserve Banks and the private-sector – will quickly evolve to provide structure for unilateral exchange agreements to support the Board's proposed electronic same-day settlement provisions.

Under the existing same-day settlement provisions, presenting banks must notify and comply with reasonable delivery requirements of the paying bank, or by default, the paying bank must receive the presentment at any location identified in

§229.36(b), along with appropriate payment instructions. ICBA believes the industry would benefit from the clarification of paying banks' same-day settlement requirements in an electronic presentment environment. ICBA's recommended clarifications follow below.

- A paying bank must provide a secure IP address (electronic presentment point) either directly or through an agreement with a third-party (correspondent bank or service provider). Standard industry formats, including a Collection Type Indicator for same-day settlement and secure transmission protocols must be supported as well.
- A paying bank must receive and verify a test transmission file from the presenting bank within a reasonable time period (e.g., 30 business days) upon receipt of a written request from the presenting bank.
- A paying bank must provide a secure email address or alternate notification method for the receipt of settlement instructions for each same-day settlement file presented.

ICBA urges the Board to adopt these recommended clarifications to provide greater certainty, without being overly prescriptive, for both collecting and paying banks and their intermediaries in an electronic same-day settlement environment.

There is also concern that a paying bank may designate an unreasonably remote or unavailable electronic presentment point for same-day settlement; that a paying bank would refuse to enter into a same-day settlement agreement with the presenting bank; or, that an electronic presentment option would require larger paying banks to receive small-volume files from any presenting bank. ICBA believes the proposed provisions with the recommended clarifications would ensure a paying bank has reasonable presentment accommodations in place to receive electronic same-day settlement presentments. In the event a paying bank does not provide a reasonable electronic presentment point, timely testing of files and an appropriate method of receipt for settlement instructions, it would then be required to accept paper same-day settlement items. If a bank does not require electronic presentment of same-day settlement items, the existing paper presentment provisions would continue to apply as the Board's proposal does not mandate electronic receipt.

Finally, ICBA urges the Board to retain provisions in §229.3(d)(2) allowing a paying bank to require that same-day settlement presentments (paper and electronic) be separated from other forward and return presentments to ensure that existing and operational, settlement and reconciliation controls remain in place.

Again, ICBA appreciates the opportunity to comment on this important proposal. Please do not hesitate to contact me at viveca.ware@icba.org or 202.659.8111 with any questions regarding our comments.

Sincerely,

/s/

Viveca Y. Ware
Senior Vice President
Regulatory Policy