

May 02, 2014

Federal Reserve Board
Secretary, Board of Governors
20th Street and Constitution Avenue, NW
Washington, DC 20551

RE: Comments on Proposed Rule: Reg CC - Collection of Checks; Docket No. R-1409

Dear Robert deV. Frierson,

I am writing on behalf of the California and Nevada Credit Union Leagues (Leagues), one of the largest state trade associations for credit unions in the United States, representing the interests of more than 400 credit unions and their 10 million member-consumers. The Leagues welcome the opportunity to provide comments to the Federal Reserve Board (Fed) on its proposed rule for Regulation CC, Collection of Checks.

Return Requirements

The Fed has proposed two alternative approaches to modify the current expeditious return and notice of nonpayment requirements to encourage institutions that currently request paper returns to transition to electronic returns.

The Leagues support proposed Alternative 1. This alternative eliminates the expeditious return for both the paying bank and returning bank; however, the paying bank remains subject to the Uniform Commercial Code (UCC) midnight deadline for return and the returning bank remains subject to UCC's standard for ordinary care in handling returns. An expeditious return is not necessary since all checks are now "local checks" and should be settled within two business days.

Alternative 1 imposes a notice of nonpayment requirement for any check returned by a paying bank in paper form, regardless of the dollar amount of the return. The notice must be received by the depository bank by 2:00 p.m. on the second business day. In absence of an expeditious return requirement, a notice of nonpayment for paper returns makes sense. However, the Leagues do not agree that the notice be sent for any dollar amount and recommend the current \$2,500 threshold be maintained.

Indemnity – Truncating Bank (Remote Deposit Capture)

The Fed proposes to establish an indemnity relating to remote deposit capture (RDC) items that would cover depository financial institutions that accept an original paper check for deposit that is subsequently returned unpaid because it was previously paid.

The proposed rule would allow the depository bank that accepts the original paper check to make a claim against the depository bank that permitted RDC for up to one year after the date of the occurrence. In this scenario, whoever has the paper wins.

The Fed contends that a depository bank that permits its customers to truncate checks and deposit electronic images (RDC) accepts the liability that their customers may intentionally or mistakenly deposit original paper checks in other depository institutions. The Leagues refute that argument in that credit unions and banks address the risk of intentional and unintentional duplicate deposits by implementing risk mitigation procedures with their RDC program. These include setting qualification requirements, educating members/customers' of their responsibilities regarding the retention, storage, and destruction of checks, and outlining these requirements in RDC agreements and disclosures.

The Leagues strongly oppose creation of the proposed truncating bank indemnity. The Fed's intention in issuing

their proposed rule is to facilitate and encourage the banking industry's transition to fully electronic processing. Credit unions and their members desire the same thing, fully electronic banking. Electronic banking is the new normal and it continues to expand through innovation—consumers no longer merely desire electronic banking and RDC, they demand it.

Implementing this indemnity rule for truncating banks will have a significant adverse impact on credit unions and small community banks that may be forced to exit the RDC business because they cannot afford to take on the liability. These small financial institutions will be left unable to compete in the marketplace.

Another flaw in the proposal is that it contemplates one truncating bank, when in theory there may be multiple truncating banks. The proposed rule would allow a depository bank that accepted an original paper item to make a claim against a truncating bank that did not receive a return of the item. The recourse for additional truncating banks that did receive a return is to attempt recovery from the depositor who was unjustly enriched. This should be true for all banks receiving a return because the item has already been paid, whether the bank accepted an original paper check or an electronic image.

The Leagues fervently oppose creating this indemnity for truncating banks. We maintain that the financial institution of first deposit, whether by electronic image or by paper check, should be protected—as they accepted a deposit, did not receive a return of the check unpaid, and therefore made funds available to their member or customer. The financial institution receiving the return should attempt to recover the loss from the depositor.

Same-Day Settlement for Electronic Checks

The Leagues agree that Reg CC's current same-day settlement rule for paper checks should remain unchanged and should not be extended to electronic checks. It is not necessary to specify terms for electronic same-day settlement in Reg CC because almost all financial institutions currently use electronic check presentment and the terms of electronic presentment are determined by agreement.

Indemnity - Electronically Created Items or Electronic Payment Orders (EPOs)

The Fed proposes to require a financial institution sending an electronically-created item to indemnify subsequent transferees for losses caused by the fact the item was not derived from a paper check. These electronically created items (also known as Electronic Payment Orders) are electronic images created by the drawer. The Leagues support this proposed indemnification since banks cannot distinguish between images derived from paper checks and images not derived from paper.

Effective Date

The Leagues recommend an effective date of at least 12 months after a final rule is published. This extended effective date will allow financial institutions time to fully understand all amendments and make necessary technological, policy, and consumer disclosure changes.

Summary

In conclusion, the Leagues support the Fed's desire to transition the expeditious return and notice of nonpayment requirements to a fully electronic process. We ask the Fed also recognize that the payment industry and consumers demand electronic banking as well. The proposed indemnity for truncating banks will severely hinder the availability of an important electronic banking service. We oppose the proposed indemnity for truncating banks as we believe it will force many credit unions to discontinue RDC service and place them at a competitive disadvantage.

in regard to the expeditious return and notice of nonpayment alternatives, the Leagues support proposed Alternative 1. However, we recommend a \$2,500 threshold for notice of nonpayment for paper checks.

Thank you for the opportunity to comment on the proposed changes to Reg CC and the collection of checks and for considering our views.

Sincerely,

Diana R. Dykstra
President and CEO
California and Nevada Credit Union Leagues

cc: CCUL