Office of Thrift Supervision

Thrift Bulletin

Handbook: Compliance Activities
Subject: Expedited Funds Availability Act

Section: 335
TB 9-2

June 27, 1990

Recent Changes to Federal Reserve Regulation CC and Official Staff Commentary

Summary: The Federal Reserve Board has recently adopted changes to its Regulation CC implementing the Expedited Funds Availability Act and its accompanying Official Staff Commentary.

For Further Information Contact: Your District Office or Compliance Programs, Office of Thrift Supervision, Washington, D.C.

Thrift Bulletin 9-2

The Federal Reserve Board has recently adopted amendments to its Regulation CC, Availability of Funds and Collection of Checks. The regulation requires depository institutions to make funds available to their customers within specified times, to disclose their funds availability policies to their customers, and to handle returned checks expeditiously.

The amendments attached as part of this transmission include changes to the model forms and other technical and clarifying modifications to the regulation and its Official Staff Commentary. The amendments to Section 229.13(h)(4) and its Commentary are effective September 1, 1990. The amendment to the Commentary to Section 229.36(e) is effective February 1, 1991. All other amendments are effective May 22, 1990.

Attachment

Jonathan L. Fiechter
Principal Senior Deputy Director

FEDERAL RESERVE SYSTEM

12 CFR Part 229

[Reg. CC; Docket No. R-0679]

RIN 7100-AB01

Availability of Funds and Collection of Checks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board has adopted amendments to its Regulation CC, Availability of Funds and Collection of Checks. The regulation requires banks to make funds available to their customers within specified times, to disclose their funds availability policies to their customers, and to handle returned checks expeditiously. The final amendments include changes to the model forms to reflect the permanent schedule and other technical and clarifying modifications to the regulation and its Official Commentary (appendix E to the regulation). The Board has determined not to adopt the proposed amendment that would shorten the time requirements for giving notice of nonpayment.

EFFECTIVE DATES: The amendments to § 229.13(h)(4) and its Commentary are effective September 1, 1990. The amendment to the Commentary to § 229.36(e) is effective February 1, 1991. All other amendments are effective May 22, 1990.

FOR FURTHER INFORMATION CONTACT: Louise L. Roseman, Assistant Director (202/452-3874) or Gayle Brett, Manager (202/452-2934), Division of Federal Reserve Bank Operations, Oliver Ireland, Associate General Counsel (202/452-3625), or Stephanie Martin, Attorney (202/452-3198), Legal Division. For information regarding modifications to disclosures or appendix C, contact Thomas J. Noto, Staff Attorney (202/452-3667), or Jane E. Ahrens, Staff Attorney (202/452-3667), Division of Consumer and Community Affairs. *For the hearing impaired only:* Telecommunications Device for the Deaf, EArnestine Hill or Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION: On May 13, 1988, the Board adopted Regulation CC to carry out the provisions of the Expedited Funds Availability Act ("Act") (12 U.S.C. 4001-4010). The regulation requires banks [1] to make

[1] The regulation defines "bank" to include all depositary institutions, including commercial banks.

Continued

funds available to their customers for withdrawal within specified time frames, to disclose their funds availability policies to their customers, and to handle returned checks expeditiously. Section 229.33(a) of the regulation currently requires a paying bank to provide notice of nonpayment of any returned check in the amount of $2,500 or more. This notice must be received by the depositary bank by 4 p.m. (local time) on the second business day following the banking day on which the check was presented to the paying bank. This requirement generally ensures that the depositary bank would receive the notice prior to the time it must make funds available for withdrawal under the temporary availability schedule.

Some banks have expressed concern that, under the permanent availability schedule, which becomes effective September 1, 1990, depositary banks often would not receive notice of nonpayment of large-dollar returned checks prior to the time that funds must be made available for withdrawal. Therefore, in December 1989 (Docket No. R-0679, 54 FR 51405, December 15, 1989), the Board requested comment on alternatives to shorten the current time requirements for giving notice of nonpayment. In response to various questions that have been raised by banks regarding the regulation, the Board also issued for comment proposed technical and clarifying amendments. The Board received 124 comments on the proposed amendments to Regulation CC. Commenters comprised:

Commercial Banks	43
Bank Holding Companies	24
Corporations	21
Savings and Loan Institutions	15
Trade Associations	9
Credit Unions	7
Clearing Houses	5
Federal Home Loan Banks	1
Total	124

As discussed below, commenters were divided on whether and by how much the period for notice of nonpayment should be shortened. After reviewing the comments, the Board has determined that, on balance, the operational difficulties associated with shortening the time for notice of nonpayment outweigh the risks resulting from the current requirement. Therefore, the Board has not adopted an amendment to the notice of nonpayment provision. In addition, the Board issued proposed revisions to the deposit deadlines for the Federal Reserve notice of nonpayment service that would take effect if the time requirements for notice of nonpayment were to be shortened (Docket No. R-0680, 54 FR 51493, December 15, 1989). Thirty-four commenters discussed the proposed service changes and indicated how the Federal Reserve Banks' service should be modified if specific regulatory changes were adopted. Because the Board has not amended the notice of nonpayment provision, it has not adopted changes to the Federal Reserve notice of nonpayment service.

The final amendments and substantive comments are summarized below.

Section 229.2(k) Definition of "check." The Board was requested to clarify the status of ACH debit transfers under Regulation CC. The Board proposed a revision to the Commentary to the definition of "check" to state explicitly that an ACH debit transfer is not a check. The Board received fourteen comments, all in support of this proposal. The Board has adopted the amendment as proposed.

Section 229.2(r) Definition of "local check." The Board adopted final rules regarding the issuance of bank payable through checks in July 1989 (54 FR 32035, August 4, 1989). Under the new rules, effective February 1, 1991, bank payable through checks are required to contain, in a conspicuous place such as the title plate, the words "payable through" followed by the name of the payable through bank and the first four digits of the nine-digit routing number of the bank on which the check is written. Two sentences in the Commentary to the definition of "local check" refer to bank payable through checks that do not contain a designation of the payable through bank. The Board proposed to delete those sentences and to revise the Commentary to indicate that, in the case of bank payable through checks, the depositary bank may rely on the first four digits of the nine-digit routing number of the paying bank that is printed on the face of the check to determine whether the check is local or nonlocal.

The Board received 16 comments on this proposal. Ten commenters supported the proposal with no specific comment. Four commenters requested that the Board clarify whether the proposed language refers to the first four digits located in the check's Magnetic Ink Character Recognition ("MICR") line or located elsewhere on the check. Three commenters noted that any nonautomated means of identifying the paying bank is inefficient and burdensome to the depositary bank.

The Board has revised the proposed language to clarify that the Commentary refers to the four-digit number printed near the name of the paying bank in the title plate, not the first four digits of the routing number in the MICR line. In addition, instead of making the proposed deletions, the Board has revised the existing Commentary language to explain that, until the February 1, 1991 transition date, when paying banks will be liable for payable through checks issued by their customers that do not name the payable through bank, such payable through checks may continue to be issued and depositary banks cannot rely on the routing number to determine whether these checks are local or nonlocal.

Section 229.2(u) Definition of "noncash item." The Board proposed a revision to the Commentary to "noncash item" to clarify that if a bank handles an item in the same manner as it would handle a cash item, the item does not qualify as a noncash item. The Board received 16 comments on this proposal. Six commenters supported the proposal without specific comment, and seven commenters opposed the amendment. Those in opposition stated that noncash items should not become cash items by virtue of the manner in which they are handled, and that depositary banks should be allowed to collect noncash items as quickly as possible without compromising the status of the items or giving up noncash item defenses. Two commenters asked that the Board clarify the problem this amendment is intended to address.

The Board has added the phrase "by the depositary bank" to the final amendment to clarify that if a depositary bank accepts a check as a noncash item it must forward the check as a noncash item (for example, with special payment instructions attached) and not in the same manner it normally handles checks for forward collection. The purpose of this provision is to prevent a depositary bank from evading the availability and notice requirements of the regulation by accepting a check for deposit as a noncash item, yet collecting the check in the same manner as it would collect a cash item. Banks generally handle noncash items outside of the normal check collection process because they do not qualify for automated handling. A depositary bank should accept checks as noncash items

savings and loan associations, and credit unions. A "depositary bank" is defined as the first bank to which a check is transferred. A "paying bank" is generally the bank by, at, or through which a check is payable and to which it is sent for collection. A "returning bank" is a bank (other than the paying or depositary bank) that handles a returned check or a notice in lieu of return.

only in limited circumstances, such as when its customer is concerned about whether the check will be paid and requests that the check be accompanied by special notice or payment instructions.

One commenter stated that a depositary bank should be able to attach a MICR strip to an un-MICRed item and collect it as a cash item. A depositary bank may add a MICR strip to an unMICRed item, but the item must then be treated as a check and not a noncash item.

One commenter asked whether a noncash item mistakenly accepted as a cash item by a teller must be given cash item availability. If a depositary bank accepts a noncash item as a cash item inadvertently, it must either provide availability according to the regulation or return the item to the customer.

Section 229.3(a) Enforcement agencies. As part of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Congress amended the Expedited Funds Availability Act regarding the enforcement agency for savings associations. The Board proposed a conforming amendment to Regulation CC to provide that the Director of the Office of Thrift Supervision has authority to enforce compliance with Regulation CC by savings associations. The Board received eight comments on this amendment, seven in support and one objecting to allowing the Office of Thrift Supervision to oversee compliance. Because this amendment is statutorily mandated, the Board has adopted it as proposed.

Section 229.13(h)(4) Availability of deposits subject to exceptions. The regulation provides that if a bank invokes an exception hold under § 229.13 (b) through (f), it may extend the availability schedule by a reasonable period of time. Currently, the regulation provides that a four-business-day extension is a reasonable period and that a longer extension may also be reasonable, but the bank has the burden of so establishing. The four-day period is designed to provide adequate time for the depositary bank to learn of the nonpayment of virtually all checks that are returned. Thus, under the temporary schedule, a bank invoking an exception hold under § 229.13 may normally hold local checks until the seventh business day after deposit and nonlocal checks until the eleventh business day after deposit. When the permanent schedule becomes effective on September 1, 1990, these periods would have been shortened to six and nine business days, respectively.

Because there will be no further significant payments system improvements applicable to the return of checks before the permanent schedule becomes effective, it would be unlikely that depositary banks would learn of the return of checks subject to a § 229.13 exception faster than they do today. Therefore, the Board requested comment on a proposal to extend the reasonable hold period from four days to five days for local checks and from four days to six days for nonlocal checks, thereby retaining the existing exception hold periods of seven and eleven days, respectively. The Board requested comment on whether such a change would obviate the need to revise disclosures and the need to extend the reasonable hold period, based on current returned check experience.

The Board received 51 comments on this proposal, all favoring the amendment. The commenters agreed that there have been no substantial improvements to the check collection system since the changes accompanying implementation of the temporary schedules and that the amendment would help reduce risk to depositary banks. Twelve commenters stated that this amendment would obviate the need to revise disclosures, and eight stated that they would need to revise disclosures for the permanent schedule in any event. The Board has adopted the amendment as proposed.

Section 229.18(e) Changes in policy. The Board proposed to revise the Commentary to § 229.18(e) to clarify how institutions could disclose the changes in policy due to the implementation of the permanent schedule. Any necessary notice must be provided by October 1, 1990. Eighteen commenters addressed this proposal and were generally supportive. The Board has adopted the proposed amendments, with a revision to provide guidance to banks that reserve the right to impose the cash withdrawal limitation in § 229.12(d) when invoking a case-by-case hold.

One commenter asked whether an institution could disclose current and future policies on one disclosure form. This approach is permitted under the regulation provided the period during which each policy is applicable is clearly set forth. Another commenter asked whether banks could use existing stocks of forms supplemented with an attachment indicating the permanent schedule changes. This, too, is permitted under the regulation.

Section 229.19(a) When funds are considered deposited. Under § 229.19(a)(5)(ii), funds deposited at an ATM or off-premise facility after the depositary bank's cut-off hour of 12 noon or later are considered deposited on the next banking day. The Board was asked whether the 12 noon cut-off is determined by the local time of the ATM or off-premise facility or the local time of the branch or other location at which the account is maintained (the "account-holding branch").

The Board proposed to clarify that the depositary bank could establish a cut-off hour for deposits at ATMs or other off-premise facilities of no earlier than 12 noon local time of the account-holding branch. The Board specifically requested comment on the operational and customer service implications of this proposal, and whether the cut-off should be determined by the local time of the ATM rather than the local time of the account-holding branch.

The Board received 34 comments on the proposal. Nineteen commenters supported the proposed rule that ATM cut-off hours should be determined by local time of the account-holding branch. Twelve commenters opposed or noted operational problems with the proposal. Three commenters did not voice a preference for either alternative; one of these commenters requested that the Board study the issue further and republish the proposal for comment.

Under the proposal, an East Coast bank that permits its customers to make deposits at ATMs nationwide could establish a 12 noon Eastern Time cut-off for receipt of ATM deposits. Thus, deposits made by customers of the East Coast bank at West Coast ATMs after 9 a.m. Pacific Time could be considered received on the next banking day, which may adversely affect the customer's availability of funds. Conversely, a West Coast bank would have to consider all deposits made at East Coast ATMs by 3 p.m. Eastern Time (12 noon Pacific Time) received on that banking day, which would limit the time for the ATM processor to remove the deposits from the ATM, verify and process them, and put them in the forward collection stream.

Operational and customer relations concerns were raised by both those who supported and those who opposed the proposal. It appears from the comments that some banks use a cut-off hour based on local time at the account-holding branch, some are based on local time at the ATM, and some are based on local time at a central processing facility.

Commenters in favor of the proposal stated that using local time of the ATM would require significant computer modification because their present

accounting and processing systems are currently based on local time of the account-holding branch. These commenters noted that customers understand their current cut-offs based on the local time at the account-holding branch and that this rule is consistent with other provisions of Regulation CC. Supporters of the proposal asserted that if they were required to base cut-offs on local time of the ATM, processing costs would increase, resulting in decreased services and/or increased fees to customers. One commenter, with ATM locations from the East Coast to Hawaii, strongly supported the proposal, citing servicing and processing cost savings. One trade association gave qualified support to the proposal, requesting that the Board monitor the ATM situation to protect depositors from an increasing number of interstate banks that may seek to take advantage of this rule in order to delay availability of ATM deposits by an extra day.

Many of the commenters opposed to the proposal were members of nationwide shared ATM networks. One commenter suggested that a bank be able to set its own cut-off hour consistent with its processing procedures. Another stated that the operator of a shared ATM network should be able to set the cut-off hour no earlier than noon local time of the ATM. Commenters noted that it would be impractical for the ATM operator to keep track of the local times of all the account-holding branches whose customers use the shared ATM and that the proposal may require several intraday pick-ups and manual processing.

Commenters that opposed the proposal argued that customers would benefit more from a cut-off time based on local time at the ATM because it is easier to understand and disclose. One commenter suggested that, if the ATM is in a locale where the depositary bank has a branch, the cut-off hour should be determined by the local time of that branch, otherwise the bank could use local time at the account-holding branch. A Hawaii bank indicated that Hawaii banks with East Coast ATMs would be put at extreme disadvantage by the proposal.

The Board wishes to avoid disruption in current ATM and off-premise facility operations that would increase costs to both depositary banks and consumers. The responses of the commenters indicate that if either alternative is adopted, some banks will experience significant operating difficulties, depending on the extent of their ATM network and on the relative locations of the account-holding branch and the ATM or off-premise facility. Therefore, the Board has revised the Commentary to allow the depositary bank to set a cut-off hour for ATMs and off-premise facilities at either 12 noon local time of the account-holding branch or 12 noon local time of the ATM or off-premise facility. The Board believes that this flexibility will enable banks to offer ATM deposit services to their customers over broad geographic areas, without incurring significant costs due to this provision of the Commentary. A bank must apply the cut-off hour for ATMs and off-premise facilities on a uniform basis for all locations and all customers. The choice of cut-off hour must be reflected in the bank's internal procedures, and the bank must inform its customers of the cut-off hour upon request.

Commenters also suggested other related clarifications. The Commentary to the definitions of "business day" and "banking day" stages that the day of deposit for funds received at an ATM is determined by the banking day at the account-holding branch at the time the funds are received at the ATM. One commenter requested that the Board revise this Commentary provision to clarify that deposits at ATMs are subject to a 12 noon cut-off rule, i.e., even if the account-holding branch is open until 5 p.m., deposits to an ATM are not necessarily considered received on that banking day if made between 12 noon and 5 p.m. The Board has revised the Commentary to "business day" and "banking day" to reflect the cut-off rule for ATM and off-premise facilities and to clarify how to determine the day of deposit at such locations.

Two commenters asked that the Board clarify whether the proposal would apply to both proprietary and nonproprietary ATMs. The Board believes this clarification is not necessary because § 229.19(a) does not distinguish between proprietary and nonproprietary ATMs.

Another commenter asked that the Board clarify "account-holding branch." Consistent with the Commentary to § 229.19(b), the revised Commentary refers to "the branch or other location at which the account is maintained." For example, the account-holding branch may be the branch that opened the account and acts as the primary office serving the customer, that maintains signature cards on the account or other customer information, or that is credited for the customer's deposits on the books of the bank.

Section 229.19(c) Effect on policies of depositary bank. The Board proposed a revision to the Commentary to § 229.19(c) to clarify the relationship between the availability schedules and the depositary bank's right to charge back its customer's account for a returned check. The proposed language stated explicitly that the depositary bank may charge back its customer's account upon receipt of a returned check or notice of nonpayment, even if the check or notice is received after the time by which the proceeds of the check must otherwise be made available for withdrawal under the provisions of the regulation.

The Board received 21 comments on this proposal, all in support. Two commenters suggested that the Board also allow placement of a hold upon receipt of a notice of nonpayment until the returned check is received, rather than immediately charging back the depositor's account. Under the regulation, a depositary bank that receives a notice of nonpayment may place a hold under the reasonable cause exception of § 229.13(e), but this hold may not be unlimited; the depositary bank has the burden of establishing the reasonableness of an extension of the regulation's availability schedule of more than five business days for local checks and six business days for nonlocal checks.

One commenter suggested amending the proposed language to state that "the regulation should not be interpreted as precluding the right" of the depositary bank to charge back a customer's account based on receipt of a returned check for notice of nonpayment. The Board believes that the proposed language is essentially equivalent to the commenter's suggested language and has adopted the amendment as proposed.

Section 229.30(c) Extension of deadline. Increasingly, banks are providing banking services to the public on Saturdays and/or Sundays. These days are not regarded as banking days under Regulation CC, because Saturdays and Sundays are not "business days," but they may be regarded as banking days for the purposes of the Uniform Commercial Code ("UCC"). Banks that are open on Saturday may not have couriers leaving on Saturday to deliver returned checks, and even if they did, the returning or depositary bank to which the returned checks were sent might not be prepared to receive or process checks until Sunday night or Monday morning.

Prior to the implementation of Regulation CC, these banks could meet a UCC Saturday night midnight deadline for checks presented on Friday by

mailing their returned checks on Saturday. Since the implementation of Regulation CC, however, these banks have been subject to expeditious return requirements that generally may not be met by mailing returned checks. For checks presented on Fridays, these banks cannot meet both a UCC Saturday midnight deadline and the expeditious return requirements of Regulation CC without establishing special courier runs on Saturday evening to deliver returned checks to returning or depositary banks. Such runs would often be in addition to runs during the day on Sunday delivering forward collection checks to the same banks in their capacity as collecting or paying banks in the forward collection process.

To address this problem, the Board proposed to extend the Saturday night midnight deadline if the returned checks reach the receiving bank by a cut-off hour (usually on Sunday night or Monday morning) that permits processing during the receiving bank's next processing cycle for returned checks following the Saturday midnight deadline. The Board has adopted the proposed amendments with minor revisions.

The Board received 19 comments on this proposal. Twelve supported the amendment as proposed. One commenter noted that the proposal would require banks that wish to make returns directly to depositary banks to know the cut-off hours for each of the depositary banks' processing cycles and therefore would effectively force returns to be made through the Federal Reserve. The Board did not intend this result and has amended the final Commentary language to clarify that the return must be made by the cut-off hour for the returning bank's next processing cycle or for the depositary bank's next banking day after midnight Saturday night.

One commenter asked that the extension apply to all instances when a bank is open on any non-business day, such as a mid-week holiday. Two commenters requested that the Board extend the midnight deadline even further (one suggested Monday night, the other Tuesday night) to accommodate weekend presentments that are not reviewed until Monday or Tuesday.

Another commenter suggested that the Board eliminate the problem by having the Regulation CC definition of "banking day" preempt the UCC's definition for the purpose of determining the midnight deadline. The effect of this suggestion would be that checks presented after a cut-off hour on a Friday would be considered received on the next Regulation CC banking day (normally Monday), and the midnight deadline would be midnight Tuesday night.

The Board recognizes that nonstandard banking days create difficulties for the check clearing system as well as other payments operations. Issues relating to a midnight deadline other than the Saturday night deadline were not clearly raised by the proposal. Resolution of these issues will require additional data on banking practices. The Board will continue to study problems under the expeditious return rule that may arise from nonstandard banking days and may consider further modifications in the future.

Section 229.33(a) Notice of nonpayment. This section requires a paying bank to provide notice of nonpayment of any returned check in the amount of $2,500 or more. Currently, this notice must be received by the depositary bank by 4 p.m. (local time) on the second business day following the banking day on which the check was presented to the paying bank. This requirement generally ensures that the depositary bank would receive the notice prior to the time it must make funds available for withdrawal under the temporary schedule. However, under the permanent schedule, which becomes effective September 1, 1990, a depositary bank may not receive notice of nonpayment of large-dollar returned checks being returned by local paying banks before the depositary bank must make the first $5,000 of these funds available to its customer.

In order to reduce the potential for increased risk resulting from the permanent availability schedule, some bankers suggested shortening the time within which notice of nonpayment must be provided to the depositary bank. The Board requested comment on whether the risks inherent in the requirement that funds be made available to the customer for withdrawal prior to the time the depositary bank has an opportunity to learn of the return of large-dollar local checks are sufficient to warrant accelerating the time within which notice of nonpayment must be provided to the depositary bank.

The Board received 107 comments on whether the time within which a paying bank must provide notice to the depositary bank of a large-dollar returned check should be shortened. Forty-four commenters opposed shortening the notice of nonpayment deadline. These commenters stated that the additional burdens an earlier notice deadline would place on paying banks outweigh the marginal benefits that would be derived by depositary banks. Some commenters noted that several categories of paying banks would have particular problems complying with an earlier notice deadline, including banks that use payable through banks or intercept processors, and West Coast banks, which have a shorter time frame within which to provide notice to East Coast depositary banks due to the time zone differences.

Many commenters also believed that an earlier notice of nonpayment deadline would result in an increased number of returned checks, because banks would have a shorter time frame within which to make the decision of which checks to return. Accelerating the return decision would lessen the time available for management review of checks that are candidates for return, and would limit the ability of the paying bank to allow customers to deposit funds to cover a check on the day following presentment. This may result in customer service problems and an increased number of consumer complaints. Some commenters also indicated that most banks currently make funds available for withdrawal within the time frames required in the permanent schedule, and that no loss experience has been demonstrated to justify a shorter notice requirement.

Among the commenters opposed to shortening the time within which notice of nonpayment must be provided was the largest private sector notice of nonpayment service provider. This commenter indicated that, while it could modify its services to meet shorter time requirements, it was opposed to any change because it would reduce or eliminate bank officer involvement in making the return decision, increase the number of customer complaints, and increase returned check charges to banks.

Six commenters supported an earlier notice of nonpayment deadline and an additional 57 commenters conditioned their support for accelerating the notice requirement on the adoption of a particular new recommended deadline. Of the 57 conditional responses, 27 commenters recommended that the required time be shortened to the first business day following deposit, with 13 commenters recommending a 4 p.m. deadline and 14 commenters recommending various times after 4 p.m. Thirty commenters recommended that the notice requirement be accelerated to an earlier time on the second day following presentment, with 24 of those commenters indicating that the time should be before 10 a.m.

Commenters in favor of shortening the time within which the paying bank must

provide notice of nonpayment believed that an earlier notice deadline was important to protect depositary banks from the increased risks arising from the shorter permanent availability schedule, although they generally agreed that an earlier deadline would not eliminate these risks. Those commenters that recommended that notice of nonpayment be provided to the depositary bank on the business day following presentment, or before the start of business on the second business day following presentment, argued that accelerating the notice deadline to this extent was necessary to provide the intended benefits to the depositary bank. Other commenters, which urged the Board to adopt a notice deadline on the second day following presentment between the opening of business and 4 p.m., indicated that any deadline earlier than what they recommended would impose undue operational burdens on the paying bank.

The Board has not adopted a change to the notice of nonpayment requirement. The Board does not believe that the benefits of an earlier notice deadline to depositary banks would outweigh the burdens that would be imposed on paying banks. There appears to be an inverse relationship between the benefits of prompter notice to depositary banks and the burdens and disruptions to the operations of paying banks. Notices received after the day following presentment will often be received after the funds must be made available for local checks under the permanent schedule. Although earlier notice, such as receipt on the business day following presentment, would help to protect some depositary banks that make funds available pursuant to the permanent schedule for local checks, the Board believes that this earlier notice of nonpayment deadline may increase the number of checks that are returned. This increase would be inconsistent with the objectives of the Act. If a paying bank were required to provide notice of nonpayment by the day following presentment, the paying bank's midnight deadline for returning checks under the Uniform Commercial Code would effectively be shortened, because a paying bank that provides a notice of nonpayment warrants to the depositary bank that it has or will return the check for payment. Moreover, the Board believes that requiring that notices of nonpayment be provided earlier than they are today would increase paying banks' costs of returning checks.

In many cases, paying banks currently notify depositary banks of the return of large-dollar checks prior to the regulation's notice of nonpayment deadline, where it is operationally practical to do so. The Federal Reserve recently reviewed sample notices of nonpayment precessed by the Federal Reserve Banks; almost one-half of the notices surveyed were received by the depositary bank on the second business day after the check was deposited (which generally would be the next business day following presentment). Some check clearinghouses have instituted new returned check exchanges to facilitate expeditious return of the physical checks prior to the notice deadline. The Board encourages initiatives of paying banks to notify depositary banks of large-dollar returned checks prior to the notice deadline.

One trade association recommended that the Board eliminate the notice of nonpayment requirement altogether and instead lower the large-dollar safeguard exception to $2,500. The Act provides that the large-dollar exception may not be invoked for aggregate daily deposits of less than $5,000; therefore, the Board does not have the authority to reduce the large-dollar exception from $5,000 to $2,500.

Section 229.34(a) Warranty of returned check. The regulation provides that a paying or returning bank that transfers and receives settlement for a notice in lieu of return warrants that the original check has not and will not be returned. The Board has been asked to clarify that the paying or returning bank is warranting that the original check has not and will not be returned for payment, as opposed to being returned to the depositary bank for other purposes, such as to provide evidence of a forgery, that do not call for payment of the returned check under § 229.32. The Board proposed to amend the Commentary accordingly.

The Board received six comments on the proposal, all in support. One commenter suggested that the Board change the word "payment" to "reimbursement" in the first sentence of the Commentary. Such a change would not be appropriate under subpart C, which provides that returned checks are subject to payment, not reimbursement. The Board has adopted the amendment as proposed.

Section 229.35(a) Indorsement standards. Since September 1988, when Regulation CC became effective, the quality of indorsements has varied widely. In some cases, banks that handle returned checks have found indorsements to be illegible, even though the indorsements may meet the informational requirements of the regulation. There are several reasons indorsements may be unclear, such as very small type size or poor imprinting mechanisms, which may result in faint or indistinct indorsements.

Currently under § 229.35 appendix D, the duty of an indorsing bank to apply a legible indorsement is implied, but not explicit. The Board believes that an indorsing bank should be responsible for ensuring that its indorsement is legible and proposed to make this duty explicit in the regulation and the Commentary.

The Board received 46 comments on this proposal. Only one commenter opposed the proposal on the grounds that depositary banks should not be held responsible for the inability of indorsement machine vendors to meet Regulation CC's standards. Seventeen producers of one-write (carbon-band) checks commented in favor of legible indorsements. These commenters expressed support for eye-readable indorsements because they believe machine-readable indorsements are not feasible in the immediate future.

Several respondents commented on the liability for not meeting a legibility standard. One commenter suggested that the Board allow recourse against the last identifiable processor or indorser. Another commenter suggested that all late returns should be excused when the depositary bank indorsement is illegible. Under the current provisions of the regulation, if the depositary bank is unidentifiable, a bank may return a check to a previous indorser in the forward collection chain — the bank that is responsible for the illegible indorsement is liable for damages due to a late return. The Board believes that this scheme most effectively places liability for late returns due to poor indorsement on the indorsing bank.

One commenter asked that the Board set up a mechanism to enforce the legibility standards. Another commenter asked that the Board clarify that the ordinary care standards of § 229.38 would apply. Section 229.38 clearly states that it applies to all the requirements of subpart C, and thus the duty of ordinary care will apply to all indorsing banks and will serve as the enforcement mechanism.

One commenter stated that customers who apply the depositary bank indorsement under agreement should be able to accept the liability. The regulation already allows such an agreement under § 229.37.

One commenter suggested disallowing the punching of holes in the MICR line, indicating that this practice not only prevents the check from being machine-readable, but also may render

indorsements on the back of the check illegible. Because this suggestion was not subject to the notice and comment period, the Board has not made such an amendment at this time, but may consider it in the future.

One commenter suggested the Board enlarge the space available for the payee and depositary bank indorsements. The Board believes that it would be inappropriate to change the size of the depositary bank indorsement area because of potential problems the change would create for payee and collecting bank indorsers and because this change was not subject to notice and public comment.

Other suggestions included minimum size requirements for indorsement information and establishment of legibility guidelines. The Board believes that banks should be subject to the requirement to indorse legibly but that it would be costly and burdensome to establish rigid standards such as specific type size and other guidelines.

Another commenter asked that depositary banks be allowed to wait to upgrade their equipment until a major repair or replacement of current equipment is necessary. The Board believes that the regulation should not mitigate the consequences of an illegible indorsement until current equipment is replaced. Such an action would be inequitable to a paying bank or returning bank that delays a returned check due to the illegible indorsement.

Finally, one commenter asked why the phrase "during forward collection" was deleted from regulatory language. The omission of this language was inadvertent. Accordingly, the Board has adopted the amendment and the Commentary language as proposed, with the restoration of the inadvertently omitted language in the amendment.

Section 229.36(e) Issuance of payable through checks. In July 1989, the Board amended Regulation CC to require certain information to be printed on checks payable by a bank and payable through another bank ("bank payable through checks") (54 FR 32035, August 4, 1989). Effective February 2, 1991, § 229.36(e) requires such checks to contain the name, address, and first four digits of the routing number of the bank by which the check is payable, and the phrase "payable through" followed by the name and address of the payable through bank.

The Board has received inquiries as to whether it would be permissible for a bank that holds checking accounts and processes checks at a central location but that has widely-dispersed branches to label all of its checks as "payable through" a single branch and include the name, address, and four-digit routing symbol of another branch. These checks would be payable by and through the same bank,[2] and therefore the provisions of § 229.36(e) would not apply. If the Board were to allow such a practice, the result would be to lead depositors and depositary banks to believe mistakenly that the check is a bank payable through check for which availability must be assigned based on the location of the branch whose four-digit routing symbol appears on the check rather than on the location of the central office whose nine-digit routing number is encoded on the MICR line of the check.

The Board proposed an amendment to the regulation and the Commentary to provide that a bank is responsible for damages under § 229.38 to the extent that a check payable by it and not payable through another bank is labelled as provided in § 229.36(e). The Board received nine comments on the proposal, all in support. The Board has adopted the amendment with revisions to clarify the intent of the provision.

Appendix A Routing Number Guide. Appendix A to Regulation CC contains a routing number guide to aid banks in identifying next-day-availability checks and local checks. Since the publication of the proposed amendments to Regulation CC, the Federal Housing Finance Board, which oversees the Federal Home Loan Banks, has provided the Board with two additional Federal Home Loan Bank routing numbers. These routing numbers have been added to appendix A. The Board has determined that these additions are technical in nature and do not change the substance of Regulation CC, and therefore publication for comment is not required by 5 U.S.C. 553.

Appendix C Model Forms, Clauses and Notices. The Board proposed changes to the model forms to reflect the permanent schedule and the amendments to the regulation regarding payable through checks. In addition, the Board proposed to revise the Commentary to make clear that banks may rely on earlier versions of the forms though they are encouraged to update their forms when ordering new supplies. Six commenters addressed the proposed changes, which have been adopted as proposed. In addition, the Board is revising Form C-5 and the lobby notices in Forms C-15 and C-15A to reflect the permanent schedule. Corresponding changes have been made to the Commentary. Although the revisions to appendix C and its Commentary are effective immediately, banks may continue to use disclosures that reflect the availability they provide under the temporary schedule until the permanent schedule takes effect.

Suggested Amendments to the Act. Several commenters asked the Board to request that Congress amend the Act to help ease compliance burdens. *The suggestions included:* Allowing all payable through checks to be considered local or nonlocal based on the payable through bank, delaying implementation of the permanent schedule, lengthening the allowable holds for deposits to nonproprietary ATMs under the permanent schedule, allowing all exception holds to be applied to "next-day" checks, eliminating the need to give notice on every deposit when invoking large-dollar and repeated overdraft exceptions, lowering the $5,000 large-dollar exception threshold to $2,500, permitting variation of availability schedules by agreement in the case of business customers, and expanding the $400 cash withdrawal rule to cover both cash withdrawals and payment of checks presented.

The Board has recommended to Congress several amendments to the Act, including many of those suggested by the commenters. Specifically, the Board suggested that Congress:

- Modify the permanent schedule for local checks;
- Treat nonproprietary ATM deposits under the permanent schedule in the same manner as they are treated under the temporary schedule;
- Resolve the operational and disclosure difficulties concerning payable through checks;
- Expand the applicability of the exception holds to the availability schedules to checks that must be given next-day availability;
- Limit the next-day requirement for Treasury checks and "on-us" checks to checks deposited at staffed teller facilities;
- Provide greater flexibility in the manner of giving notice to the depositor that an exception has been invoked;
- Grant the Board authority to establish rules regarding losses and liabilities among entities other than depository institutions; and
- Provide for direct review of regulations adopted by the Board in the U.S. Court of Appeals.

The Board's legislative recommendations are contained in its 1990 Report to Congress Under the Expedited Funds Availability Act (March 1990).

[2] "Bank" is defined in § 229.2(e) to include all of a bank's offices in the United States. Therefore, all of a bank's U.S. branches would be considered part of a single bank.

Competitive Impact Analysis

The Board recently formalized its procedures for assessing the competitive impact of changes that have a substantial effect on payments system participants.[3] The Board believes that the final amendments will have no adverse effect on the ability of other service providers to compete effectively with the Federal Reserve in providing similar services. Only one commenter raised a competitive issue, concerning proposed amendments to § 229.30(c) (see discussion above). The commenter believed that the proposed change would give an advantage to the Federal Reserve for certain returned check business. The Board revised the final regulatory and Commentary provisions to eliminate the potential Federal Reserve advantage noted. The Board will continue to study problems of nonstandard holidays that may raise similar issues.

Final Regulatory Flexibility Act Analysis

Two of the three requirements of a final regulatory flexibility analysis (5 U.S.C. 604), (1) A succinct statement of the need for and the objectives of the rule and (2) a summary of the issues raised by the public comments, the agency's assessment of the issues, and a statement of the changes made in the final rule in response to the comments, are discussed above. The third requirement of a final regulatory flexibility analysis is a description of significant alternatives to the rule that would minimize the rule's economic impact on small entities and reasons why the alternatives were rejected. These changes are primarily clarifications to Regulation CC in response to questions and requests for clarification that the Board has received since Regulation CC was adopted. The amendments should help all depository institutions to comply with the regulation. The Board considered the effect of these revisions when developing them and does not believe the changes will result in any significant adverse economic impact on a substantial number of small entities.

List of Subjects in 12 CFR Part 229

Banks, banking, Federal Reserve System, Reporting and recordkeeping requirements.

[3] These procedures are described in the Board's policy statement entitled "The Federal Reserve in the Payments System" (55 FR 11648, March 29, 1990).

For the reasons set out in the preamble, 12 CFR part 229 is amended as follows:

PART 229—[AMENDED]

1. The authority citation for part 229 continues to read as follows:

Authority: Title VI of Pub. L. 100-86, 101 Stat. 552, 635, 12 U.S.C. 4001 *et seq.*

2. In § 229.3, paragraph (a)(2) is revised to read as follows:

§ 229.3 Administrative enforcement.

(a) *Enforcement agencies.* * * *

(2) Section 8 of the Federal Deposit Insurance Act, by the Director of the Office of Thrift Supervision in the case of savings associations the deposits of which are insured by the Federal Deposit Insurance Corporation; and

* * * * *

3. In § 229.13, paragraph (h)(4) is revised to read as follows:

§ 229.13 Exceptions.

* * * * *

(h) *Availability of deposits subject to exceptions.* * * *

(4) For the purposes of paragraphs (h)(1), (h)(2), and (h)(3) of this section, an extension of up to five business days for local checks and six business days for nonlocal checks is a reasonable period. A longer extension may be reasonable, but the bank has the burden of so establishing.

4. In § 229.30, paragraph (c) is revised to read as follows:

§ 229.30 Paying bank's responsibility for return of checks.

* * * * *

(c) *Extension of deadline.* The deadline for return or notice of nonpayment under the UCC or Regulation J (12 CFR part 210) is extended:

(1) If a paying bank, in an effort to expedite delivery of a returned check to a bank, uses a means of delivery that would ordinarily result in the returned check being received by the bank to which it is sent on or before the receiving bank's next banking day following the otherwise applicable deadline; this deadline is extended further if a paying bank uses a highly expeditious means of transportation, even if this means of transportation would ordinarily result in delivery after the receiving bank's next banking day; or

(2) If the deadline falls on a Saturday that is a banking day, as defined in the applicable UCC, for the paying bank, and the paying bank uses a means of delivery that would ordinarily result in the returned check being received by the bank to which it is sent prior to the cut-off hour for the next processing cycle, in the case of a returning bank, or on the next banking day, in the case of a depositary bank, after midnight Saturday night.

* * * * *

5. In § 229.35, paragraph (a) is revised to read as follows:

§ 229.35 Indorsements

(a) *Indorsement standards.* A bank (other than a paying bank) that handles a check during forward collection or a returned check shall legibly indorse the check in accordance with the indorsement standard set forth in appendix D to this part.

* * * * *

6. In § 229.36, a new sentence is added to the end of paragraph (e) concluding text to read as follows:

§ 229.36 Presentment and issuance of checks.

* * * * *

(e) *Issuance of payable through checks.* * * *

* * * A bank is responsible for damages under § 229.38 of this part to the extent that a check payable by it and not payable through another bank is labelled as provided in this section.

Appendix A—[Amended]

7. In appendix A, two new numbers are added, in numerical order, to the list of numbers under the subheading "Federal Home Loan Banks" as follows:

Federal Home Loan Banks

* * * * *

0654 0348 0

* * * * *

1110 1083 7

* * * * *

Appendix C—[Amended]

8. Appendix C is amended as set forth below:

a. In model forms C-1, C-2, and C-3, the first paragraph is revised to read as follows:

YOUR ABILITY TO WITHDRAW FUNDS

at [bank name and location]

Our policy is to make funds from your deposits available to you on the first business day after the day we receive your deposit. Electronic direct deposits will be available on the day we receive the deposit. Once they are available, you can withdraw the funds in cash and we will use the funds to pay checks that you have written.

* * * * *

b. In model form C-3, the heading is revised, and under the subheading "Longer Delays May Apply," the second sentence of the first paragraph is revised

to read as follows: C-3. Next-day availability, case-by-case holds to statutory limits, and § 229.13 exceptions (permanent schedule)

* * * * *

Longer Delays May Apply

* * * Depending on the type of check that you deposit, funds may not be available until the fifth business day after the day of your deposit. * * *

* * * * *

c. In model forms C-4, C-5, C-6, and C-7, a new paragraph and a subheading is added immediately preceding the subheading "Next-Day Availability," and the first sentence under the subheading "Next-Day Availability" is revised to read as follows:

* * * * *

Same-Day Availability

Funds from electronic direct deposits to your account will be available on the day we receive the deposit.

Next-Day Availability

Funds from the following deposits are available on the first business day after the day of your deposit:

U.S. Treasury checks that are payable to you.

Wire transfers.

Checks drawn on [*bank name*] (unless [*any limitations related to branches in different states or check-processing regions*]).

* * * * *

d. In model forms C-4, C-6, and C-7, the second paragraph under the subheading "Other Check Deposits" is revised to read as follows:

* * * * *

Other Check Deposits

* * * * *

If the first four digits of the routing number (1234 in the examples above) are [*local numbers*], then the check is a local check. Otherwise, the check is a nonlocal check. Some checks are marked "payable through" and have a four or nine-digit number nearby. For these checks, use the four-digit number (or the first four digits of the nine-digit number), not the routing number on the bottom of the check, to determine if these checks are local or nonlocal. Our policy is to make funds from local and nonlocal checks available as follows.

* * * * *

e. In model form C-5, the heading is revised, and two new sentences are added at the beginning of the second paragraph under the subheading "Other Check Deposits" to read as follows: C-5. Holds to statutory limits on all deposits (permanent schedule, includes chart)

* * * * *

Other Check Deposits

* * * * *

Some checks are marked "payable through" and have a four or nine-digit number nearby. For these checks, use this four-digit number (or the first four digits of the nine-digit number), not the routing number on the bottom of the check, to determine if these checks are local or nonlocal. * * *

* * * * *

f. In model form C-5, in the chart under the subheading "Other Check Deposits," the second and fourth entries are revised to read as follows:

First four digits from routing number	When funds are available—	When funds are available if a deposit is made on a Monday
*	* * *	*
	Remaining funds on the second business day after the day of your deposit.	Wednesday.
*	* * *	*
	Remaining funds on the fifth business day after the day of your deposit.	Monday of the following week.

g. In forms C-2, C-3, C-4, C-5, and C-6, under the subheading "Special Rules for New Accounts," the second paragraph is deleted, and the third paragraph is revised to read as follows:

Special Rules for New Accounts

* * * * *

Funds from electronic direct deposits to your account will be available on the day we receive the deposit. Funds from deposits of cash, wire transfers, and the first $5,000 of a day's total deposits of cashier's, certified, teller's, traveler's, and federal, state and local government checks will be available on the first business day after the day of your deposit if the deposit meets certain conditions. For example, the checks must be payable to you (and you may have to use a special deposit slip). The excess over $5,000 will be available on the ninth business day after the day of your deposit. If your deposit of these checks (other than a U.S. Treasury check) is not made in person to one of our employees, the first $5,000 will not be available until the second business day after the day of your deposit.

* * * * *

h. In form C-7, under the subheading "Special Rules for New Accounts," the second, third, and fourth sentences of the first paragraph are deleted and the second paragraph is revised to read as follows:

Special Rules for New Accounts

* * * * *

Funds from electronic direct deposits to your account will be available on the day we receive the deposit. Funds from deposits of cash, wire transfers, and the first $5,000 of a day's total deposits of cashier's, certified, teller's, traveler's, and federal, state and local government checks will be available on the first business day after the day of your deposit if the deposit meets certain conditions. For example, the checks must be payable to you (and you may have to use a special deposit slip). The excess over $5,000 will be available on the ninth business day after the day of your deposit. If your deposit of these checks (other than a U.S. Treasury check) is not made in person to one of our employees, the first $5,000 will not be available until the second business day after the day of your deposit.

* * * * *

i. In model clause C-8, the last sentence is deleted.

j. In model form C-15, the heading is revised, a new entry to be the first entry in the chart is added, and the third and fourth entries are revised to read as follows: C-15. Notice at locations where employees accept consumer deposits (permanent schedule)

FUNDS AVAILABILITY POLICY

Description of deposit	When funds can be withdrawn by cash or check
Direct deposits	The day we receive the deposit
* * *	* *
Local checks	The second business day after the day of deposit.
Nonlocal checks	The fifth business day after the day of deposit.

k. In model form C-15A, the heading is revised, a new sentence is added after the first sentence of the paragraph, and the last sentence of the paragraph is revised to read as follows: C-15A. Notice at locations where employees accept consumer deposits (case-by-case holds) (permanent schedule)

Funds Availability Policy

* * * Funds from electronic direct deposits will be available on the day we receive the deposit. * * * Then, the funds will generally be available by the fifth business day after the day of deposit.

l. Model clauses C-19 and C-19A are deleted.

Appendix E—[Amended]

9. Appendix E is amended as set forth below:

a. In the Commentary to § 229.2, the last four sentences of the third paragraph of paragraphs (f) and (g) are removed and four new identical sentences are added to the end of both paragraphs (f) and (g), the first sentence of the last paragraph of paragraph (k) is revised, the next to last sentence of paragraph (r) is revised and a new sentence is added to the end, and a new sentence is added to the end of the first paragraph of paragraph (u) to read as follows: