

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 79-202

December 11, 1979

PROPOSED SECTION TO REGULATION J

TO ALL BANKS, OTHER CREDITORS,
AND OTHERS CONCERNED IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:

The Board of Governors has released a proposed Subpart C to Regulation J governing the clearing and settlement of electronic fund transfers made through automated clearing houses operated by the Federal Reserve. The Board has asked for public comments on this proposal to be received by January 31, 1980.

The press release and complete proposal are printed on the following pages. Any inquiries should be directed to Donald L. Jackson, Ext. 6123, Larry J. Reck, Ext. 6337, or C. J. Pickering, Ext. 6294.

Sincerely yours,

Robert H. Boykin

First Vice President

Banks and others are encouraged to use the following incoming WATS numbers in contacting this Bank: 1-800-442-7140 (intrastate) and 1-800-527-9200 (interstate). For calls placed locally, please use 651 plus the extension referred to above.

FEDERAL RESERVE press release



For immediate release

November 26, 1979

The Federal Reserve Board today issued a proposal to add a new section to its regulation governing the clearing and settlement of payments that would deal with the handling of electronic fund transfers made through automated clearing houses operated by the Federal Reserve.

The Board asked for comment on its proposal by January 31, 1980.

At present, the rules for the clearing and settlement of such transfers are set forth in a series of agreements between the Federal Reserve and groups of private financial institutions participating in local or regional automated clearing house associations. The Board's proposal to add a Subpart C to its Regulation J -- Collection of Checks and Other Items and Transfer of Funds -- would establish a regulatory framework for such rules.

Subpart A of Regulation J deals with clearing and settling of checks. Subpart B deals with wire transfer of funds. Proposed Subpart C would parallel the existing parts of the regulation by setting out the terms and conditions under which the Federal Reserve Banks make their automated clearing house services available, and by establishing in regulatory form the duties and responsibilities of banks and other financial institutions involved in making payment transfers through Federal Reserve automated clearing houses.

An automated clearing house is a computer operation in which electronically recorded payments instructions, received from or through a member bank, are sorted according to the financial institutions which will receive the instructions and are prepared for presentation to the receiving

institutions for action. Settlement is made by crediting or debiting a member bank's reserve account. The electronically recorded payments instructions received by the ACH are records of instructions for payments (credits) or collections (debits) received from customers of a financial institution.

In 1976 the Board adopted an interim policy providing for access to Federal Reserve ACH facilities by all Federal Reserve member banks, whether or not members of ACH Associations and by all financial institutions that are members of ACH associations. This policy remains substantially unchanged. Subpart C, however, would specify certain agreements that member banks that are not in an ACH association must have in place to make use of Federal Reserve ACHs.

Subpart C would not affect the use of Federal Reserve ACHs by the U.S. Treasury and other Federal government agencies, as Federal government usage is covered by rules adopted by the Treasury. The new Subpart would not apply to point of sale or automatic teller transactions, or to the proposed Federal Reserve electronic check presentment program.

Of the 37 automated clearing houses in operation, 36 are Federal Reserve facilities, developed in cooperation with automated clearing house associations as a means of restraining the growth and rising cost of making payments by check. The remaining ACH is the privately owned and operated New York Automated Clearing House. The proposed Subpart C would apply -- through special provisions -- to the clearing and settling by the Federal Reserve Bank of New York of transactions sent between other ACHs and the New York ACH.

In general, proposed Subpart B would not directly relate to the rights of consumers. The Board's Regulation E, based upon the Electronic Fund Transfer Act, would contain provisions applicable to ACH transactions, including

required disclosures to consumers, documentation of preauthorized transactions, error resolution procedures and limitations on consumer liability for unauthorized transfers affecting their account.

The rules for use of Federal Reserve ACHs proposed in Subpart C contain the following definitions:

1. An originator of a payment instruction to be carried out through an ACH is the depository institution sending the instruction (item) to the Federal Reserve's ACH for clearance and settlement.

2. The depository institution receiving either credit or debit payment instructions is a recipient institution.

3. ACH operations involve two types of electronic fund transfers:

--Credit items, meaning that the originating institution has funds that the institution, or its customer, wishes to pay to another institution or the customer of another institution. This is the direct parallel, in electronic payment form, of transfer of funds by check. One common use of credit payments made through ACHs is the deposit of payroll payment instructions. A company may receive authorization from all or part of its employees to deposit their pay, electronically via an ACH, directly in the employee's financial institution, which credits the employee's account. Another common use is direct electronic deposit by the U.S. Treasury of Social Security benefit payments, in place of sending checks to the recipients.

--Debit items, meaning that the originating financial institution requests that funds be delivered to it from another depository institution, as preauthorized by customers of the two institutions. Debit items include preauthorized payment of utility bills, mortgage payments and like recurring payments. In such a case, the financial institution of a utility company may, upon the preauthorized instructions of a customer of the utility company, request payment of the customer's utility bill from the customer's financial institution.

In summary, the duties and responsibilities set forth in Subpart C would provide that:

1. The originating institution would authorize its Reserve Bank to debit or credit the reserve account of the recipient institution in accordance with the payment instruction received by the Reserve Bank. The originator would assure the recipient that the fund transfer is being made in accordance with Subpart C of Regulation J, and it would agree to indemnify the Reserve Bank for any loss or expense resulting from the originator's failure to comply with the Regulation.

2. The recipient financial institution similarly would authorize its Reserve Bank to debit or credit a reserve account and would give assurances providing against loss by the Reserve Bank due to the recipient's failure to abide by the Regulation.

3. Both the originator and recipient institutions must have agreements in place covering matters identified in Reserve Bank circulars that are necessary for efficient and reliable handling of transactions to be cleared and settled through ACH operations. For most institutions this requirement will be met by the rules of the ACH Association to which they belong.

4. For Federal Reserve member banks that are not participants in an ACH Association, Subpart C would require that the member bank assure the Federal Reserve that it has agreements in place with the financial institutions with which it exchanges payments covering matters set forth in Reserve Bank circulars.

5. Items will be handled in specified ways when (a) the originator and recipient both have the same Reserve Bank, (b) the originator and recipient have different Reserve Banks, and (c) a privately operated ACH is sending or receiving the item.

6. There are specific time limits within which an item must be handled and specifications as to how settlement for an item is to be made, as well as provisions for revocation and return of items.

7. The responsibility of a Reserve Bank is that of good faith and ordinary care, the same standard as applies in Subpart A and Subpart B to check and wire transfer operations.

Payment would be regarded as final in the case of debit items if the Reserve Bank receives final payment from the institution being debited by the opening of business on the day following the settlement date specified in the item. Otherwise, the Reserve Bank would reverse the transaction, revoking it. Thus, if the Reserve Bank receives on Day A a debit item specifying that the amount is to be paid on Day B, but does not receive payment from the institution being debited by the opening of business on Day C, the transaction will be cancelled.

With respect to credit items (such as direct payroll deposits) Subpart C would make payment final on the settlement date (the date contained in the payment instructions) on which the transaction is to take place. The originating institution would be required to have sufficient funds available in a reserve account at the opening of business on the settlement date to cover the credit payments it requested the Federal Reserve to make.

The present proposal follows publication for comment of similar proposals in November 1973 and January 1976. The present proposal has been substantially revised in the light of comment previously received.

The Board's proposal is attached.

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TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

PART 210--COLLECTION OF CHECKS AND OTHER ITEMS
AND TRANSFER OF FUNDS

REGULATION J

[Docket No. R-0262]

Automated Clearing House Items

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The action proposes that a Subpart C be added to the Board's present Regulation J. The proposed new Subpart would establish the respective duties and responsibilities of the Federal Reserve Banks and those financial depository institutions using the Federal Reserve operated electronic clearing and settlement facilities to transfer funds. These facilities are known as automated clearing house facilities.

DATE: Comments must be received on or before January 31, 1980.

ADDRESS: Comments, which should refer to Docket No. R-0262, may be mailed to Theodore E. Allison, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551, or delivered to Room B-2223 between 8:45 a.m. and 5:15 p.m. Comments received may also be inspected at Room B-1122 between 8:45 a.m. and 5:15 p.m., except as provided in section 261.6(a) of the Board's Rules Regarding Availability of Information (12 CFR § 261.6(a)).

FOR FURTHER INFORMATION CONTACT: Lee S. Adams, Senior Attorney (202/452-3594), Legal Division, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

SUPPLEMENTARY INFORMATION: The proposal sets forth a system of rights and responsibilities governing the receipt and use of Federal Reserve electronic clearing and settlement services through automated clearing house facilities. These facilities were developed by associations of depository institutions in conjunction with the Federal Reserve as a means of reducing the growing volume and increased cost of processing paper checks.

The ACHs clear and settle both debit and credit items. Debit items include preauthorized bill payments, insurance premiums, mortgage payments, etc., and cash concentration transfers. Credit items include direct deposit of income payments and batched customer-initiated transfers, such as telephone bill payment items. At the present time, 36 Federal Reserve ACH facilities are in existence.

Automated clearing house operations and the Federal Reserve's role in such operations essentially parallel check clearing operations except that the payment information is contained on electronic media as opposed to paper checks. In ACH transactions, financial institutions create computer records of debit and credit items based upon customer instructions and deliver the media to their local Federal Reserve clearing and settlement facility, just as those institutions would deliver checks to the Federal Reserve's check collection facility. A Federal Reserve computer reads, edits, and balances the information and sorts items according to the receiving financial organization. When the processing has been completed, the computer creates output media consisting of magnetic tapes or descriptive paper listings. The Federal Reserve then sends the output media to the receiving financial organization generally using the same delivery system as that used for delivering checks. The settlement of balances arising out of the clearing of such items is made by debiting and crediting accounts of member banks of the Federal Reserve.

The Board has published for public comment proposed rules for handling such transactions on two prior occasions, November 1973 (30 Federal Register 32952) and January 1976 (41 Federal Register 3097). The present proposal has been substantially revised from the earlier proposals. These revisions reflect the Board's consideration of the numerous comments received by the Board to the earlier publications and the fact that as originally proposed both Subpart B and Subpart C would have provided rules governing both large dollar amount payments and small dollar amount ACH payments. On June 23, 1977, the Board published in final form Subpart B of its Regulation J (12 CFR 210) that sets forth rules governing wire transfer of funds between member banks over the Federal Reserve communications system.

In its present form, the Subpart C proposal sets forth only the rules governing the rights and responsibilities of member banks and of financial depository institutions that are members of ACH associations that use Federal Reserve ACH facilities. Although ACH facilities are also used in connection with the Federal Reserve's participation in the federal government's recurring payments program, rules under which these facilities are used for distribution of such federal payments have previously been adopted by the United States Treasury (31 CFR 210) and, therefore, the provisions of the proposed Subpart C would not apply to such transactions. In addition, the proposed Subpart C to Regulation J does not establish rules regulating the operation of other electronic payment systems, such as automated teller machine and point-of-sale networks. The Subpart would not apply to the Federal Reserve's proposed electronic check presentment project.

The rules proposed in Subpart C would not directly relate to the rights of consumers except insofar as such rights flow from responsibilities imposed on financial depository institutions. The Board's Regulation E (12 CFR 205, 44 Federal Register 59464, 44 Federal Register 59474), issued under the Electronic Fund Transfer Act, would contain provisions applicable to ACH transactions. Such provisions include disclosure of terms, handling and documentation of preauthorized transfers, and error resolution procedures. That Regulation also contains limitations on liability for unauthorized transfers, among other provisions.

In setting forth the respective rights and responsibilities of participants in ACH operations, the proposed Subpart would not modify or otherwise affect the Board's interim policy announced on January 15, 1976 (41 Federal Register 3097) regarding depository institution access to Federal Reserve ACH facilities. Under the interim access policy, both member banks and depository institutions that are participants in local ACH associations will continue to be able to deposit items with or receive them from a Federal Reserve Bank.

Like the other Subparts to Regulation J, Subpart C is intended to govern principally the relationship between the Federal Reserve Banks and the financial depository institutions. Unlike the check collection system, which has a comprehensive system of rules provided by the UCC and case law, ACH transactions currently rely upon agreements between financial institutions involved. The Board considers it essential that a comprehensive set of rules and procedures be in place for the ACH system to operate in a reliable and efficient manner. Accordingly, section 210.76 of the proposed regulation provides that the operating circular to be issued by the Federal Reserve Banks in connection with Subpart C contain a requirement that financial depository institutions agree with each other on rules and procedures to govern the ACH transaction between them. The subject matter to be covered by such an agreement would be specified in the operating circular, such as authorization requirements, prenotification procedures and settlement rules. The detailed provisions of these agreements would be decided upon by the financial depository institutions. It is expected that the existing rules and procedures of the ACH associations and of the National Automated Clearing House Association would satisfy the requirement for such agreements. ACH rules govern ACH transactions where both parties are members of ACH associations.

As noted above, banks that are members of the Federal Reserve System but are not members of an ACH association, are enabled by the access policy to make use of ACH facilities operated by the Reserve Banks. For example, if a member bank not belonging to an ACH association wishes to originate ACH items, it must have agreements in place with the financial institutions that are to receive such items. Likewise, if a member bank not belonging to an ACH association receives ACH items, it must have agreements with the financial institutions sending items to it. These agreements must be in writing, and either may be signed by both parties or may be in the form of a written offer to handle ACH

transactions under certain specified terms. The latter alternative may be satisfied by the member bank sending a written statement of terms and conditions under which that member bank will handle the ACH transaction. If the other party continues to send ACH items to the member bank, or receives items from the member bank, the written terms and conditions would apply. The Board has considered various alternative means of assuring that transactions will be governed by rules in addition to those provided by the regulation and solicits comment on its proposal to impose the responsibility for obtaining these agreements as stated herein.

The Board believes that publication of this proposed Subpart is appropriate at this time in view of the continuing increase in the volume of ACH transactions and the benefits that would be derived from the establishment of a uniform system of rules and responsibilities applicable to all participants in Federal Reserve ACH operations. Currently, each group of depository institutions forming and participating in an ACH association enters into separate agreements and understandings among themselves and with a Federal Reserve office or offices regarding the operations of the regional ACH facility for regional and interregional transactions. Adoption of Subpart C will provide needed clarification to all parties obtaining services from an ACH as to their respective duties and responsibilities.

While this Subpart is not intended to replace rules issued by an ACH association, the rules set forth in this Subpart and the operating circulars issued pursuant to this Subpart will take precedence over any rules issued by one or more ACH associations that are inconsistent with this Subpart or the operating circulars. For example, when the proposed regulation becomes effective, it will replace existing agreements and rules under which Reserve offices act as "operator" of ACHs. On the other hand, as noted above, existing provisions of ACH rules on subjects such as authorization requirements, warranties, prenotification, and settlement will satisfy the regulation's requirements for supplemental rules. In addition, proposed section 210.81(a) permits a recipient to reverse an entry not only by returning an item within the midnight deadline, but also by taking other action provided for in an agreement between the parties and authorized by the operating circular. It is contemplated that the circular would authorize the reversal of an entry on receipt of an adjustment for debit in error, now commonly provided for in ACH rules, if similar reversal could be made to the originator's account. An example of conceptual change without substantive effect is that the proposal defines an interoffice transaction as one where the originator and recipient maintain accounts at different Federal Reserve offices. Thus, under the proposal a transaction may be an interoffice transaction although it is between members of the same ACH association and a transaction may be an intraoffice transaction even though it is between members of different ACHs.

Under the proposed Subpart, an originator is the depository institution sending an item to a Reserve Bank's electronic clearing and settlement facility. In the case of a credit item, the originator has funds which it or its customer desires to send to another depository institution's customer or to its account at another depository institution. With regard to a debit item, the originator requests or orders funds to be delivered to it from another depository institution. The depository institution that receives an item from a Federal Reserve Bank is referred to as the recipient. In these ACH transactions, funds may not shift at the same time the items are sent and received. Under the proposal, the time of settlement may be based upon a date specified for a grouping of items ("batch") that may be independent of, although subsequent to, the time of receipt of the magnetic tape containing the items by the recipient. The settlement and return times stated in the proposal may be modified as further experience with these transactions is gained.

The Federal Reserve Banks would assume the standard of ordinary care in handling and processing items under this Subpart. That standard is currently applied with respect to check collections under Subpart A and wire transfers of funds under Subpart B, and is the standard usually adopted by banks in dealing with customers. A Reserve Bank does not act as agent or subagent of the originator of an item, but is performing the functions of a clearing house.

The regulation also applies to the clearing and settlement by the Federal Reserve Bank of New York for ACH items sent through the New York Automated Clearing House. Under proposed section 210.77(c), a Reserve Bank may receive and send items through a privately operated ACH and settle for such transactions by means of debits and credits to accounts held at the Reserve Bank. The operating circular of such a Reserve Bank would contain special provisions for such services.

This notice is published pursuant to § 553(b) of Title 5, United States Code, and § 262.2(a) of the Rules of Procedure of the Board of Governors. The proposal is made under the authority of sections 11 and 16 of the Federal Reserve Act (12 U.S.C. 248(j), (o)), that authorize the Board to promulgate rules governing the transfers of funds through Federal Reserve Banks. To aid in the consideration of this material by the Board, interested persons are invited to submit relevant data, views, comments, or arguments.

To implement its proposal, the Board is considering amending Regulation J (12 CFR 210) as set forth below:

1. Paragraph (a) of § 210.2 would be amended, but without change in footnotes, to read as follows:

§ 210.2 Definitions

* * * * *

(a) The term "item" means any instrument for the payment of money, whether negotiable or not, which is payable in a Federal

Reserve district,^{1/} is sent by a sender or a nonbank depositor to a Federal Reserve Bank for handling under this subpart, and is collectible in funds acceptable to the Federal Reserve Bank of the district in which the instrument is payable, except that^{2/} the term does not include any check that cannot be collected at par,^{2/} or any item as defined in § 210.52(a) or § 210.71(j) of this part.

* * * * *

2. Paragraph (a) of § 210.52 would be amended to read as follows:

§ 210.52 Definitions

* * * * *

(a) The term "item" means any instrument for the payment of money, issued, transmitted, or received in accordance with this subpart, except that the term does not include any item as defined in § 210.2(a) or § 210.71(j) of this part.

* * * * *

3. Part 210 would be amended by adding after § 210.65 the following:

Subpart C--Clearing and Settlement of Credit and Debit Items

Section

- 210.70 Authority, Purpose, and Scope
- 210.71 Definitions
- 210.72 General Provisions
- 210.73 Sending Items to Reserve Banks
- 210.74 Originator's Agreement
- 210.75 Recipient's Agreement
- 210.76 Supplemental Agreements
- 210.77 Handling Items
- 210.78 Time Limits
- 210.79 Settlement
- 210.80 Advice of Debit
- 210.81 Revocation of Items
- 210.82 Return of Items
- 210.83 Return of Funds
- 210.84 Extension of Time Limits
- 210.85 Reserve Bank Liability

§ 210.70 Authority, Purpose, and Scope

The Board of Governors of the Federal Reserve System ("Board") has issued this subpart pursuant to the Federal Reserve Act, paragraph 1 of section 13, as amended (12 U.S.C. 342), paragraph (f) of section 19, as amended, (12 U.S.C. 464), paragraphs 13 and 14 of section 16 (12 U.S.C. 360, 248(o)), paragraphs (i) and (j) of section 11 (12 U.S.C. 248(i) and (j)), and other laws. This subpart governs the clearing and settlement by Federal Reserve Banks ("Reserve Banks") of credit and debit items recorded on magnetic tape or other approved media, but it does not apply to wire transfers of funds governed by Subpart B or federal recurring payments, governed by 31 Code of Federal Regulations, Part 210. Its purpose is to provide rules for the transfer of bank balances on the books of financial depository institutions and Reserve Banks. This subpart and the operating circulars of the Reserve Banks preempt or supersede agreements or other arrangements among account holders, originators, and recipients only to the extent that provisions of those arrangements are inconsistent with this subpart and the operating circulars.

§ 210.71 Definitions

As used in this subpart, unless the context otherwise requires:

(a) "Account holder" means a member bank, a Reserve Bank, or another institution maintaining an account with a Reserve Bank.

(b) "Actually and finally collected funds" means settlement that is, or has become, final and irrevocable.

(c) "Approved medium" means any of the following media if specified in the operating circular of the originator's Reserve Bank: any form of communication, other than voice, registered on (or in form suitable for being registered on) magnetic tape, disc, or other medium designed to contain in durable form conventional signals used for electronic communication of messages, or output produced from this form of communication.

(d) "Automated clearing house" means a facility, other than a Reserve Bank, that clears debit and credit items for financial depository institutions.

(e) "Banking day" means a day during which a Reserve Bank, depositor, originator, or recipient is open to the public for carrying on substantially all its banking functions.

(f) "Credit item" means an item sent to a Reserve Bank by an originator for debit to the originator's account and for credit to a recipient's account.

(g) "Customer" means a party designated in an item for whose account the originator or recipient sends or receives the item.

(h) "Debit item" means an item sent to a Reserve Bank by an originator for credit to the originator's account and for debit to a recipient's account.

(i) "Interoffice transaction" means a transaction between an originator and recipient that do not maintain or use accounts at the same Reserve Bank office.

(j) "Item" means a writing contained in an approved medium that evidences a right to the payment of money and that is sent to a Reserve Bank for clearing and settlement under this subpart. "Item" does not include: (1) an item subject to Subpart A governing the collection of checks and other items; (2) an item subject to Subpart B governing wire transfers of funds; (3) a credit payment subject to 31 Code of Federal Regulations, Part 210, governing federal recurring payments by means other than by check; or (4) wire transfer of U.S. Treasury or federal agency securities by a Reserve Bank. An item is deemed to be the same item even if the medium in which it is contained changes during handling of the item.

(k) "Originator" means an account holder or other financial depository institution that maintains or uses an account with a Reserve Bank for settlement under this subpart and that is authorized by that Reserve Bank to send a credit or debit item to it.

(l) "Originator's account" or "recipient's account" means the account at its Reserve Bank maintained or used by the originator or recipient, respectively, under a special arrangement between the Reserve Bank and the account holder, for settlement under this subpart.

(m) "Originator's Reserve Bank" or "recipient's Reserve Bank" means the Reserve Bank office at which the originator or recipient, respectively, maintains or uses an account.

(n) "Recipient" means an account holder or other financial depository institution that is authorized by a Reserve Bank to receive a credit or debit item from the Reserve Bank.

(o) "Settlement date" means the date for settlement of an item as provided in § 210.79(c).

§ 210.72 General Provisions

(a) General. Each Reserve Bank shall clear and settle for items in accordance with this subpart, and shall issue an operating circular governing the details of its handling of items and other matters deemed appropriate by the Reserve Bank. The circulars may, among other things, set minimum or maximum dollar amounts and specific format requirements for items, and impose charges for handling items.

(b) Binding effect. This subpart and the Reserve Banks' operating circulars are binding on each originator, recipient, and customer, and on each account holder agreeing to settle for items under this subpart.

(c) Government originators and recipients. Except as otherwise provided by statutes of the United States, or regulations issued or arrangements made thereunder, this subpart and the operating circulars of the Reserve Banks apply to the following when acting as an originator or recipient: a department, agency, instrumentality, independent establishment or office of the United States, or a wholly owned or controlled government corporation, that maintains or uses an account with a Reserve Bank.

§ 210.73 Sending Items to Reserve Banks

(a) An originator may send an item to its Reserve Bank only if it arranges to have in its account, at the opening of its Reserve Bank's banking day on the settlement date, a balance of actually and finally collected funds sufficient to cover the amounts of credit items to be debited to the account on that day. The Reserve Bank has a security interest in the assets of the originator, and of the account holder whose account the originator uses for settlement, in the possession of, or held for the account of, the Reserve Bank if:

- (1) the balance in the originator's account at the close of the Reserve Bank's banking day on the settlement date is not sufficient to cover the amounts debited to the account during that day; or
- (2) the originator suspends payment or is closed at any time during the Reserve Bank's banking day on the settlement date, and does not have a balance in its account sufficient to cover the amounts debited to the account.

(b) In an interoffice transaction, the originator's Reserve Bank may permit or require the originator to send the item direct to the recipient's Reserve Bank. If an item is sent direct, the relationships and the rights and liabilities between the originator, its Reserve Bank, and the recipient's Reserve Bank are the same as if the originator had sent the item to its Reserve Bank and that Reserve Bank had sent the item to the recipient's Reserve Bank.

(c) An originator may send a notification of an item it intends to send in the future to its Reserve Bank for handling as if the notification were an item, except that no funds will be transferred. A recipient may return the notification to its Reserve Bank for return to the originator.

§ 210.74 Originator's Agreement

- (a) By sending an item to a Reserve Bank, the originator:
- (1) warrants to the recipient that the item is sent in accordance with this subpart and the Reserve Bank's operating circulars;
 - (2) authorizes its Reserve Bank and the recipient's Reserve Bank to handle the item in accordance with this subpart and the Reserve Banks' operating circulars;
 - (3) authorizes its Reserve Bank (i) to debit the amount of a credit item to the originator's account at the opening of its Reserve Bank's banking day on the settlement date, and (ii) to credit the amount of a debit item to the originator's account on the settlement date; and
 - (4) agrees to indemnify each Reserve Bank handling the item for any loss or expense sustained (including attorneys' fees and expenses of litigation) resulting from any action taken by the Reserve Bank in accordance with this subpart and the Reserve Banks' operating circulars.

(b) The warranty, authorizations, and indemnity in subsection (a) do not limit any other warranty, authorization, or indemnity made by an originator to a recipient or a Reserve Bank.

§ 210.75 Recipient's Agreement

(a) A recipient designated in an item, by maintaining or using an account with a Reserve Bank for settlement under this subpart and receiving an item from the Reserve Bank:

- (1) authorizes its Reserve Bank to credit or debit the amount of the item to the recipient's account on the settlement date; and
- (2) agrees to indemnify each Reserve Bank handling the item for any loss or expense sustained (including attorneys' fees and expenses of litigation) resulting from a breach of the foregoing authorizations or from the recipient's failure to comply with this subpart and the Reserve Banks' operating circulars.

(b) The authorization and indemnity in subsection (a) do not limit any other authorization or indemnity made by a recipient to a Reserve Bank.

§ 210.76 Supplemental Agreements

Each Reserve Bank shall include in its operating circulars a provision requiring the originator or recipient of an item to warrant to each Reserve Bank handling the item that the originator and recipient have agreed to provisions governing specified matters that are not covered by this subpart but which are necessary for the efficient and reliable handling of credit and debit items. The Reserve Bank may impose the warranty requirement on an originator or recipient taking into consideration the requirements of existing supplemental systems of rules.

§ 210.77 Handling Items

(a) Intraoffice transactions. If an originator and recipient maintain or use accounts at the same Reserve office, that office shall send or make available any item it receives to the recipient.

(b) Interoffice transactions.

- (1) The originator's Reserve Bank shall handle an interoffice transaction by sending the item to the recipient's Reserve Bank, which shall send the item or make it available to the recipient.
- (2) With the agreement of the recipient's Reserve Bank, the originator's Reserve Bank may send or make an item available directly to the recipient. This subpart applies as though the originator's Reserve Bank had sent the item to the recipient's Reserve Bank and that Reserve Bank had sent the item or made it available to the recipient.

(c) Automated clearing houses.

- (1) An originator may send an item to a Reserve Bank through an automated clearing house, and a Reserve Bank may send an item to a recipient through an automated clearing house. In either case, the Reserve Bank shall debit or credit the originator's or recipient's account, as the case may be, with the amount of the item. The debit or credit may be commingled with other entries to be posted to the account in connection with the settlement of clearings at the automated clearing house.

- (2) The rights and duties of an originator or recipient and a Reserve Bank sending or receiving an item through an automated clearing house are the same as though the item had been sent direct to, or received direct from, the Reserve Bank.

§ 210.78 Time Limits

(a) Time schedule. Each Reserve Bank shall include in its operating circulars a schedule showing the hours during which it accepts items and returned items. The schedule will show the minimum and maximum number of days, in advance of the date specified for settlement of the item, during which the Reserve Bank accepts the item ("date limitations"). When the specified date is outside the date limitations, the Reserve Bank will not accept the item.

(b) Acting seasonably. A Reserve Bank acts seasonably if it takes proper action on the banking day it receives an item. Taking proper action within a reasonably longer time may be seasonable but the Reserve Bank has the burden of so establishing.

(c) Transactions after time limit. A Reserve Bank is not required to act on the day it receives an item if the Reserve Bank receives the item after the time shown in its schedule. In emergency or other unusual circumstances, a Reserve Bank may handle items before or after the hours or days shown on its schedule of time limits. No action taken under this paragraph is binding on any other Reserve Bank.

§ 210.79 Settlement

(a) Recipient's Reserve Bank. The recipient's Reserve Bank, on the settlement date, shall credit or debit the recipient's account in the amount of the item and shall debit or credit in the same amount the originator's account, or, in an interoffice transaction, the account of the originator's Reserve Bank.

(b) Originator's Reserve Bank. In an interoffice transaction, the originator's Reserve Bank, on the settlement date, shall debit or credit the originator's account in the amount of the item, and shall credit or debit in the same amount the account of the recipient's Reserve Bank.

(c) Settlement date. Settlement for an item shall take place on:

- (1) the date specified in an item or its accompanying medium for payment of the item ("specified date"); or

- (2) the date shown for settlement in the Reserve Bank's operating circulars, when:
- (i) the specified date is earlier than the date limitations referred to in § 210.78(a);
 - (ii) the specified date is not a banking day for the originator, the recipient, the account holder whose account either of them use for settlement, or a Reserve Bank involved with the transaction; or
 - (iii) there is no specified date.^{1/}

(d) Right to use funds. A Reserve Bank may, at any time until its opening of business on the banking day following the settlement date, refuse to permit the use of credit given for a debit item for which the Reserve Bank has not received actually and finally collected funds. Credit given by a Reserve Bank for a credit item is available for use on the settlement date, subject to the Reserve Bank's right to apply the funds to an obligation owed to it.

(e) Suspension or closing of financial institution. A Reserve Bank shall not settle for an item after it receives notice of the suspension or closing of the originator, the recipient, or an account holder whose account the originator or recipient uses for settlement.

(f) Credit to customer. If the amount of a credit item is to be paid to a customer, the recipient shall credit to the customer's account, or make available to the customer, the amount of the item on the settlement date, unless the recipient returns the item in accordance with section 210.82 of this Subpart.

§ 210.80 Advice of Debit

An account holder is deemed to approve, on its own behalf, and on behalf of an originator or recipient using the account holder's account for settlement, the accuracy of the advice of debit to its account unless it sends to its Reserve Bank written objection within 10 calendar days of receiving the advice of debit.

§ 210.81 Revocation of Items

(a) No originator or prior party has a right to revoke an item after it has been received by a Reserve Bank. A Reserve Bank may, on request by the originator, revoke an item by (1) returning the item;

^{1/} When a recipient's Reserve Bank expects that an item will not be delivered to the recipient by the date scheduled for delivery, the settlement date will be the date the Reserve Bank gives telephone advice of the item to the recipient, as provided in the Reserve Bank's operating circular.

(2) asking the recipient to return the item or funds that have been transferred; or (3) asking the recipient's Reserve Bank to return the item or to ask the recipient to return the item or funds that have been transferred, as the case may be. If an item is so returned, all debits and credits previously made in settlement of the item shall be reversed.

(b) A Reserve Bank may, on its own initiative, cease acting on an item (1) if, because of circumstances beyond its control, it is unable to handle the item in accordance with this subpart and its operating circular; or (2) in the case of a credit item, if the originator's Reserve Bank judges that there may not be sufficient funds in the originator's account on the settlement date to cover the item. A Reserve Bank shall promptly notify the originator and a recipient to which it has sent an item, or their Reserve Banks, of nonpayment of the item.

(c) A Reserve Bank may initiate a reversing batch of items promptly after it discovers that it sent a duplicate or erroneous batch of items. The Reserve Bank shall notify the originator or its Reserve Bank accordingly.

§ 210.82 Return of Items

(a) A recipient has the right to reversal of a credit or debit made under section 210.79 of this subpart by returning the item to the Reserve Bank from which the item was received before midnight of the recipient's banking day next following (1) the settlement date; or (2) the banking day of receipt, whichever is later. A recipient also has the right to reversal of a credit or debit by taking other action as specified in an agreement between the originator and recipient and as authorized in the Reserve Banks' operating circulars. A recipient shall return an item in the medium and format specified in the operating circular of its Reserve Bank.

(b) In an interoffice transaction, the recipient's Reserve Bank shall send a returned item to the originator's Reserve Bank.

(c) A recipient that returns an item to a Reserve Bank: (1) warrants to the originator and to each Reserve Bank handling the item that it took all action necessary to recover its settlement within the time limits of this subpart and other law; and (2) agrees to indemnify each Reserve Bank handling the item for any loss or expense sustained (including attorneys' fees and expenses of litigation) resulting from the Reserve Bank's action in returning the item, or in reversing a debit or credit previously made in settlement for the item. A Reserve Bank shall not have or assume any responsibility for determining whether the action taken by a recipient was timely.

§ 210.83 Return of Funds

(a) A Reserve Bank that receives a returned item in accordance with section 210.82 of this subpart shall reverse the debit and credit previously made in settlement of the item.

(b) A Reserve Bank that does not receive actually and finally collected funds in settlement of a debit item in accordance with section 210.79 of this subpart, shall, at or before the opening of business on the banking day following the settlement date, reverse the debit and credit previously made in settlement of the item, whether or not the item is available for return. The Reserve Bank shall promptly notify the originator and the recipient, or their Reserve Banks, of the reversal.

§ 210.84 Extension of Time Limits

If, because of circumstances beyond its control, an originator, recipient, or Reserve Bank is delayed in acting on an item beyond applicable time limits, the time for acting is extended for the time necessary to complete the action, if the originator, recipient, or Reserve Bank exercises such diligence as the circumstances require.

§ 210.85 Reserve Bank Liability

(a) Limitations on liability. A Reserve Bank shall be responsible or liable only to an originator, a recipient, a customer, or another Reserve Bank, and only for its own lack of good faith or failure to exercise ordinary care. A Reserve Bank shall not act as the agent or subagent of another bank or person and shall not be liable for the insolvency, neglect, misconduct, mistake, or default of another bank or person or for the loss or destruction of an item in transit or in the possession of others. A Reserve Bank shall not make or be deemed to make any warranty with respect to an item it handles under this Subpart.

(b) Measure of damages. The measure of damages for a Reserve Bank's failure to exercise ordinary care in handling an item is the amount of the item reduced by an amount that could not have been realized by the use of ordinary care. Where there is bad faith, the measure of damages includes other damages, if any, suffered by the party as a proximate consequence.

(c) Reliance on routing designation appearing on item. A Reserve Bank may handle an item based on the routing number or other designation of a recipient appearing in any form on the item when the Reserve Bank receives it. A Reserve Bank shall not be responsible for any delay resulting from its acting on a designation, whether or not the designation is consistent with any other designation appearing on the item.

(d) Right to indemnity. A Reserve Bank shall indemnify another Reserve Bank that handles an item for any loss or expense sustained (including attorneys' fees and expenses of litigation) as a result of the former Reserve Bank's failure to exercise ordinary care or to act in good faith in an interoffice transaction.

(e) Limitation on claims. No claim may be made by any person against a Reserve Bank for loss resulting from the Reserve Bank's handling of an item after one year from the settlement date of the item.

(f) Recovery by Reserve Bank. If an action or proceeding is brought against a Reserve Bank that has handled an item, based on:

- (1) the alleged breach of, or the alleged failure to have the authority to make, any of the warranties, representations, authorizations and agreements referred to in sections 210.74, 210.75, 210.82, or 210.85 of this subpart, by the originator, the recipient or another Reserve Bank; or
- (2) any action by the Reserve Bank in accordance with this subpart and its operating circulars,

the Reserve Bank may, upon the entry of a final judgment or decree, recover from the originator, the recipient or the other Reserve Bank, as the case may be, any amount the Reserve Bank is required to pay under the judgment or decree, together with interest, as well as the amount of attorneys' fees and other expenses of litigation incurred.

(g) Methods of recovery. The Reserve Bank may recover the amount stated in paragraph (f) of this section by charging the originator's or recipient's account (or if the item was received from or sent to another Reserve Bank, by charging the other Reserve Bank through the Inter-District Settlement Fund), if

- (1) the Reserve Bank has made reasonable written demand on the originator, recipient, or other Reserve Bank to assume defense of the action or proceeding; and
- (2) no other arrangement for payment acceptable to the Reserve Bank has been made.

A Reserve Bank that has been charged through the Inter-District Settlement Fund may recover from the originator or recipient in the manner and under the circumstances set forth in this paragraph. A Reserve Bank's failure to avail itself of the remedy provided in this paragraph does not prejudice its enforcement in any other manner of the indemnity agreements referred to in sections 210.74, 210.75, 210.82, and 210.85.

By order of the Board of Governors of the Federal Reserve System, November 26, 1979.

Theodore E. Allison
Secretary of the Board