FEDERAL RESERVE BANK
OF DALLAS

WILLIAM H. WALLACE
FIRST VICE PRESIDENT
AND CHIEF OPERATING OFFICER

DALLAS, TEXAS 75222

October 29, 1990

Circular 90-74

TO: The Chief Operating Officer of
each financial institution in the
Eleventh Federal Reserve District

SUBJECT

**Board Requirement that Reserve Banks Provide
Fedwire Notice to Offline Institutions**

DETAILS

The Federal Reserve Board of Governors has adopted a requirement that Reserve Banks notify by telephone all financial institutions that do not have electronic access to Fedwire ("offline institutions") of the receipt of incoming Fedwire third-party funds transfers. Also included in the notification requirement are non-value messages that are related to a transfer of funds and settlement transfers if the offline receiving institution has notified the Reserve Bank that it acts on behalf of a respondent institution.

In addition to the basic transfer fee (currently $.50), a surcharge per transfer (currently $4.00) will be assessed to the offline receiving institution for each transfer for which the Reserve Bank attempted to provide telephone notice.

Same-day telephone notice of incoming funds transfers to offline institutions will promote efficiency in the payments mechanism by providing timely information, thereby permitting prompt crediting of funds to the accounts of beneficiaries.

This requirement will become effective January 1, 1991.

ATTACHMENT

The text of the Board's press release announcing the requirement is attached.

MORE INFORMATION

For more information about the new transfer-of-funds notification requirement, please contact the persons listed below at the Dallas Office.

Jonnie Miller	(214) 651-6290 or	(800)-333-6640, ext. 6290
Vinton Myers	(214) 698-4349 or	(800)-333-6640, ext. 4349
Larry Ripley	(214) 651-6118 or	(800)-333-6640, ext. 6118

Sincerely yours,

William H Wallace

FEDERAL RESERVE SYSTEM
[Docket R-0690]
Federal Reserve Bank Services

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final Action.

SUMMARY: The Board is adopting a requirement that Reserve Banks notify by telephone all depository institutions that do not have electronic access to Fedwire ("off-line banks") of the receipt of incoming Fedwire third-party funds transfers, including non-value messages that are related to a transfer of funds. Notice will also be provided for settlement transfers and related non-value messages, if the off-line receiving bank has notified its Reserve Bank that it acts on behalf of a respondent institution. In addition to the basic transfer fee (currently $.50), a surcharge per transfer (currently $4.00) will be assessed to the off-line receiving bank for each transfer for which the Reserve Bank attempted to provide telephone notice. Same-day telephone notice of incoming funds transfers to off-line banks will promote efficiency in the payments mechanism by providing timely information, which permits prompt crediting of funds to the accounts of beneficiaries.

EFFECTIVE DATE: January 1, 1991.

FOR FURTHER INFORMATION CONTACT: Louise L. Roseman, Assistant Director (202/452-3874), Julius Oreska, Manager (202/452-3878); Christine G. Slater, Senior Financial Services Analyst (202/452-2539), or Sandra Scales, Financial Services Analyst (202/452-2728), Division of Federal Reserve Bank Operations; for

the hearing impaired only: Telecommunications Device for the Deaf, Earnestine Hill or Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION:

Parties to Fedwire funds transfers expect the completion of payments on the same day that the transfers are initiated. Fedwire participants with electronic access to the Reserve Banks receive timely electronic notice of all incoming funds transfers. Off-line banks, however, do not have an electronic connection with the Federal Reserve and are not necessarily notified on the day of the transfer. Without same-day notification, the off-line receiving bank would be unable to credit the account of its customer on the transfer date. Approximately forty-five percent of institutions using Fedwire currently receive funds transfers off-line, although off-line transfers account for less than one percent of total Fedwire volume.

The Federal Reserve currently offers two optional services by which Reserve Banks provide same-day telephone notice to off-line receivers of incoming funds transfers. Under the "standing order" service, the off-line receiving bank requests the telephone notice and pays a surcharge in addition to the basic transfer fee for telephone notice of each incoming funds transfer. The "immediate advice" (type code 12) service enables the sender of the funds transfer to request that the Reserve Bank notify by telephone the off-line receiving bank of a particular funds transfer upon receipt. The sending bank selects specific transfers that should receive telephone notice and pays the surcharge for each transfer selected.

These optional services, by providing the off-line banks prompt notice of incoming funds transfers, enable the banks to make funds available to their customers on a timely basis and better manage their own reserve positions. All off-line banks receive paper advices of credit of Fedwire transfers, which are delivered by courier or mail with the daily account statements. Courier delivery occurs on the next business day; mail delivery usually occurs one or more days after the transfer. The paper advice of credit is the only means of notifying off-line banks of incoming Fedwire transfers for which telephone notice is not provided.

On May 4, 1990, the Board requested public comment on a proposal to notify by telephone <u>all</u> off-line banks of the receipt of incoming third-party funds transfers (55 FR 18758; May 4, 1990).[1] Notice would also be provided for settlement transfers, if the off-line receiving bank has notified its Reserve Bank that it acts in a correspondent capacity for another bank with respect to transfers received through Fedwire.[2] The Reserve Bank would assess

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[1]"Third-party" funds transfers refer to all regular funds transfers (type code 10) regardless of whether these transfers include third-party information.

[2]Revised Subpart B of Regulation J provides that an off-line bank that does not expressly notify its Reserve Bank in writing that it maintains an account for another bank warrants to that Reserve Bank that the off-line bank does not act as an intermediary bank or a beneficiary's bank with respect to payment

(Footnote Continued)

a surcharge to the off-line bank on each transfer for which telephone notice was attempted. (The fee for telephone notice is currently $4.00 per transfer in addition to the basic transfer fee.)

Same-day telephone notice of incoming funds transfers to off-line banks would promote efficiency in the payments mechanism by providing timely information, which permits prompt crediting of funds to the accounts of beneficiaries. Both the recently developed Article 4A of the Uniform Commercial Code and the Expedited Funds Availability Act (12 U.S.C. 4001-4010) encourage prompt funds availability and timely notification to receiving institutions and ultimate beneficiaries.

Under Section 4A-302 of Article 4A, a Reserve Bank would be required to execute funds transfers by means reasonably necessary to allow payment to the beneficiary on the payment date or as soon thereafter as is feasible. If a Reserve Bank executes a transfer in a manner that results in a delay in the payment to the beneficiary, the Reserve Bank would be liable for interest to either the originator or the beneficiary under Section 4A-305(a) of Article 4A. The official comments to Section 4A-305 indicate that a bank that delays the execution of a transfer would generally back-value the credit to the beneficiary's bank to compensate for the delay. This is consistent with current Reserve Bank practice,

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(Footnote Continued)
orders received through Fedwire for a beneficiary that is a bank. [See Section 210.29(b).]

because the Reserve Bank credits the receiving bank on the day of the transfer, even if an off-line bank does not receive notice of the transfer until one or more days later. The off-line receiving bank that credits its beneficiary on a day following the transfer day should similarly be compensating its customer by paying interest on the transfer amount for the period of the delay. Notification to receiving banks on the transfer day would permit them to credit their customer's account on that day, and not have to pay compensation to their customers; this would be consistent with Article 4A's objective to ensure timely payment to the beneficiary.

Regulation CC (12 CFR Part 229) requires that depository institutions make the proceeds of funds transfers available to their customers at the start of the business day following the day the depository institution receives the transfer. Section 229.10(b) of Regulation CC defines receipt of an electronic payment as occurring when the bank receives both the payment in finally collected funds and the payment instructions. Therefore, same-day notification of funds transfers would be consistent with the purpose of the Expedited Funds Availability Act to ensure prompt availability of funds.

The Board received 34 comments in response to its proposal to require telephone notice to off-line banks of incoming Fedwire funds transfers. The following table reflects comments by category of respondent:

Commercial banks and bank holding companies	25
Savings and loan associations	1
Credit unions	1
Trade associations	4
Federal Reserve Banks	3

Eight commenters are off-line Fedwire participants; 18 depository institution commenters have on-line access to Fedwire; and one depository institution commenter is not a direct Fedwire participant, but occasionally uses a correspondent bank for funds transfers.

All but one of the commenters supported the proposal. Supporting commenters noted that adoption of the proposal would improve the efficiency of the payments mechanism, ensure compliance with the provisions of Article 4A and Regulation CC, and equitably allocate the costs to the party that benefits from the service. The dissenting commenter argued that off-line banks should not have to pay for telephone notice of incoming funds transfers.

Twenty-one commenters stated that the proposed Fedwire telephone notice service would enhance the efficiency of the payments mechanism, ensuring more timely notification of receipt of funds transfers and crediting of funds to the beneficiaries' accounts. Seven commenters indicated that the new service would improve off-line banks' settlement and reserve account monitoring capability. Eleven commenters noted that the service would facilitate compliance with the funds availability requirements of Article 4A and Regulation CC.

Commenters generally concurred with the pricing aspects of the proposal. Thirteen commenters stated that charging the off-line receiving bank rather than the sending bank for the telephone notice was an equitable allocation of the cost of providing the service.[3] These commenters noted that the off-line receiving bank would receive more timely information to use in managing its reserve position, and the bank's customers would benefit from more timely crediting of funds to their accounts. Moreover, several commenters noted that the receiving bank should pay for the telephone notice as a consequence of its decision to participate in Fedwire as an off-line bank, which directly affects its ability to receive prompt notification.

Several commenters suggested that the current fee may not fully recover the cost of providing telephone notices. The American Bankers Association, Washington, D.C., and the United States League of Savings Institutions, Chicago, Illinois, stated that the service pricing should be based on cost, including the private sector adjustment factor, and should be justified in accordance with the Monetary Control Act of 1980. The Independent Bankers Association of America, Washington, D.C., and the United States League of Savings Institutions expressed concern about using service pricing as an impetus for off-line banks to establish

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[3]The telephone notice service would replace the current immediate advice service (type code 12), in which the sending bank requests and pays for the telephone notice of a Fedwire transfer to an off-line receiving bank. Transfers submitted as type code 12 would therefore be handled in the same manner as type code 10 transfers. The Board anticipates that the type code 12 message format would no longer be supported as of July 1, 1991.

electronic connections to Fedwire. Other commenters stated that off-line banks obtaining electronic access to Fedwire would improve the efficiency of the payments mechanism, and several commenters suggested that the Federal Reserve should use pricing incentives to achieve this objective.

The funds transfer service fees, including the fee for telephone notice, are set to recover the cost of the funds transfer service in accordance with the provisions of the Monetary Control Act and the Board's pricing principles, and are not set to provide inducements to off-line banks to acquire electronic connections to their Reserve Banks. Nevertheless, in response to the telephone notice service, some off-line banks may reassess whether off-line Fedwire service continues to best address their own and their customers' needs and may find it more cost-effective to establish electronic connections with their Reserve Bank rather than pay for telephone notices.

The Chase Manhattan Corporation, New York, New York, the American Bankers Association, and the Independent Bankers Association of America were concerned that an off-line bank would be charged for an attempted telephone notice, even if the Reserve Bank was not successful in contacting the receiving bank. Under the telephone notice service, the Reserve Bank would make several attempts to notify an off-line bank. If an off-line bank cannot be reached on the date of the transfer, then the Reserve Bank staff would attempt to notify the off-line bank soon after the bank opens for business on the next business day. Reserve Banks will charge off-line banks for each transfer requiring telephone notice, even if the notification attempts were unsuccessful, because the Reserve Banks would incur the costs of repeatedly trying to reach the off-line banks.

The United States League of Savings Institutions suggested that the Reserve Banks should accumulate transfers and notify the off-line banks only two or three times per day and charge on the basis of each notification call. The Board believes that notifying off-line banks at predetermined intervals would result in less timely notice and would diminish the benefits of telephone notice. Also, the cost a Reserve Bank incurs to provide telephone notice of incoming transfers varies in proportion to the amount of information provided, that is, with the number of transfers received. Therefore, off-line banks will be notified promptly after receipt of each Fedwire message and charged on the basis of each message.

Several commenters suggested other modifications to the proposed service. Bankers Trust Company, New York, New York, requested that telephone notice be provided for all Fedwire messages, including non-value messages.[4] The Board believes that providing prompt notice for non-value Fedwire messages, which are often time-critical, would promote efficiency in the payments

[4]Non-value Fedwire messages refer to Fedwire messages designated as subtype 01 (request for reversal), 07 (request for reversal of prior day transfer), 31 (request for credit transfer), 33 (refusal of request for funds), or 90 (service message).

mechanism. Therefore, telephone notice will be provided for these messages.

Twelve commenters stated that the Board should require Fedwire participants to be electronically linked to a Reserve Bank for funds transfer service. These commenters stated that the Board should set a sunset date by which all participants would be required to have electronic access to Fedwire. The Reserve Banks have developed and currently offer banks an intelligent terminal software product, known as FLASH-Light, which enables the Reserve Banks to transmit ACH output data electronically in a print-display format to low-volume receiving banks. To facilitate inexpensive, electronic access for Fedwire notices, the Board anticipates that the Reserve Banks will enhance the FLASH-Light product to provide Fedwire notices and will begin offering this capability to off-line banks during the third quarter of 1991. The Federal Reserve will continue to seek enhancements that would facilitate electronic access.

Wells Fargo Bank, San Francisco, California, noted that telephone notice of incoming Fedwire transfers presents security and operational risks. The Reserve Banks will reiterate to off-line banks the importance of calling the Reserve Bank to confirm the validity and accuracy of all Fedwire telephone notices received. The Reserve Banks will continue to evaluate possible off-line security enhancements, which may be implemented in the future.

First Chicago Corporation, Chicago, Illinois, recommended that the Reserve Banks provide an account status inquiry capability for off-line banks. Several Reserve Banks have implemented an account balance inquiry capability for their Fedwire participants, including off-line banks, and the remaining Reserve Banks are considering offering this capability.

Based on an analysis of the comments received, the Board has adopted a requirement that Reserve Banks notify by telephone all depository institutions that do not have electronic access to Fedwire of the receipt of incoming Fedwire third-party funds transfers and related non-value messages. Notice will also be provided for settlement transfers and related non-value messages, if the off-line receiving bank has notified its Reserve Bank that it may receive Fedwire transfers for credit to a respondent institution. An off-line bank that does not maintain an account for another depository institution will not be required to receive telephone notice of incoming settlement transfers, but could request such notice as an optional service. Transfers to off-line receiving banks from foreign central banks and international agencies (type code 15) will also be subject to the telephone notice service. A per transfer surcharge will be assessed to the off-line receiving bank for each transfer for which the Reserve Bank attempted to provide telephone notice.

The telephone notice service will be implemented on January 1, 1991. This fall, the Board will adopt the 1991 funds transfer fees, including the telephone notice surcharge, as part of the 1991 fee schedules for Federal Reserve priced services.

Competitive Impact Analysis. The Board believes that this action will have no adverse effect on the ability of other service providers to compete effectively with the Federal Reserve in providing similar services. Several commenters concurred with the Board's belief that implementing the telephone notice service would have no effect on the operations of the Clearing House Interbank Payments System (CHIPS), because this system does not serve off-line banks.

Correspondent institutions provide access to Fedwire to a number of small institutions, and this action generally will not affect the correspondents' relationship with their respondent institutions. The American Bankers Association and the Chase Manhattan Corporation noted that a sending bank, knowing that an off-line bank would receive telephone notice from its Reserve Bank, may bypass the off-line bank's correspondent bank and remit the funds transfer directly to the off-line bank. The Board believes that relatively few off-line banks would typically receive third-party funds transfers both directly from their Reserve Bank as well as through a designated correspondent account, and that any adverse effect on correspondent services stemming from the proposed telephone notice service would be minimal.

By order of the Board of Governors of the Federal Reserve System, September 28, 1990.

(Signed) William W. Wiles
William W. Wiles
Secretary of the Board