



FEDERAL RESERVE BANK  
OF DALLAS

TONY J. SALVAGGIO  
FIRST VICE PRESIDENT

DALLAS, TEXAS  
75265-5906

May 27, 1994

Notice 94-50

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

**SUBJECT**

**Final Rule Adopting Amendments to Subpart A  
of Regulation J (Collection of Checks  
and Wire Transfers of Funds)**

**DETAILS**

The Board of Governors of the Federal Reserve System is adopting amendments to Subpart A of Regulation J, which governs collection of checks and other items by Federal Reserve Banks. The amendments, in general, conform the warranties and various other provisions of Regulation J to recent amendments to Regulation CC or to the Uniform Commercial Code.

The amendments become effective June 6, 1994.

**ATTACHMENT**

A copy of the Board's notice as it appears on pages 22962-67, Vol. 59, No. 85, of the Federal Register dated May 4, 1994, is attached.

**MORE INFORMATION**

For more information, please contact Terry Campbell at (214) 922-6603. For additional copies of this Bank's notice, please contact the Public Affairs Department at (214) 922-5254.

Sincerely,

**FEDERAL RESERVE SYSTEM****12 CFR Part 210****[Regulation J; Docket No. R-0821]****Collection of Checks and Other Items by Federal Reserve Banks and Funds Transfers Through Fedwire****AGENCY:** Board of Governors of the Federal Reserve System.**ACTION:** Final rule.

**SUMMARY:** The Board is adopting amendments to subpart A of its Regulation J, governing collection of checks and other items by Federal Reserve Banks. The amendments, in general, conform the warranties and various other provisions of Regulation J to recent amendments to Regulation CC or to the Uniform Commercial Code.

**EFFECTIVE DATE:** June 6, 1994.

**FOR FURTHER INFORMATION CONTACT:** Oliver I. Ireland, Associate General Counsel (202/452-3625), or Stephanie Martin, Senior Attorney (202/452-3198), Legal Division; for the hearing impaired only: Telecommunications Device for the Deaf, Dorothea Thompson (202/452-3544).

**SUPPLEMENTARY INFORMATION:** Subpart A of the Board's Regulation J (12 CFR part 210) governs the collection of checks and other items by Federal Reserve Banks. Regulation J sets out the warranties made by institutions that send items for collection through the Federal Reserve System as well as warranties made by Reserve Banks.<sup>1</sup> Regulation J also covers liability for breach of warranty, presentment of and settlement for cash items and returned checks, and other related issues.

In October 1992, the Board published amendments to its Regulation CC (12 CFR part 229) that require paying banks to make same-day settlement for certain checks presented by private-sector banks, effective January 3, 1994 (57 FR 46956, October 14, 1992). As part of

these amendments, the Board revised the Regulation CC warranties to require private-sector collecting, returning, and presenting banks to warrant the accuracy of cash letter totals and check encoding. In December 1993, the Board published proposed amendments to Regulation J to clarify that the Reserve Banks and institutions that send items to Reserve Banks also make the Regulation CC warranties, to conform certain Regulation J provisions to the 1990 version of the Uniform Commercial Code (U.C.C.), and to make other minor changes (58 FR 68566, December 28, 1993). The Board received 10 comments on the proposed amendments, which are discussed in the section-by-section analysis below.

The Board has established procedures for assessing the competitive impact of changes that have a substantial effect on payments system participants.<sup>2</sup> Under these procedures, the Board assesses whether the proposed regulatory changes would have a direct and material adverse effect on the ability of other service providers to compete effectively with the Federal Reserve Banks in providing similar services due to differing legal powers or constraints or due to a dominant market position of the Federal Reserve deriving from such legal differences. The Regulation J amendments are largely technical, clarifying, or conform Regulation J to the rules applicable to private-sector banks under Regulation CC and the U.C.C. The Board believes that the amendments would not have a direct and material adverse effect on the ability of others to compete effectively with the Federal Reserve Banks.

**Section-by-Section Analysis****Section 210.1**

This section sets forth the authority, purpose, and scope of subpart A of Regulation J. At the suggestion of one commenter, the Board is updating the authority citations in this section to conform with the authority citations in the CFR. Specifically, the Board has added a citation to section 11(j) of the Federal Reserve Act, which authorizes the Board to exercise general supervision over the Reserve Banks.

**Section 210.2(g)**

The Board proposed to amend the definition of "item" in keeping with the definition of "item" in U.C.C. § 4-104(a)(9). Under the amended language, "item" would expressly include promises or orders, such as certain

bonds or other investment securities, that are handled through the bank collection system. The Board received no comments on this section and has adopted the amendment as proposed.

**Section 210.2(p)**

The Board proposed to add a definition of "Uniform Commercial Code" that conforms to the definition in Regulation CC (12 CFR 229.2(ii)). The Board received no comments on this section and has adopted the amendment as proposed.

**Section 210.3(a)**

The Board proposed to amend this section to set forth more accurately the scope of the Federal Reserve Banks' operating circulars, which include provisions for service terms and adjustments. The amendment specifies that the operating circulars may include provisions for adjustments of amounts, waiver of expenses, and payment of interest by as-of adjustment.

One commenter believed that the proposed change, at least as it relates to Reserve Bank adjustment practices, impedes the ability of correspondent banks to compete with the Reserve Banks. This commenter stated that the adjustment accounting practices of its local Reserve Bank require intercept processors and depository institutions to engage in a burdensome reconciliation process. The commenter stated that the Board should not incorporate the operating circulars into Regulation J.

The proposed amendments, however, would not incorporate the operating circulars into Regulation J, but rather would provide greater detail as to the scope of the operating circulars. Issues related to adjustment posting alternatives generally can be settled between the Reserve Bank and the parties involved and would not be affected by the proposed amendment to Regulation J. Thus, the Board has adopted the amendment as proposed.

**Section 210.3(f)**

The Board proposed to add a new paragraph to § 210.3 to clarify that Regulation J supersedes the U.C.C., other state laws, and Regulation CC to the extent of any inconsistency. This provision parallels § 229.41 of Regulation CC, which provides that Regulation CC supersedes the U.C.C. and other state law to the extent of the inconsistency. The Board received no comments on this section and has adopted the amendment as proposed.

<sup>1</sup> As used in this docket, sender means any institution that sends a check to a Reserve Bank for collection, and bank includes all depository institutions, such as commercial banks, savings institutions, and credit unions.

<sup>2</sup> These procedures are described in the Board's policy statement "The Federal Reserve in the Payments System" (55 FR 11648, March 29, 1990).

**Section 210.5(a)**

The Board proposed to amend § 210.5(a) to conform the warranties made by banks that send items to Reserve Banks to the transfer and presentment warranties in U.C.C. 4-207 and 4-208. A sender would warrant that it was (or acted on behalf of a person who was) entitled to enforce the item. The U.C.C. substituted the concept of "person entitled to enforce" for "person with good title" in recognition that the right to enforce an instrument is not limited to holders. In addition, the proposed amendment would require the sender to warrant that the item was not altered, dropping the adverb "materially." The U.C.C. formerly incorporated the concept of a "material" alteration as one that changed the contract of the parties in any respect. The revised U.C.C. refers to such a change simply as an alteration. Finally, the proposed amendment would clarify that the sender also makes the warranties set forth in Regulation CC and that the Regulation J warranties may not be disclaimed and are made regardless of whether the sender's indorsement appears on the item.

One commenter was concerned that dropping the word "materially" would mean that repair of MICR encoding on a check that rejects from automated processing would constitute an alteration. Section 3-407 of the U.C.C. defines "alteration" as an unauthorized change that purports to modify the obligation of a party or an unauthorized addition of words or numbers or other change to an incomplete instrument relating to the obligation of a party. The 1990 version of the U.C.C. appears to use the terms "alteration" synonymously with the former term "material alteration" (see Official Comment (1) to U.C.C. 3-407). MICR repair, which is intended to facilitate check collection and not to affect the obligations of the parties to a check, is unlikely to be considered an alteration.

**Sections 210.5(d) and 210.12(i)**

The Board proposed to add new paragraph (d) to § 210.5 and new paragraph (i) to § 210.12 to give a Reserve Bank a security interest in a sender's or prior collecting or returning bank's assets held by the Reserve Bank. The security interest would attach when a warranty is breached or other obligation is incurred. The proposed provisions were based on similar provisions in subpart B of Regulation J, which gives a Reserve Bank a security interest in the assets of a sender of a payment order to secure overdrafts and

other obligations (§ 210.28(b) (3) and (4)).

Two commenters were concerned that the proposal would give Reserve Banks greater rights than private-sector banks to resolve warranty breach issues. One of the commenters stated that the proposal appeared to give Reserve Banks a complete self-remedy for breaches absent a court order or agreement of the parties. The commenter noted that security interests under § 210.28 are designed to secure overdrafts, which are easily determinable, as opposed to warranty breaches, which are often a matter of dispute. The commenter requested that the proposal be clarified to provide that security interests do not attach and a Reserve Bank may not set off or realize upon collateral without a judicial determination or agreement of the parties.

Section 9-501(5) of the U.C.C. provides that when a claim of a secured party is reduced to judgment, the secured party's lien on collateral relates back to the date the security interest was perfected. Accordingly, the Board believes that a Reserve Bank's security interest in the assets of a warranting bank should attach on the date the warranty is breached (generally the date the Reserve Bank handles the check in question) so that the Reserve Bank may take actions to protect its collateral, if necessary, as discussed below.

The Monetary Control Act of 1980 (12 U.S.C. 248a) directed the Board and the Reserve Banks to establish and set prices for services with due consideration to ensuring an adequate level of services nationwide. In keeping with this directive, the Board expects that Reserve Banks will provide check collection services to financially troubled banks that cannot obtain services elsewhere. If a troubled bank fails, the Reserve Bank may be liable on warranty claims that it cannot pass back to the failed bank. Accordingly, the Board believes that it is appropriate to provide some protection to the Reserve Banks from pending insolvencies. Thus, the Board has adopted the proposed security interest provisions, with modifications.

The modifications to §§ 229.5(d) and 229.12(i) clarify when a default occurs. Specifically, a Reserve Bank's rights to take any action under those sections will apply only: (1) If the Reserve Bank, in its sole discretion, deems itself insecure and gives notice thereof to the sender or (2) at the time the sender suspends payments and is closed. The Board believes that requiring the Reserve Bank to advise a bank of its concerns about the bank's solvency will

prevent the routine use of set-off or other actions on collateral by Reserve Banks. The Board believes that private-sector banks often reserve the right under security agreements to take steps, such as placing a hold on collateral, to protect themselves in cases where the banks consider themselves insecure.

Under the final rule, when a Reserve Bank receives notice of a warranty claim based on alleged forged indorsement or alteration, it would pass the notice back to the bank from which it received the check. The Reserve Bank would not, however, unilaterally pass judgment on such a claim. Rather, the Reserve Banks' uniform operating circulars provide that they will process adjustments for these types of warranty claims only with the agreement of the prior collecting bank. If such agreement is not forthcoming, the Reserve Bank would wait to be sued on the warranty claim and would tender defense of the suit to the prior collecting bank under §§ 210.5 (b) and (c) and 210.12 (e) and (f) of Regulation J. Entries would be made or collateral disposed of only after judgment as provided in those sections. The amendments to §§ 229.5(d) and 229.12(i), however, would not require a sender bank to fail or a Reserve Bank to deem itself insecure before the Reserve Bank could make credit or debit adjustments to reserve or clearing accounts in accordance with adjustment procedures established in Reserve Bank operating circulars.

**Section 210.6(b)**

The Board proposed to amend § 210.6(b) to conform the Reserve Bank warranties to the transfer and presentment warranties in U.C.C. 4-207 and 4-208. (See discussion of § 210.5(a).) The amendment clarifies that the Reserve Banks make the warranties set out in § 229.34 of Regulation CC. The Board received no comments on this section and has adopted the amendment as proposed.

**Section 210.6(c)**

Section 210.6(c) provides a 2-year statute of limitations for claims against Reserve Banks for lack of good faith or failure to exercise ordinary care under Regulation J. The Board proposed to amend this section to clarify that the Regulation CC limitation period of one year would apply to any claims against a Reserve Bank under Regulation CC, such as breach of a warranty under § 229.34 or lack of good faith or failure to exercise ordinary care under § 229.38. This amendment clarifies that claims against Reserve Banks for Regulation CC violations are subject to the same time



limitations as those against private-sector banks.

The Board received three comments on this section. Two commenters believed that limitation period for breach of Regulation CC warranties should be two years rather than one year. One of these commenters often receives adjustment requests from the IRS one to two years after the fact and does not wish to be precluded from pursuing such adjustments with a Reserve Bank. This commenter suggested that the Regulation CC limitation period be extended to 2 years. Another commenter noted that, if the one year limitation period is adopted, it should run from the date of the last entry for the check in question rather than from the date the check first cleared.

The Board believes that the same limitation period should apply to Reserve Banks and private-sector banks for Regulation CC violations. As Regulation CC provides a one-year statute of limitations, the Board does not believe Regulation J should lengthen this period for Reserve Banks and has adopted the proposed amendment. The one-year period was established in subpart C of Regulation CC to match the one-year limitation period for subpart B (funds availability) violations, which was set by statute. As provided in Regulation CC § 229.38(g), an action must be brought within one year after the date of the occurrence of the violation involved.

#### Section 210.9(a)(5)

Section 210.9(a)(5) provides that paying banks must settle for checks presented by Reserve Banks by "autocharge" (i.e. a debit to an account at a Reserve Bank), cash, or other means agreed to by the Reserve Bank. The Board proposed to amend this section to clarify that a Reserve Bank may, in its discretion, elect to obtain settlement by autocharging the account of the paying bank for the amount of a cash letter. Virtually all Reserve Bank presentments are settled via autocharge. This amendment would restate the autocharge provisions that currently are set out in the Reserve Banks' uniform cash item operating circular.

The Board also proposed to amend this section to provide that paying banks that receive presentment from Reserve Banks may not set off other claims against the amount of settlement owed to the Reserve Bank. Paying banks may set off against private-sector presenting banks under § 229.34(c)(4) of Regulation CC. The Regulation CC set-off provision was designed to protect paying banks under the same-day settlement rule,

which requires paying banks to accept presentment from and settle with all presenting banks, some of which may be in poor financial condition. If a paying bank overpays a cash letter in reliance on a cash letter total or check encoding warranted by the presenting bank, it could face the risk that the presenting bank would be unable to settle for adjustments. Protection against insolvency risk would not be necessary against a Reserve Bank. In addition, as banks generally settle with Reserve Banks via autocharge, set-off against a Reserve Bank would be impractical. Therefore, the Board does not believe this amendment would have a direct and material adverse effect on the ability of private-sector banks to compete effectively with Reserve Banks.

The Board received no comments on this section and has adopted the amendments as proposed.

#### Section 210.12(a)

Section 210.12(a) provides that a paying bank that has settled for a check presented by a Reserve Bank may return the check in accordance with Regulation CC, the U.C.C., and the Reserve Bank's operating circular. The Board proposed to amend this section to clarify that the paying bank may also return a check prior to settlement in accordance with § 210.9(a) of Regulation J and the Reserve Bank's operating circular. This amendment would clarify that a paying bank would have the same return rights under Regulation J as under Regulation CC and the U.C.C. The Board received no comments on this section and has adopted the amendment as proposed.

#### Section 210.12(c)

Section 210.12(c) sets out the warranties and agreements made by a bank that sends a returned check to a Reserve Bank. The Board proposed to amend this section to clarify that, in addition to the warranties set forth in § 229.34 of Regulation CC, the sender also makes any applicable warranty under state law. For example, the amendment would clarify that a depository bank that settled for a returned check could recover the amount paid plus expenses and lost interest from a prior bank that breached a transfer warranty, in accordance with U.C.C. 4-208(d). In addition, similar to the amendments to § 210.5(a), the proposed revisions to this paragraph would clarify that the Regulation J warranties may not be disclaimed and are made regardless of whether the sender's indorsement appears on the item. These amendments restate provisions that are already applicable to private-sector banks under Regulation

CC and the U.C.C. The Board received no comments on this section and has adopted the amendments as proposed.

#### Section 210.12(d)

The Board proposed to add a new paragraph (d) to § 210.12 to clarify that when a Reserve Bank transfers and receives settlement for a returned check, it makes the warranties set out in § 229.34 of Regulation CC. In addition, the new paragraph would parallel revised § 210.6(b) (governing Reserve Bank warranties for cash items) by providing a limitation of the Reserve Bank's liabilities, other than those allowed for in Regulation J, to the Reserve Bank's own lack of good faith or failure to exercise ordinary care. (The amendments redesignate current §§ 210.12(d) through (g) as §§ 210.12(e) through (h).) The Board received no comments on this section and has adopted the amendments as proposed.

#### Section 210.12(e) (Formerly 210.12(d)) and Section 210.5(b)

The U.C.C. (3-119) and Regulation CC (§ 229.34(e)) provide that a bank that receives a tender of defense may in turn tender defense to a prior bank in the collection or return chain. Unless the prior bank comes in and defends, it is bound by the determination of fact common to the current litigation and any subsequent litigation.

Section 210.5(b) of Regulation J provides that, when a Reserve Bank tenders defense to a sender as a result of a tender to it, the Reserve Bank need not be a defendant in the suit in order to recover from the sender any losses that it incurs because of the judgment, so long as the judgment addresses the fact issue of breach of warranty. The Board adopted this provision in 1986 in order to reduce litigation and provide a more efficient way of handling forged indorsement cases (51 FR 21740, June 16, 1986). Due to an oversight, when the Board amended § 210.12 to provide a similar rule for returned checks, the language did not match that of § 210.5(b) and could have been interpreted to apply only when a Reserve Bank is a defendant (53 FR 21983, June 13, 1988). The Board proposed to amend § 210.12(e) to conform it to § 210.5(b). (The amendments redesignate current § 210.12(d) as § 210.12(e) and add a new paragraph (d) as discussed above.) The Board also proposed to correct a typographical error in § 210.5(b). The Board received no comments on this section and has adopted the amendments as proposed.

**Section 210.12(h) (Formerly 210.12(g))**

This section provides that a depository bank must settle for returned checks received from a Reserve Bank in the same manner as it settles for cash items presented by the Reserve Bank. The Board proposed to amend this section to clarify that settlement for returned checks also must be made by the same time as settlement for cash items, as provided in § 210.9(a). The Board received no comments on this section and has adopted the amendment as proposed.

**Section 210.13(a)**

Section 210.13(a) authorizes a Reserve Bank that does not receive payment for an item to charge back the account of the sender, paying bank, or returning bank from which the item was received. The Board proposed to amend this section to clarify that a Reserve Bank also may charge the account of a prior collecting bank through which the item was received. This amendment is consistent with § 229.35(b) of Regulation CC, which allows a bank that handles a check or returned check to recover from any prior indorser in the event that the bank does not receive payment for the check from a subsequent bank in the collection or return chain. In the event of such a recovery by a Reserve Bank, § 229.13(a) provides that no bank or person in the forward collection or return chain would have an interest in any funds in the Reserve Bank's possession of the bank that failed to pay. The amendment would clarify that, when a Reserve Bank charges back an item, this limitation of interest applies only when a bank or person seeks payment of the amount of the item out of funds or property held by the Reserve Bank. The Board received no comments on this section and has adopted the amendment as proposed.

**Section 210.13(b)**

Section 210.13(b) provides that a Reserve Bank will not debit an institution's reserve account for drafts or other orders on the account after receiving notice that the institution has been closed. The Board proposed to amend this section to clarify that Reserve Banks will not charge an account as authorized by § 210.9(a)(5) after receiving notice the institution is closed. The amendment also would clarify that this section applies only to charges to reserve accounts to settle for items (including returned checks) and does not affect the Reserve Bank's security interest under proposed §§ 210.5(d) and 210.12(i). The Board

received no comments on this section and has adopted the amendments as proposed.

**Section 210.14**

Section 210.14 describes those circumstances under which the time limits for acting on an item may be extended, such as interruption of communication facilities, suspension of payments by a bank, and other emergency conditions. The Board proposed to amend this section to clarify that computer and equipment failure would constitute emergency conditions. This amendment is consistent with the emergency provisions in § 229.38(e) of Regulation CC and U.C.C. 4-109(b). The Board received no comments on this section and has adopted the amendment as proposed.

**Final Regulatory Flexibility 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. The amendments apply to all depository institutions that receive items from or send items to Federal Reserve Banks, regardless of size. The amendments generally clarify rights and duties of banks and do not impose any substantial economic burden on small entities.

**List of Subjects in 12 CFR Part 210**

Banks, Banking, Check collection.

For the reasons set out in the preamble, 12 CFR part 210 is amended as follows:

**PART 210—COLLECTION OF CHECKS AND OTHER ITEMS BY FEDERAL RESERVE BANKS AND FUNDS TRANSFERS THROUGH FEDWIRE (REGULATION J)**

1. The authority citation for part 210 is revised to read as follows:

**Authority:** 12 U.S.C. 248 (i), (j), and (o), 342, 360, 464, and 4001-4010.

2. The first sentence of § 210.1 is revised to read as follows:

**§ 210.1 Authority, purpose, and scope.**

The Board of Governors of the Federal Reserve System (Board) has issued this subpart pursuant to the Federal Reserve Act, sections 11 (i) and (j) (12 U.S.C. 248 (i) and (j)), section 13 (12 U.S.C. 342), section 16 (12 U.S.C. 248(o) and 360), and section 19(f) (12 U.S.C. 464); the Expedited Funds Availability Act (12 U.S.C. 4001 *et seq.*); and other laws.

\* \* \*

3. In § 210.2, paragraph (g) introductory text is revised and a new paragraph (p) is added immediately before the concluding text to read as follows:

**§ 210.2 Definitions.**

\* \* \*

(g) *Item* means an instrument or a promise or order to pay money, whether negotiable or not, that is:

\* \* \*

(p) *Uniform Commercial Code* means the Uniform Commercial Code as adopted in a state.

\* \* \*

4. In § 210.3, the last sentence of paragraph (a) is revised and a new paragraph (f) is added to read as follows:

**§ 210.3 General provisions.**

(a) \* \* \* The circulars may, among other things, classify cash items and noncash items, require separate sorts and letters, provide different closing times for the receipt of different classes or types of items, set forth terms of services, and establish procedures for adjustments on a Reserve Bank's books, including amounts, waiver of expenses, and payment of interest by as-of adjustment.

\* \* \*

(f) *Relation to other law.* The provisions of this subpart supersede any inconsistent provisions of the Uniform Commercial Code, of any other state law, or of part 229 of this title, but only to the extent of the inconsistency.

5. In § 210.5, paragraph (a) introductory text and paragraph (a)(2) are revised, in paragraph (b)(3) the phrase "judgment or decree of the tender of defense" is revised to read "judgment or decree or the tender of defense", and a new paragraph (d) is added to read as follows:

**§ 210.5 Sender's agreement; recovery by Reserve Bank.**

(a) *Sender's agreement.* The warranties, authorizations, and agreements made pursuant to this paragraph may not be disclaimed and are made whether or not the item bears an indorsement of the sender. By



sending an item to a Reserve Bank, the sender:

\* \* \*

(2) Warrants to each Reserve Bank handling the item that:

- (i) The sender is a person entitled to enforce the item or authorized to obtain payment of the item on behalf of a person entitled to enforce the item; and
- (ii) The item has not been altered; but this paragraph (a)(2) does not limit any warranty by a sender or other prior party arising under state law or under subpart C of part 229 of this title; and

\* \* \*

(d) *Security interest.* To secure any obligation due or to become due to a Reserve Bank by a sender or prior collecting bank under this subpart or subpart C of part 229 of this title, the sender and prior collecting bank, by sending an item directly or indirectly to the Reserve Bank, grant to the Reserve Bank a security interest in all of the sender's or prior collecting bank's assets in the possession of, or held for the account of, the Reserve Bank. The security interest attaches when a warranty is breached or any other obligation to the Reserve Bank is incurred. If the Reserve Bank, in its sole discretion, deems itself insecure and gives notice thereof to the sender or prior collecting bank, or if the sender or prior collecting bank suspends payments or is closed, the Reserve Bank may take any action authorized by law to recover the amount of an obligation, including, but not limited to, the exercise of rights of set off, the realization on any available collateral, and any other rights it may have as a creditor under applicable law.

6. In § 210.6, paragraphs (b)(1) and (b)(2) are revised, a new first sentence is added to paragraph (b) concluding text, and a new last sentence is added to paragraph (c) to read as follows:

**§ 210.6 Status, warranties, and liability of Reserve Bank.**

\* \* \*

(b) \* \* \*

(1) That the Reserve Bank is a person entitled to enforce the item (or is authorized to obtain payment of the item on behalf of a person who is either:

- (i) Entitled to enforce the item; or
- (ii) Authorized to obtain payment on behalf of a person entitled to enforce the item); and

(2) That the item has not been altered. The Reserve Bank also makes the warranties set forth in § 229.34(c) of this title, subject to the terms of part 229 of this title. \* \* \*

(c) \* \* \* This paragraph does not lengthen the time limit for claims under

§ 229.38(g) of this title (which include claims for breach of warranty under § 229.34 of this title).

7. In § 210.9, paragraph (a)(5) is revised to read as follows:

**§ 210.9 Settlement and payment.**

(a) \* \* \*

(5) Settlement with a Reserve Bank under paragraphs (a)(1) through (4) of this section shall be made by debit to an account on the Reserve Bank's books, cash, or other form of settlement to which the Reserve Bank agrees, except that the Reserve Bank may, in its discretion, obtain settlement by charging the paying bank's reserve or clearing account. A paying bank may not set off against the amount of a settlement under this section the amount of a claim with respect to another cash item, cash letter, or other claim under § 229.34(c) of this title or other law.

\* \* \*

8. In § 210.12, a new sentence is added after the first sentence of paragraph (a), paragraph (c) introductory text and paragraph (c)(2) are revised, paragraphs (d) through (g) are redesignated as paragraphs (e) through (h), respectively, new paragraphs (d) and (i) are added, and newly-designated paragraph (e) concluding text and newly-designated paragraph (h) are revised to read as follows:

**§ 210.12 Return of cash items and handling of returned checks.**

(a) \* \* \* A paying bank that receives a cash item directly or indirectly from a Reserve Bank also may return the item prior to settlement, in accordance with § 210.9(a) and its Reserve Bank's operating circular. \* \* \*

\* \* \*

(c) *Paying bank's and returning bank's agreement.* The warranties, authorizations, and agreements made pursuant to this paragraph may not be disclaimed and are made whether or not the returned check bears an indorsement of the paying bank or returning bank. By sending a returned check to a Reserve Bank, the paying bank or returning bank—

\* \* \*

(2) Makes the warranties set forth in § 229.34 of this title (but this paragraph does not limit any warranty by a paying or returning bank arising under state law); and

\* \* \*

(d) *Warranties by Reserve Bank.* By sending a returned check and receiving settlement or other consideration for it, a Reserve Bank makes the returning

bank warranties as set forth in § 229.34 of this title, subject to the terms of part 229 of this title. The Reserve Bank shall not have or assume any other liability to the transferee returning bank, to any subsequent returning bank, to the depository bank, to the owner of the check, or to any other person, except for the Reserve Bank's own lack of good faith or failure to exercise ordinary care as provided in subpart C of part 229 of this title.

(e) \* \* \*

The Reserve Bank may, upon the entry of a final judgment or decree, recover from the paying bank or returning bank the amount of attorneys' fees and other expenses of litigation incurred, as well as any amount the Reserve Bank is required to pay because of the judgment or decree or the tender of defense, together with interest thereon.

\* \* \*

(h) *Settlement.* A subsequent returning bank or depository bank shall settle for returned checks in the same manner and by the same time as for cash items presented for payment under this subpart.

(i) *Security interest.* To secure any obligation due or to become due to a Reserve Bank by a paying bank, returning bank, or prior returning bank under this subpart or subpart C of part 229 of this title, the paying bank, returning bank, and prior returning bank, by sending a returned check directly or indirectly to the Reserve Bank, grant to the Reserve Bank a security interest in all of the paying bank's, returning bank's, and prior returning bank's assets in the possession of, or held for the account of, the Reserve Bank. The security interest attaches when a warranty is breached or any other obligation to the Reserve Bank is incurred. If the Reserve Bank, in its sole discretion, deems itself insecure and gives notice thereof to the paying bank, returning bank, or prior returning bank, or if the paying bank, returning bank, or prior returning bank suspends payments or is closed, the Reserve Bank may take any action authorized by law to recover the amount of an obligation, including, but not limited to, the exercise of rights of set off, the realization on any available collateral, and any other rights it may have as a creditor under applicable law.

9. Section 210.13 is revised to read as follows:

**§ 210.13 Unpaid items.**

(a) *Right of recovery.* If a Reserve Bank does not receive payment in actually and finally collected funds for an item, the Reserve Bank shall recover by

charge-back or otherwise the amount of the item from the sender, prior collecting bank, paying bank, or returning bank from or through which it was received, whether or not the item itself can be sent back. In the event of recovery from such a party, no party, including the owner or holder of the item, shall, for the purpose of obtaining payment of the amount of the item, have any interest in any reserve balance or other funds or property in the Reserve Bank's possession of the bank that failed to make payment in actually and finally collected funds.

(b) *Suspension or closing of bank.* A Reserve Bank shall not pay or act on a draft, authorization to charge (including a charge authorized by § 210.9(a)(5)), or other order on a reserve balance or other funds in its possession for the purpose of settling for items under § 210.9 or § 210.12 after it receives notice of suspension or closing of the bank making the settlement for that bank's own or another's account.

10. Section 210.14 is revised to read as follows:

**§ 210.14 Extension of time limits.**

If a bank (including a Reserve Bank) or nonbank payor is delayed in acting on an item beyond applicable time limits because of interruption of communication or computer facilities, suspension of payments by a bank or nonbank payor, war, emergency conditions, failure of equipment, or other circumstances beyond its control, its time for acting is extended for the time necessary to complete the action, if it exercises such diligence as the circumstances require.

By order of the Board of Governors of the Federal Reserve System, April 28, 1994.

**William W. Wiles,**

*Secretary of the Board.*

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