

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 10163]
[April 16, 1987]

REDEPOSIT SERVICE FOR SMALL DISHONORED CHECKS

To All Depository Institutions, and Others Concerned,
in the Second Federal Reserve District:

Following is the text of a statement issued by the Board of Governors of the Federal Reserve System:

The Federal Reserve Board has approved a proposal to allow Federal Reserve Banks to offer a redeposit service for low-dollar checks that have been returned unpaid.

Beginning in July 1984, the Reserve Banks conducted several pilot programs to test the feasibility of reclearing low-dollar return items. The dollar cutoffs used to select the recleared checks eligible for the test programs ranged from \$100 to \$900. Based on encouraging results from the pilot programs and requests from the banking industry, in November 1986 the Board issued for public comment a proposal to adopt this program on an optional Systemwide basis.

The Reserve Banks may now offer this service to financial institutions that send checks to the Bank for collection (sender). In addition, the Reserve Banks may add other features to the basic service. For example, the sender may 1) select its own dollar cutoff for eligible returns, 2) specify eligible returns by account number rather than by having a blanket redeposit policy, or 3) designate the redeposit service for local area checks only.

If Reserve Banks opt to provide this service, they will use a two-part fee structure. The fee structure will include a fixed daily fee for reclearing items up to a specified volume level and a per item fee for any additional volume.

The Board's action also allows the Director of the Board's Division of Federal Reserve Bank Operations to approve additional service features under delegated authority.

Printed below is the text of the Board's notice in this matter, which has been reprinted from the *Federal Register* of April 3. Questions thereon may be directed to John F. Sobala, Vice President, Check Processing Function.

E. GERALD CORRIGAN,
President.

FEDERAL RESERVE SYSTEM

[Docket No. R-0582]

**Fees for Federal Reserve Bank; Check
Collection Services**

AGENCY: Board of Governors of the
Federal Reserve System.

ACTION: Notice.

SUMMARY: The Board has approved a Federal Reserve Bank redeposit service for low-dollar cash items that are returned unpaid. Reserve Banks offering the service will, if their senders so instruct, intercept low-dollar cash items being returned for insufficient or uncollected funds, and redeposit the items for collection.

EFFECTIVE DATE: March 30, 1987.

FOR FURTHER INFORMATION CONTACT: Anne M. DeBeer, Assistant Director (202/452-3879), or Gayle Thompson, Senior Analyst (202/452-2934), Division of Federal Reserve Bank Operations; or, for the hearing impaired *only*: Earnestine Hill or Dorothea Thompson, Te1ecommunication Device for the Deaf (TDD) (202/452-3544), Board of Governors of the Federal Reserve System, Washington, DC 20551.

SUPPLEMENTARY INFORMATION:

Background

On November 4, 1986, the Board issued for public comment a proposal to allow Federal Reserve Banks to offer a redeposit service for low-dollar cash

items that are being returned unpaid.¹ This proposal was initiated as a result of requests from the banking industry. Many collecting institutions routinely redeposit for collection low-dollar cash items returned to them for insufficient funds, because a large proportion of these items are paid on their second presentment. The collecting institutions find this practice to be simpler and less expensive than returning the items to their depositing customers.

In order to test the feasibility of accelerating the reclearing of certain low-dollar return items, the Federal Reserve Bank of St. Louis was authorized to conduct a pilot, which commenced in July, 1984, which was

¹ 51 FR 40516 (Nov. 7, 1986).

designed to determine what benefits could be provided to collecting institutions and the payments mechanism if Reserve Banks were to intercept and redeposit low-dollar return items on behalf of their senders.² In May, 1985, based on encouraging results from the St. Louis program, the Atlanta and Cleveland Reserve Banks were authorized to provide a similar service so that comparative data on the benefits of the return item reclearing service could be obtained.³

Results of the pilot program indicated that the reclearing service can benefit collecting institutions by reducing the costs associated with low-dollar return items and by accelerating collection times. Depositors of all sizes indicated cost savings due to the pilot, and large depositors in the St. Louis District were found to experience monthly savings of as much as \$1,000. The pilot found that between 57 and 64 per cent of the redeposited checks were collected on the second presentment.

Comments

A total of 225 public comments⁴ were received on the Board's proposal to offer a redeposit service. Of these, 176 commenters, or 78 per cent, were in favor of the proposal; 25 commenters, or 11 per cent, were opposed; and 24 (11 per cent) did not indicate whether they were for or against the proposal.

The commenters that favored the proposal indicated that the potential for reduced in-house costs and the potential

for faster payment of the redeposited items were the primary factors in their decision to support the proposal. In addition, several commenters reported that it is their current practice to redeposit low-dollar items. The experience reported by six of these commenters comports with the pilot results which show that a large percentage of unpaid items are paid on the second presentment.

Those opposing the proposal did so primarily out of a concern that a sender could incur liability if it redeposits an item without providing prompt notice of the redeposit to its depositor. The Board notes, however, that senders need not incur such liability. The redeposit service will be an option offered by Reserve Banks; any sender concerned that potential liability may outweigh the benefits of using the service need not participate.

Several commenters suggested enhancements to the service as proposed by the Board. These enhancements include allowing the sender to select its own dollar cutoff for eligible returns; allowing the sender to specify eligible returns by account number rather than requiring a blanket redeposit policy; and allowing the sender to select the redeposit service only for items payable within the local area, but not for non-local items.

Board Action

In its policy statement, "The Federal Reserve in the Payment System," 70 Fed. Res. Bull. 707 (1984), the Board established a policy that before the Federal Reserve introduces a new service or a major service enhancement, all of the following criteria must be met:

(1) The Federal Reserve must expect to achieve full recovery of costs over the long run.

(2) The Federal Reserve must expect its provision of the service to yield a clear public benefit, including, for example . . . improving the efficiency of the payment mechanism or reducing the use of real resources. . . .

(3) The service should be one that other providers alone cannot be expected to provide with reasonable effectiveness, scope, and equity. 70 Fed. Res. Bull. at 710.

Based on the comments and the continuing evidence from the pilot programs, the Board believes that the proposed low-dollar reclearing service meets all of these criteria: (1) Reserve Banks will recover all costs associated with the service. (2) The service will yield clear public benefits by improving the efficiency of the return item process and reducing the amount of real resources expended by collecting institutions in the return item process. (3) For cash items that are collected through the Federal Reserve, Reserve Banks alone can provide the service to their senders. Thus, while other collecting institutions can and do provide reclearing services for institutions that send items to them for collection, the Federal Reserve must provide this service for it to be available to institutions that choose to collect some or all of their cash items through a Reserve Bank.

Accordingly, the Board has approved the proposal to allow all Federal Reserve Banks to offer as an option to their senders a basic redeposit service for low-dollar cash items being returned unpaid for insufficient or uncollected funds. Reserve Banks offering the service will use a two-part fee structure consisting of a fixed daily fee for reclearing items up to a number of items specified by the Reserve Bank and a per item fee for any additional volume.

The Board has also approved enhancements to the basic service, including permitting the sender to choose the dollar cut-off for return items to be redeposited, allowing the sender to specify eligible return items by account number rather than requiring a blanket redeposit policy, and permitting the sender to select the redeposit service only for items payable within the local area. Reserve Bank proposals to offer these and other service enhancements will be approved by the Director of the Division of Federal Reserve Bank Operations under delegated authority from the Board.

Board of Governors of the Federal Reserve System, March 30, 1987.

William W. Wiles,
Secretary of the Board.

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² A "sender" is an entity that sends items to a Federal Reserve Bank. A sender may be a depository institution, an international organization, a foreign correspondent, a branch or agency of a foreign bank, or another Reserve Bank. 12 CFR 210.2(k). As Reserve Banks will not be reclearing items for other Reserve Banks, they will be excluded from the meaning of the term "sender" when it is used in this notice.

³ The dollar cutoff for the reclearing service is \$100 in St. Louis; items for amounts over \$100 are not eligible for the reclearing service. Atlanta and Cleveland allow the sender to choose its own dollar cutoff. Experience in Cleveland indicates that \$100 is favored by the majority of senders. In Atlanta, however, one sender elected to use a dollar cutoff of \$900.

⁴ Comments were also received from nine Federal Reserve Banks. The Reserve Banks' comments are not included in the totals discussed in this notice.